TESTIMONY OF HARRY MARKOPOLOS, CFA, CFE

CHARTERED FINANCIAL ANALYST

CERTIFIED FRAUD EXAMINER

BEFORE THE U.S. HOUSE OF REPRESENTATIVES

COMMITTEE ON FINANCIAL SERVICES

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INTRODUCTION

Good Morning. Thank you for the opportunity to testify today before this Committee on the subject of the "Madoff Ponzi Scheme." I will refer to Mr. Bernard Madoff, whose alleged fraud casts a stark light over the failures of the regulatory structures, procedures and institutions in place to prevent such crimes and is the subject of this hearing, as Madoff, BM, and Mr. Madoff interchangeably within my testimony.

You will hear me talk a great deal about over-lawyering at the SEC very soon.   Let me say I have nothing against lawyers. In fact, I have brought two of my own here with me today. On my right, I have Ms. Gaytri Kachroo, a brilliant transactional attorney and my long time general counsel for all personal and business matters. She is a partner at McCarter & English LLP (Boston), heading their international corporate practice and also represents investors and funds. On my left, counsel Phil Michael, of Troutman Sanders LLP, (NY) is a former deputy police commissioner and budget director for New York City, and now represents whistleblowers in fraud cases involving harm caused to government, and is a great strategist in such cases.

As early as May 2000, I provided evidence to the SEC's Boston Regional Office that should have caused an investigation of Madoff. I re-submitted this evidence with additional support several times between 2000 – 2008, a period of nine years. Yet nothing was done. Because nothing was done, I became fearful for the safety of my family until the SEC finally acknowledged, after Madoff had been arrested, that it had received credible evidence of Madoff's Ponzi Scheme several years earlier. There was an abject failure by the regulatory agencies we entrust as our watchdog. I hope that my testimony will provide you with further insights as to how the process failed and enable you to enact appropriate legislation that will prevent this from happening in the future. As a result of my experiences, I also have some suggestions that I would like to share with the Committee for it to consider as it develops its Congressional recommendations..

I have broken my testimony into two parts:

1) Part I will provide an overview of my contacts with the SEC between 2000 – 2008 relating solely to the Madoff case with a time line of key events during the investigation.[Timeline Color Chart].

2) Part II consists of my recommendations on fixing the SEC so that it can become an effective securities regulator for the 21st century.[Charts of SEC and NASD/FINRA from 2000-2008].

I find it difficult to compress my testimony because there were so many victims, the damages have been vast, and the scandal has ruined or harmed so many of our citizens. I feel that by writing this testimony in narrative form, the public will better understand what steps my team and I took, the order in which we took them, along with how and why we took them. The details will also afford the Committee the information necessary to ask the right questions and hopefully aid the Committee in ferreting out the truth and in restructuring the SEC which currently is non-functional and, as witnessed by the Madoff scandal, is harmful to our capital markets and harmful to our nation's reputation as a financial leader around the globe. In my testimony, wherever possible I have strived to present the mathematical concepts simply and to use word explanations instead of formulas.

Part I – My Contacts with the SEC from 2000 – 2008

Just as there is no "I" in "TEAM," I had a brave, highly trained team that greatly assisted me throughout the 9 year Madoff investigation. Let me introduce the key team members to you. Neil Chelo, Chartered Financial Analyst (CFA), Financial Risk Manager (FRM) checked every formula, math calculation, modeling technique presented to the SEC from 2000 to the present. From late 2003 to the present, as Director of Research for Benchmark Plus, a Tacoma, WA based $1 billion plus fund of funds, Mr. Chelo went out of his way to interview key marketing and high level risk managers at several Madoff feeder funds. He also obtained Greenwich Sentry audited financial statements for the year's ending 2004, 2005, and 2006. Frank Casey, a former US Army airborne ranger infantry officer with intelligence gathering experience, is the North American President for UK based Fortune Asset Management, a $5 billion hedge fund advisory firm. Mr. Casey closely tracked the Madoff's feeder funds and collected their marketing documents, figured out Madoff's cash situation. He determined that Madoff's Ponzi was unraveling in June 2005 and May 2007 and in need of additional funds to keep the scheme going, and tabulated Madoff's likely assets under management. Institutional Investor's Michael Ocrant, a brilliant investigative journalist also made key contributions to our efforts to stop Madoff. Mr. Ocrant was the only team member to actually meet Mr. Madoff in person and to step inside Mr. Madoff's operation at great personal and professional risk to himself.

These three gentlemen were my eyes and ears out in the hedge fund world, closely tracking who Madoff was dealing with, acquiring Madoff marketing literature and investigating directly with the staff of feeder funds into Mr. Madoff's fund to collect additional pieces of the puzzle. My army special operations background trained me to build intelligence networks, collect reports from field operatives, devise lists of additional questions to fill in the blanks, analyze the data, and send draft reports for review and error correction before submission to the SEC.

In order to minimize the risk of discovery of our activities and the potential threat of harm to me and to my team, I submitted reports to the SEC without signing them. My team and I surmised that if Mr. Madoff gained knowledge of our activities, he may feel threatened enough to seek to stifle us. If Mr. Madoff was already facing life in prison, there was little to no downside for him to remove any such threat. At various points throughout these nine years each of us feared for our lives. Our analysis lead us to conclude that Mr. Madoff"s fund and the secret walls around it posed great danger to those questioning and investigating them. We also concluded both the fund and the secrets that assisted its growth and development were of unimaginable size and complexity. Neither my team nor I had any personal knowledge of Mr. Madoff or his psychological make up. As such we had only the conclusions of our investigation into his fund to surmise of what he may have been capable. We did know, however, that he was one of the most powerful men on Wall Street and in a position to easily end our careers or worse.

My first submission to the SEC was coordinated through Ed Manion, CFA, a member of the Boston Regional Office with 25 years of industry experience. Mr. Manion was a former trader at the Boston Company and a portfolio manager at Fidelity serving alongside Peter Lynch. He has been with the SEC for 15 years and, in my opinion, was the only person in the Boston Regional Office with the proper industry background to comprehend fully the size, scope and danger of the Madoff Ponzi scheme. Mr. Manion is a Chartered Financial Analyst (CFA) and is highly respected in Boston's financial district and is considered the go-to person for securities fraud cases in Boston. We would call Ed "the SEC's hit-man," because when the SEC brought Ed in, people often ended up in jail via SEC criminal referrals to the DOJ. Throughout the past 9 years, Ed Manion was the only SEC staff member who ever truly understood the Madoff scheme and the threat it posed to the public. Unfortunately, as I will soon relate, my experiences with other SEC officials proved to be a systemic disappointment, and led me to conclude that the SEC securities' lawyers if only through their investigative ineptitude and financial illiteracy colluded to maintain large frauds such as the one to which Madoff later confessed. In brief, SEC securities lawyers did not want to hear from a non-lawyer SEC staffer like Mr. Manion with 25 years of trading and portfolio management experience. As much as Boston's financial community looks up to and respects Ed Manion, that's how much the SEC looked down upon and ignored Mr. Manion's repeated requests for SEC enforcement action against Mr. Madoff.

Without Mr. Manion's continued encouragement, I would have stopped the Madoff investigation after my October 2001 SEC Submission. Every time I threatened to quit the investigation, Mr. Manion would tell me I had a duty to the public to keep going no matter how badly the odds were stacked against us. I believe that the SEC would fire him if he were to testify before Congress about his role and that of the SEC during the past 9 years; but if the proper protections could be worked out in advance to safeguard his career and guarantee him another 3 years until his government retirement, I recommend that the Committee speak with him. I owe him much thanks for his dedication to the effort of sharing Mr. Madoff's alleged fraud to the appropriate authorities within the SEC.

Late 1999 – 2000

I started the Madoff investigation in late 1999 and early 2000 as a result of Frank Casey, Senior Vice-President of Marketing for Rampart Investment Management Company, Inc., telling me about the fantastic returns of one Bernard Madoff (hereafter referred to as BM). Mr. Casey told me that investors he met with in New York considered BM to be the premier hedge fund manager because of his steady return streams with unusually low volatility. This unusually low volatility was attributed to BM having very few negative months, with the largest price decline in one month a reported minus 0.55%, or barely more than half a percent. Mr. Casey and one of my employer's partners, Mr. David Fraley, asked me to replicate BM's split-strike conversion strategy so that Rampart Investment Management Company, Inc. could offer this product and compete with BM for clients.

A split-strike conversion strategy consists of 3 main parts. Part I is a basket or grouping of stocks that you purchase. Many managers will choose to purchase their stocks in index form such that the stock basket is a 100% match to the index options they plan on using as part of the strategy. Part II consists of the call options that you are selling to generate income. Part III consists of the put options that you will be buying to protect your stock portfolio from market price declines (these cost you money just like auto insurance does). Let's simplify even further, there are 3 sources of income from this strategy, stock price appreciation (i.e. the stocks go up in price), stock dividends which you receive every quarter as the stocks in your stock basket pay their quarterly dividends, and the income you receive from selling out-of-the-money call options. However, there are also 3 sources of loss with this strategy. You lose when the stocks in your stock basket decline in price and you also lose money when you purchase put options to protect your stock basket from market price declines. The third source of loss is when the OEX index rises above the strike price of your short OEX index calls.

As you can tell from reading the above, there are lots of moving parts in this strategy and it is best left to the experts. I would be happy to diagram this strategy out on a white board during testimony in an easier to understand form if you'd like. Since BM never actually used this strategy it may be a moot point.

Suffice it to say that the strategy is complex enough, with enough moving parts, that even market professionals without derivatives experience would have trouble keeping track of all the moving parts and understanding them fully. This is probably why BM settled on marketing this split-strike strategy to his victims. He knew most wouldn't understand it and would be embarrassed to admit their ignorance so he would have less questions to answer. And, with Ponzi schemes, you never ever want the victims to understand how the sausage is made, nor do you want them asking too many questions.

Mr. Casey obtained a one-page marketing document from the Broyhill All-Weather Fund, L.P. (May 2000 SEC Submission) which described the strategy, listed its monthly returns from 1993 through March 2000, and provided the background of the fund and its manager. I was told that "Manager B" was BM. The strategy and performance numbers foot with other information we collected in later years that all pointed to BM. I studied the Broyhill document and within 5 minutes suspected it was a fraud since the strategy as described was not capable of beating the typical percent return on US Treasury Bills less fees and expenses. Once fees and expenses were included, the Split-Strike Conversion Strategy as depicted in the marketing document would have had trouble beating a 0% return.

The reason I was immediately suspicious was that I had run a slightly similar, but actually functional, product that my firm called our Protected Equity Program (PEP). PEP delivered approximately 2/3rds of the market's return with only 1/3rd of the risk. To earn those types of returns we had to make a lot more good trading decisions than bad ones and sometimes our returns would greatly lag the market but then catch up later. The important point to remember is that even as good as this product was, it often lagged the market whereas BM's was always doing well under all market conditions which is, of course, impossible. However, our PEP strategy was vastly superior to BM's in that we owned the actual stock in index form with perfect replication and did not have the single stock risk included in BM's strategy. Here my expertise with the product helped me to quickly determine BM couldn't have been using a split-strike strategy as he described to earn the kind of always positive return stream that he claimed.

Let me explain this critical difference, BM said that he purchased a basket of 30 – 35 stocks that closely replicated the OEX Standard & Poor's 100 stock index. But, of course, if you are using only 30 – 35 stocks to replicate a 100 stock index you have to assume a much higher degree of risk, by taking larger position weights than are in the underlying 100 stock index. You don't get compensated with extra returns by taking this additional risk, and you should experience a performance penalty when your 30 – 35 stock basket under-performs the 100 stock index. Let's assume that BM owned 33 stocks and each stock was 3.03% of his portfolio totaling 100% of his stock portfolio (33 stocks x 3.03% invested in each stock = 100% of his stock portfolio). Now let's say that one of those stocks during the 7¼ year time period from 1993 to March 2000 put in an Enron, WorldCom or Global Crossing type of performance and went to zero. BM would be down 3.03% for that month [1/33rd= 3.03%]. The odds of a 30 - 35 stock portfolio not experiencing heavy single stock losses over a 7 ¼ time period ranged between slim and none.

Furthermore, BM's strategy required all or substantially all of the stocks in his portfolio to rise during the month, something which wasn't sustainable for 7¼ years straight without interruption. If BM had said he owned the OEX Standard & Poor's 100 stock index in its entirety, he would have passed my initial 5 minute sniff test but, fortunately for us, he was not a sophisticated enough fraudster to get his portfolio construction math correct and I suspected fraud immediately.

I then spent a couple of hours inputting BM's monthly returns into an excel spreadsheet and modeling against the S&P 500 Stock Index's monthly returns. BM made a key error in how he presented his performance because he kept comparing himself to the S&P 500 stock index when his strategy purported to replicate the S&P 100 stock index. That signaled a startling lack of sophistication on his part since there was a noticeably large difference in price returns between the two indices. This lack of sophistication on BM's part was a recurring theme during the 9 year investigation. BM's math never made sense, his performance charts were clearly deceiving, and his return stream never resembled any known financial instrument or strategy. As will be made clear in the rest of this story, to believe in BM was to believe in the impossible.

BM said he was earning 82% of the S&P 500's return with less than 22% of the risk. More alarmingly, his returns only had a 6% correlation to the S&P 500 Stock Index when I would have expected to see something like a 50% correlation and wouldn't have questioned any correlation figures between 30% - 60%. A 6% correlation was so low as to signal "FRAUD" in flashing red letters. The easiest explanation for why a 6% correlation is so low as to be wholly unbelievable is that if your returns are coming from the S&P 100 stock index, you had better at least partially resemble that stock index's performance. Having only a 6% resemblance in a situation where, due to the price limiting performance of the put and call options, one would expect a 30 – 60% correlation, was outside the bounds of rationality. The biggest, most glaring tip-off that this had to be a fraud was that BM only reported 3 down months out of 87 months whereas the S&P 500 was down 28 months during that time period. No money manager is only down 3.4% of the time. That would be equivalent to a major league baseball player batting .966 and no one suspecting that this player was cheating, and therefore fictional.

A quick glance at Exhibit 1 of my May 2000 SEC Submission next to the letter "C" shows the "Cumulative Performance of Manager B" where Manager B is BM. Note how the line goes up at nearly a perfectly rising 45 degree angle with no noticeable downturns whatsoever from 1993 thru March 2000. Now ask yourself, how can any manager's performance be that perfectly smooth and in only the up direction when markets go down as well as up? Then ask yourself what the managers of these feeder funds were thinking as they performed due diligence or even if they were thinking while they performed due diligence. Yes, BM was a "no-brainer" investment but only in the sense that you had to have no brains whatsoever to invest into such an unbelievable performance record that bears no resemblance to any other investment managers' track record throughout recorded human history.

I then assembled OEX Standard & Poor's 100 Index Option open interest and volume statistics from the Chicago Board Options Exchange (CBOE) as reported in the Wall Street Journal's Money & Investing Section. There were not enough OEX index options in existence for BM to be managing the Split-Strike Conversion Strategy he purported to be running. This test took me less than 30 minutes to complete. At this point, I was incredulous as to how any fund would willingly invest in such an obvious fraud.

In less than four hours I knew I had proved mathematically that BM was a fraud and so I then furthered my analysis and developed two alternate fraud hypotheses to explain what might be happening. *Fraud hypothesis 1* was that BM was simply a Ponzi scheme and the returns were fictional. *Fraud hypothesis 2* was that the returns were real but they were being illegally generated by front-running Madoff Securities broker/dealer order flow and the split-strike conversion strategy was a mere “front” or “cover.” Either way, BM was committing a fraud and should go to prison.

I ran some option pricing model calculations to determine how much money BM could earn by illegally front-running his stock order flow through Madoff Securities (page 4, 2000 SEC Submission) and determined that he could earn 3 – 12 cents per share for time periods of 1 – 15 minutes if he was front-running order flow. That meant returns of 30% - 60%, given the size of the assets under management we believed he had; front-running seemed like a likely possibility in 2000 and 2001. To double check my modeling techniques and calculations, I had my assistant, derivatives portfolio manager Neil Chelo, CFA and Daniel DiBartolomeo, one of the world’s most accomplished financial mathematicians, review my work. Both gentlemen concluded that either Hypothesis I or II was, in fact, correct and that BM was a fraudster. However, in 2000 and 2001 we did not have enough information on hand to determine which of the two fraud hypotheses was correct. During later time periods as Mr. Casey, Mr. Chelo, and Mr. Ocrant kept tabulating higher and higher assets under management totals, the front-running fraud hypothesis became unworkable because BM’s illegal trading activity could not have gone undetected by his firm’s brokerage customers.

I spent hours writing my eight-page 2000 SEC Submission and arranged with the Boston SEC’s Ed Manion to meet with the Boston Regional Director of Enforcement (DOE), Attorney Grant Ward in May 2000. Given Mr. Ward’s position and my understanding of his mandate, I was shocked by his financial illiteracy and inability to understand any of the concepts presented in that submission. Mr. Manion and I compared notes after the meeting and neither of us believed that the Boston Region's DOE had understood any of the information presented. Little did I know that over the next several years I would come to understand that financial illiteracy among the SEC's securities lawyers was pretty much universal with few exceptions.

2001

In 2001, the Boston SEC's Ed Manion and I spoke often of the lack of follow up to my May 2000 SEC Submission. Immediately after 9-11, Mr. Manion called me, convinced that my work had somehow fallen through the cracks and never made it to the responsible parties in the New York Regional Office. In October 2001 or thereabouts, I resubmitted my original 8-page report, wrote an additional 3 pages and included 2 pages entitled "Madoff Investment Process Explained." The New York Regional Office never contacted me after either my May 2000 or October 2001 SEC Submissions. To my mind, the mathematical analysis provided compelling proof that an investigation was required. Yet, none was conducted to my knowledge.

2002

In 2002, I continued my research into BM. I took a key trip to Europe with Access International Advisors Limited to market a Statistical Options Arbitrage Strategy that I had developed**.** During that trip I met with 14 French and Swiss private client banks and hedge fund of funds (FOF's). All bragged about how BM had closed his hedge fund to new investors but "*they had special access to Madoff and he'd accept new money from them*." It was during this trip that I knew that BM was most likely a Ponzi Scheme and that he was not front-running. If

BM was really front-running he would not want new money because additional money to invest would bring down his returns and also raise the odds of getting caught. My European trip allowed me to lower the odds that the front-running fraud hypothesis was true and focus more effort on my Ponzi scheme fraud hypothesis, which simplified the investigation. BM's masterful use of a "hook" by playing hard to get and his false lure of exclusivity were symptomatic of a Ponzi scheme. The dead give-away was BM's need for new money, another trait of Ponzi schemes, because Ponzi managers always need ever increasing amounts of new money flowing in the door to pay off old investors. I also came to realize that several European royal families were invested with BM. I met several counts and princes during my trip and it seemed they all were invested with BM or were marketing BM's strategies to noble families throughout Europe. BM had a marketing strategy that appeared to be based on false trust, not analysis.

2003 -2004

My records for 2003 & 2004 are non-existent due to my leaving my former employer at the end of August 2004 and not taking a copy of my e-mail archives with me. I am sure I worked on the case, but I don't have any supporting documentation at this time. I have a non-functioning hard drive from my old home PC which I am sending out to see if any 1999- 2004 home e-mails can be recovered that relate to this case. Unfortunately, my former employer was always on the leading edge of technology, rapidly acquiring and putting the newest, high-speed servers into service. The firm was a derivatives' management company, requiring machines that could run millions of calculations quickly. Therefore it is unlikely old e-mail records have been maintained before the mandatory 7-year e-mail retention period was enacted into law, but it can be asked for these records.

2005

In June 2005 (see page 11 of my November 7, 2005 SEC Submission) Frank Casey sent me an e-mail where I substituted "ABCDEFGH" for the name of the individual, showing that BM was attempting to borrow funds from a major European bank. This was our first inkling that BM was struggling to keep his Ponzi scheme afloat.

Fortunately, I have plenty of e-mails from the last quarter of 2005 and it was a very busy quarter for the Madoff investigation. In late October, most likely on October 25, 2005, I met with Mike Garrity, Branch Chief, of the SEC's Boston Regional Office. Mr. Ed Manion, CFA felt that Mr. Garrity was a conscientious, hard-working Branch Chief who would give me a fair and impartial hearing that might be what was needed to get this case re-submitted to the SEC's New York Office. Ed Manion scheduled an appointment for me with Mr. Garrity and I thought that perhaps the third time submitting this case would turn out to be the charm.

I met with Mr. Garrity for several hours and found him to be very patient and eager to master the details of the case. Unlike my disastrous May 2000 meeting with that office's Director of Enforcement, Attorney Grant Ward, I found Mr. Garrity to be interested and fully engaged in my telling of the scheme. Some of the derivatives math was difficult for him to understand, so I went to the white board and diagrammed out Madoff's purported strategy and its obvious failings until he understood it. A few of the more difficult concepts required repeated trips up to the white board but at the end of our meeting, it was clear that Mr. Garrity understood the scheme, it's size, and it's threat to the capital markets.

Mr. Garrity promised to follow up and he was true to his word. About a week or so later, Mike Garrity called me back telling me that he did some investigating and found some irregularities but that he couldn't tell me what they were, only that he was in contact with the New York Regional Office and wanted to put me in touch with a Branch Chief there for follow on investigation. He also said that I would have to identify myself as "the Boston Whistleblower" when I called because he wanted to protect my identity to the extent possible.

Perhaps the most impressive thing about Mr. Garrity was his willingness to think outside of the box. He was able to imagine the impossibility of Madoff's returns and understand that BM's returns were too good to be true and this obviously concerned him. He told me that if BM were located within the New England region, he would have had an inspection team inside BM's operation the very next day.

On Friday, November 4, 2005, Mr. Garrity sent me the names and contact information for Doria Bachenheimer and Meaghan Cheung. (Branch Chief). I called the latter and revealed my identity, and e-mailed her a revised 21-page report. I then e-mailed my thanks to Mike Garrity and informed him that I would be working the case with New York. On Monday, November 7, 2007, I sent Ms. Cheung the report which the Wall Street Journal has now posted on-line less everything past Attachment 1. This report further detailed BM's fraud.

My experience with New York Branch Chief Meaghan Cheung was akin to my previous discussions with Attorney Grant Ward, and demonstrated to me an SEC failure in providing appropriate personnel to understand the case I was submitting. Ms. Cheung also never grasped any of the concepts in my report, nor was she ambitious enough or courteous enough to ask questions of me. Her arrogance was highly unprofessional given my understanding of her responsibility and mandate. When I questioned whether she understood the proofs, she dismissed me by telling me that she handled the multi-billion dollar Adelphia case. I then replied that Adelphia was merely a few billion dollar accounting fraud and that Madoff was a much more complex derivatives fraud that was easily several times the size of the Adelphia fraud. Ms. Cheung never expressed even the slightest interest in asking me questions; she told me that she had my report and that if they needed more information they would call me. She never initiated a call to me. I did follow-up. I was the one always calling her . She was unresponsive and mostly uncommunicative when I did call, demonstrating a lack of interest and acumen for this area of investigation.

In December 2005, I decided that the third time was not a charm and that the SEC was, once again, not going to pursue the Madoff case. I also decided that if I was going to continue my investigation and attempt to involve the authorities, I should ensure my personal safety in case of possible efforts to silence me and end my investigation. I decided that I should go to the press. I went to Pat Burns, communications director at Taxpayers Against Fraud, an educational group that supports the False Claims Act, for advice and assistance on how to have my Madoff case materials investigated by the press. Mr. Burns put me in contact with John Wilke, senior investigative reporter for the Wall Street Journal's Washington Bureau. Mr. Wilke and I would become friends over the course of the next three years. Unfortunately, as eager as Mr. Wilke was to investigate the Madoff story, it appeared that the Wall Street Journal's editors never gave their approval for him to start investigating. As you will see from my extensive e-mail correspondence with him over the next several months, there were several points in time when he was getting ready to book air travel to start the story and then would get called off at the last minute. I never determined if the senior editors at the Wall Street Journal failed to authorize this investigation.

2006

On March 3, 2006, I had a 5-minute call with NY Branch Chief Cheung (Conversation memo e-mail to Frank Casey and Neil Chelo, Friday, March 3, 2006, 3:23 pm). When I mentioned that my derivatives expertise would be needed to break the case open, she dismissed me by saying that the SEC's Washington Headquarters had Ph.D.'s in an economics analysis unit with derivatives expertise. When I pointed out that the SEC likely didn't have any Ph.D.'s on staff with derivatives trading experience who truly understood how these financial instruments worked because a true derivatives expert couldn't afford to work for SEC pay, she ignored me. She was in "listen only mode." A trained investigator would have kept me on the phone for as long as possible, asking me as many open-ended questions as possible in order to advance their investigation. But as is typical for the SEC, too many of the staff lawyers lack any financial industry experience or training in how to conduct investigations. In my experience, once a case is turned into the SEC, the SEC claims ownership of it and will no longer involve the investigator. The SEC never called me. I had to call the SEC repeatedly in order to try to move the case forward and with little to no response. This may go a long way in explaining the SEC's long and consistent history of regulatory failures.

In the 2006 case materials you will see long strings of e-mails between myself, Neil Chelo and Frank Casey as we pushed the investigation forward because we felt that the SEC was not doing any work to advance the case. At the time, the SEC's reputation was slipping in the press, due to reports of its failure to investigate the Pequot insider-trading investigation. Additionally, the Integral Partners derivatives' Ponzi scheme from five years earlier was just beginning to go to trial. If the SEC could not successfully investigate and bring to justice a $50 million derivatives' Ponzi scheme, how would it handle a $30 billion derivatives Ponzi scheme? My team and I were on our own. We continued to vigorously pursue the investigation.

Perhaps the biggest breakthrough during the year was my September 29, 2006 telephone call to Matt Moran, Esq., Vice President of Marketing, for the Chicago Board Options Exchange. Mr. Moran confirmed to me that several OEX Standard & Poor's 100 index options traders were upset and believed that BM was a fraudster. Mr. Moran said he couldn't talk to either the Wall Street Journal. or the SEC without permission but that if these organizations went through proper channels and got permission from Lynn Howard, the CBOE's Public Relations Head, then the CBOE staff and traders would be able to cooperate with an investigation and answer questions. This was exciting news! Unfortunately, neither the Wall Street Journal. nor the SEC were inclined to even pick up a phone and dial any of the leads I had provided to them. It is a sickening thought but if the SEC had bothered to pick up the phone and spend even one hour contacting the leads, then BM could have been stopped in early 2006. One hour of phone calls was the difference between almost 3 more years of fraud and untold billions of additional investor losses. That's how close we were and how far we were from busting this case wide open in 2006.

2007

2007 was apparently a tough year for BM. Frank Casey got a hold of key May 2007 offering documents from Prospect Capital, a San Francisco based firm that was marketing the "Wickford Fund LP," which promised to deliver a swap that paid out between 3 to 3 ¼ times whatever BM's returns were less borrowing costs and management fees. Here I am using BM fund and Fairfield Sentry, a Greenwich, CT feeder fund interchangeably. This was a clear signal that BM was running low on new funds to keep his Ponzi scheme afloat.

In order to keep paying out funds to existing investors, a Ponzi operator must ensure that new funds are continually coming in the door to offset the outflow of payments to old investors. Creating a leveraged swap product was a sign that the inflow of new dollars was insufficient to keep the scheme going and that BM needed to create additional incentives sufficient to attract new money.

In a June 29, 2007 e-mail document submission to New York SEC Branch Chief, Meaghan Cheung I forwarded these offering documents to her office and copied Ed Manion of the Boston SEC Office. I also included updated April 2007 performance data from Fairfield Greenwich Group. The interesting thing about the performance data was that BM was noticeably stepping down his stated returns. If you look closely at the data, you will see that he went from double-digit returns from 1991 – 2000, but that all subsequent years returns were in single digits, a clear sign that he needed to cut back on the payouts to old investors in order to conserve cash and keep the scheme going. How the SEC could look at the same data we did and not arrive at the same conclusions that we did is hard to fathom. One would have to seriously question their industry experience and investigative expertise to have missed the red flags contained in the June 29, 2007 SEC Submission.

The Prospect Capital "Wickford Fund LP" performance chart just jumps out of the page at any experienced investment professional. Notice how the unlevered Sentry Fund performance is a steadily rising line. Well, that type of rising line without any downward interruption does not exist in the capital markets for any asset class over any meaningfully long period of time.

Above that steadily rising line is an exponentially rising line that depicts what the "Wickford Fund LP's" returns, using 3.1 to 1 leverage**,** would have been like if the fund had existed back in time. Let me explain 3 to 1 leverage. If a Madoff investor wanted to invest $1 million with BM he could do that on an unlevered basis without borrowing any money. Now Wickford Fund was allowing this same investor to invest her $1 million and borrow an additional $2 million so that she could now invest a full $3 million with BM. Nothing is free in finance and you can be sure there is a bank lending this investor the $2 million dollars she is borrowing and charging a profitable interest rate for providing this service. Wickford Fund LP is even happier to do this because they now get to charge 3 times as much in management fees because the investment amount is now $3 million and not $1 million. BM is also happier because instead of receiving $1 million, he's taking in $3 million and cheating not only the investor but the bank that is lending the investor the additional $2 million. This leveraged performance return line as provided on the graph not only does not exist for any asset class but any student of biology will recognize it as denoting a growth curve for natural organisms such as for population. How can any capital market return over any length of time only go up and never down? How did so-called due diligence "professionals" at the Madoff feeder funds miss this? How did the SEC's staff miss this? If a picture says a thousand words, then this picture said "FRAUD" a thousand times over.

In retrospect, perhaps I should have explained every single page to the SEC's New York Office. But, I was dismissed and ignored making any further attempts to explain on my part impossible. I do not know whether the cause was political interference or incompetence but the result was a refusal to look and an unwillingness to grasp even the simplest explanations for the red flags present in the "Wickford Fund LP" offering documents. Every phone call to Meaghan Cheung made me feel diminished as a person, so I consciously chose to e-mail her so that I didn't have to undergo unpleasant and unsatisfying telephone calls.

On July 10, 2007 Neil Chelo collected a key set of financial statements for 2004, 2005, and 2006 for BM's largest feeder fund – Greenwich Sentry, L.P.. Here I am using Greenwich Sentry and Fairfield Sentry interchangeably believing them to have the same ownership. Again, red flags popped up everywhere. Greenwich Sentry used three different auditors over that three year period which is a major red flag. Berkow, Schecter & Company LLP out of Stamford, CT was the auditor in 2004, Price Waterhouse Coopers (Rotterdam, The Netherlands) was the auditor for 2005, and Price Waterhouse Coopers (Toronto, Canada) was the auditor for 2006. This raised suspicions in my mind that Greenwich Sentry L.P. might be "auditor shopping."

The financial statements themselves were nothing but a giant red flag to any investment professional looking at them because BM was in US Treasury bills at year-end and there were no investment positions to mark to market. How convenient for a fraudster not to have any trading positions for an auditor to inspect. Since US Treasury Bills exist in book-entry form only, how convenient not to have any physical securities on hand to inspect either.

In late July, I also analyzed a BM portfolio that Neil Chelo obtained, dated February 28, 2007 which contained a 51 stock portfolio, OEX Standard & Poor's Index call options and OEX Standard & Poor's Index put options. The portfolio as constructed did not look capable of earning a positive return and I marked it as having lost .32% but Frank Casey sent me a performance number for February that showed a loss about a third of what this portfolio produced. Inconsistencies like this were so constant throughout the investigation, we had become immune to them. We would have been surprised only if something associated with BM actually made sense.

Neil Chelo lined up Amit Zjayvergiya, Fairfield Sentry's Head of Risk Management, for a 45-minute phone interview. Mr. Zjayvergiya's answers to Mr. Chelo's questions are listed in a August 24, 2007 e-mail. We discovered from this interview that BM's largest feeder fund, a fund with over $7 billion invested in BM, was not asking any of questions one would expect of a firm purporting to conduct due-diligence. Mr. Chelo is professionally certified as a Financial Risk Manager and asked several key risk management questions of Mr. Zjayvergiya and he did not receive satisfactory answers. I actually had hopes this interview would be longer and more intensive with full responses to the two full pages of questions I had sent to Mr. Chelo. Nevertheless our doubts were confirmed by the information we obtained.

2008

2008 was a strange year for everyone in global finance and our team was no exception. Because of market turbulence all of us were busy with other matters and let our BM investigation drop by the wayside with one exception which occurred in April. A good friend of mine, a University of Chicago Ph.D. in finance, Mr. Rudi Schadt, Oppenheimer Funds' Director of Risk Management, ran into a fellow University of Chicago Ph.D., a Mr. Jonathan Sokobin who was the SEC's new Director of Risk Assessment in Washington. Mr. Schadt, who was familiar with my work in the field of risk management, put Mr. Sokobin in touch with me in late March 2008. Mr. Sokobin asked that I call him, which I did a couple of days later. I wanted to give him a heads-up on some new emerging risks that I saw looming over the horizon. After our call, I felt that I had established my bona fides as a risk expert and felt comfortable enough to send him my updated, 32-page, December 22, 2005 SEC Submission along with a short 4 paragraph e-mail. I tried calling back a few times but never got through and gave up. I never heard from Mr. Sokobin again. At this point I truly had given up on the BM investigation.

Why did BM suddenly turn himself in on Thursday, December 11, 2008? Clearly, it was because he could not meet cash redemption requests by the feeder funds and fund of funds. Due to the seductive steadiness of his returns and the purported liquidity of his strategy, the fund of funds, in a down market, would consider him the best in their lineup of managers and would most likely go to him first with their redemption requests. Many hedge funds invest in illiquid securities for which they might have trouble finding buyers in a down market. Therefore, rather than sell in a down market when there may be no buyers and drive prices even lower than they were already, these fund of fund managers felt that they would have less negative price impact by asking BM to redeem what they considered to be their "safe" investments. BM's strategy of investing in highly liquid, blue-chip stocks seemed tailor made for easy redemptions. Therefore the fund of funds managers went to BM first (and most reliable investment) and this is what brought about his downfall. Too many hedge fund investors were asking to redeem their money and BM ended up with too many of these redemption requests which brought the entire house of cards down around him.

CONCLUDING THOUGHTS

The e-mails, marketing materials, conversation records and SEC Submissions you have as part of my official document submission to Congress are what four unpaid volunteers accomplished in our spare time to try and stop BM. We don't pretend to know what really happened on the mysterious 17th floor of the Lipstick Building at BM's corporate offices. Every bit of information we obtained was in the public domain. We never had any secret insider documents or smoking gun e-mails. We did what we could to stop BM from bilking the public. All of us feel very badly that we failed to achieve a positive result.

There were many things we definitely did not know. We never conceived that any high net worth professional investor would have 100% of their money invested in hedge funds. To investment professionals, a proper allocation to hedge funds would range between 0% - 25%, and certainly any such allocation would be spread among several managers, not given in its entirety to just one manager. And being from the institutional side of the business, we closely tracked the feeder funds and fund of funds that were investing in BM, but never realized that charities and individual investors were investing 100% of their money with BM. We also missed the obvious, that BM was Jewish, and as a result, he would be preying most heavily on the Jewish community because Ponzi schemes are first and foremost an affinity fraud.

We more closely tracked BM's affinity fraud through Europe which was a different community of victims from those targeted in the U.S. In Europe the affinity groups sought by the BM feeder funds were mainly European royal families, the high born old money families, and the nouveau riche. In Europe, the victims were mostly blue blood families. BM was truly masterful in using his feeder funds to draw in people close in make-up to the owners of the feeder funds. In this way he was able to expand his affinity victims to those beyond that of the Jewish community and gain entry into other affinity communities as well.

I am sure that we missed many other clues, warning signs and red flags but assure you that we did the best that we could with the information we dared collect. Every time we raised our heads to collect information, we exposed ourselves to discovery and feared the result.

By this time, law enforcement officials know a lot more than we do. The four of us will be waiting to find out what really went on behind closed doors. For those who ask why we did not go to FINRA and turn in Madoff, the answer is simple: Bernie Madoff was Chairman of their predecessor organization and his brother Peter was former Vice-Chairman. We were concerned we would have tipped off the target too directly and exposed ourselves to great harm. To those who ask why we did not turn in Madoff to the FBI, we believed the FBI would have rejected us because they would have expected the SEC to bring the case as subject matter experts on securities fraud. Given our treatment at the hands of the SEC, we doubted we would have been credible to the FBI.

And, I wish to clear the air on a very important matter about ethics, public trust, civic duty and what this all says about self-regulation in the capital markets. The four of us did our best to do our duty as private citizens and industry experts to stop what we knew to be the most complex and sinister fraud in American history. We were probably a lot more foolish than brave to keep up our pursuit in the face of such long odds. What troubles us is that hundreds of highly knowledgeable men and women also knew that BM was a fraud and walked away silently, saying nothing and doing nothing. They avoided investing time, energy and money to disclose what they also felt was certain fraud. How can we go forward without assurance that others will not shirk their civic duty? We can ask ourselves would the result have been different if those others had raised their voices and what does that say about self-regulated markets?

To the victims, words cannot express our sorrow at your loss. Let this be a lesson to us all. White collar crime is a cancer on this nation's soul and our tolerance of it speaks volumes about where we need to go as a nation if we are to survive the current economic troubles we find ourselves facing; because these troubles were of our own making and due solely to unchecked, unregulated greed. We get the government and the regulators that we deserve, so let us be sure to hold not only our government and our regulators accountable, but also ourselves for permitting these situations to occur.

Thank you and May God Bless the United States of America

<u>TIMELINE -SEE CHART</u>

Late	1999 Frank Casey "discovers" BM
Late 1999	Rampart tasks me to reverse engineer BM's strategy
Early 2000	4 hours of research proves mathematically that BM is a Fraudster
May 2000	8-page submission to SEC Boston Regional Office's Director of Enforcement
Jan 2001	Michael Ocrant starts researching the BM story for MAR Hedge
May 2001	Michael Ocrant publishes "Madoff Tops charts; skeptics ask how"
Sep 2001	SEC's Ed Manion calls to ask me to re-submit the Madoff Case
Oct 2001	2nd SEC Submission consists of original 8-page May 2000 Submission+ 3 additional pages + 2 page Investment Process Explained
2002	Investigation continues: e-mail records lost

June 2002	Key Marketing trip to London, Paris, Geneva & Zurich where I discover that Europeans are likely BM's largest investors
2003	Investigation continues: e-mail records lost
2004	Investigation continues: e-mail records lost
Oct 2005	SEC's Ed Manion arranges for 3rd case submission
Oct 2005	I meet with Boston SEC Branch Chief Mike Garrity
Oct 2005	SEC's Mike Garrity investigates
June 2005	Frank Casey discovers that BM is attempting to borrow money at European Banks – the 1st indication that the scheme is running short of $
Nov 2005	SEC's Mike Garrity puts me in contact with New York SEC
Nov 2005	3rd SEC Submission to SEC's Error! Bookmark not defined. in NY
Dec 2005	I start to doubt NY SEC and contact WSJ Washington Bureau
Jan 2006	Integral Partners $40 million derivatives Ponzi scheme goes to trial, 5 years and 5 months after its discovery causing us to further doubt SEC competence
Sep 2006	Chicago Board Options Exchange Marketing VP tells me that several OEX option traders also believe that BM is a fraudster
2007	Neil Chelo obtains Feb 28, 2007 portfolio of BM trading positions, portfolio shows no ability to earn a positive return
June 2007	Frank Casey obtains Wickford Fund LP prospectus showing that BM is now so short of cash that he is offering a 3:1 leverage swap to obtain new funds
June 2007	This prospectus is e-mailed to NY SEC's Error! Bookmark not defined.
July 2007	Neil Chelo obtains Greenwich Sentry LP Financial Statements for 2004-06; Auditors are different for each of the 3 years which is very odd
Aug 2007	Neil Chelo has opportunity to interview Fairfield Sentry's head of risk management who displays a startling lack of acumen
Aug 2007	Hedge funds all have losses this month except for BM – he's amazing!

2008	Global markets dive, entire investigating team loses interest and is busy with more pressing matters
April 2008	Jonathan Sokobin, SEC's Director of Risk Assessment calls me per the recommendation of a mutual friend
April 2008	I send Mr. Sokobin my last SEC Submission and quit the investigation
Fall 2008	Stock Markets crumble, panicked investors rush to redeem
Dec 2008	Madoff "confesses" and turns himself in after running out of cash to meet investor redemptions

PART II REBUILDING THE SEC

The Current Situation is Dire but Fixable: there is no where to go but up!

Securities fraud is a scourge on the marketplace. Investors who suspect fraud or who aren't confident that a level playing field exists will properly require higher returns. To the companies trying to raise capital in the marketplace, investors' higher return requirements mean a higher, unaffordable cost of capital or worse, the total unavailability of capital at any price. Today, thanks to the lack of effective regulation and oversight, our capital markets are barely functioning. Markets need to be fair, efficient and transparent in order to work properly. They also need to be regulated in order to ensure a constant availability of credit at affordable rates.

Right now, investors are afraid and do not trust the banks, insurance companies, brokerage firms, credit ratings agencies, investment managers, hedge funds, or other financial institutions nor should they. Investors particularly do not trust our nation's financial regulators, particularly the Federal Reserve Bank (FED) and US Treasury who have both told them repeatedly that things were fine, when in fact, things were only about to get worse. The ultimate insult to investors is the FED's refusal to tell us which financial institutions are borrowing from the Discount Window and how much they are borrowing. This startling lack of transparency from regulators has led to a massive lack of investor confidence. Only by providing investors with full transparency and allowing them to make rational investment decisions, will our capital markets find the proper price levels so that buyers can find sellers and sellers can find buyers.

Investors want to know that the financial firms they are dealing with are solvent and right now they feel that our government isn't telling them the truth about the solvency of this nation's largest financial institutions so the entire system remains paralyzed, needlessly wondering who the zombie financial institutions are. My advice is to take the pain up front and either nationalize or close the zombie financial institutions as soon as possible and put the uncertainty to rest. Trust will not be restored until full transparency is restored.

Every single one of this nation's too many financial regulators failed to earn their paychecks. This is the reason our financial system has been on the verge of collapse over these past several months. Unfortunately, as bad a regulator as the SEC currently is, and the SEC certainly is a bad regulator, it's the best of a very sorry lot. Compared to the FED which has led this nation to the abyss of national bankruptcy by it's refusal and inability to regulate the banks, the SEC actually looks halfway competent. Thanks to the ineptitude of financial regulators, Wall Street as we once knew it ceases to exist and too many of the nation's largest banks are on government life support, too weak to lend and too battered to survive as currently constituted.

Our nation has too many financial regulators. The separation and lack of connection and communication between them leaves too many gaping holes for financial predators to engage in "regulator arbitrage" and exploit these regulatory gaps where no one regulator is the monitor. In more than one financial institution, employees have two different business cards. One card has their registered investment advisor title (which falls under SEC regulation) and the other has their bank title (which falls under banking regulators). When the FED comes in to question them, they say they're under the SEC's jurisdiction and when the SEC comes in to question them, they say they're under the FED's jurisdiction. Clearly this situation has to be corrected so firms cannot play one regulator against the other or worse, choose to be regulated by the most incompetent regulator available while avoiding the most vigorous and thorough regulators.

The goal needs to be to combine regulatory functions into as few a number as possible to prevent regulatory arbitrage, centralize command and control, ensure unity of effort, eliminate expensive duplication of effort, and minimize the number of regulators to which American businesses have to answer. To this end, I recommend that one super-regulatory department be formed and that it be called the Financial Supervision Authority (FSA). Under it's command would come the SEC, the FED, a national insurance regulator and some sort of combined Treasury / DOJ law enforcement function with staffs of dedicated litigators to carry out both criminal and civil enforcement for all three. All banking regulators should be merged into the FED so that only one national banking regulator exists. The FED Chairman, Vice-Chairman, and Governors who set monetary policy can be spun out into a separate, independent operating units, but since they've shown themselves to be such incompetent regulators, this critical function would be stripped away from them. Pension regulation should be moved from the Department of Labor to the SEC. Futures and commodities regulation should be moved from the CFTC to the SEC. Cross-functional teams of regulators from the SEC, FED, national insurance regulator and Treasury/DOJ should be sent on audits together whenever possible to prevent regulatory arbitrage. I envision the inspection arms to be the SEC, FED and national insurance regulator while the Treasury / DOJ litigators house the litigation teams that take legal action against defendants. American businesses deserve to have a simpler, easier to understand set of rules to abide by and they also deserve to have competent regulation at an affordable price. Right now financial institutions pay a lot in fees for regulation but they aren't getting their money's worth. Government needs to give business regulation that provides a value-proposition, where fees paid to regulators equal value received by business.

The SEC is a Failed Regulator: But it Can't Remain One

The story I have related in Part 1 underscores the deeply flawed connections or lack thereof between financial regulators as well as the systemic failures of the SEC. These systemic failures are instantiated by my particular experiences with the SEC as explained above but also generally replete in the history of the SEC over the past few decades. Let me provide you with a representative list of only some of the agency's major failures. During the tech bubble years, the SEC ignored the Wall Street Analysts' recommendations, almost all of which were "buy recommendations" even though these same analysts privately advised a few privileged investors to sell these over-priced or worthless securities, leading up to the 2000 – 2003 bear market. In 2003, the SEC's Boston Regional Office turned away Mr. Peter Scannell, the Putnam market-timing whistleblower. Fortunately, Mr. Scannell survived a vicious beating and went to both the Massachusetts Securities Division (MSD) and the New York Attorney General (NYAG) who believed him and enforced the nation's first market-timing scandals while the SEC watched from the sidelines until embarrassed enough to finally enter the fray with enforcement actions of its own. In 2007 and 2008, the Auction Rate Securities scandal hit the headlines, and once again the SEC remained busy looking the other way, protecting predatory investment banks from defrauded investors. And, once again, the NYAG and MSD conducted effective and timely enforcement actions to ensure that defrauded investors got their money back. More recently, the SEC watched quietly but did nothing to prevent the train wreck as the nation's five largest domestic investment banks either failed like Lehman, were rescued by government forced acquisitions like Bear Stearns and Merrill Lynch, or became bank holding companies in order to survive like Goldman Sachs and Morgan Stanley. And today, no investor knows what the bank's balance sheets look like because the SEC is refusing to enforce transparency rules.

When the industry you purported to regulate implodes and the nation's financial system is frozen, then it is safe to say that you've failed as a regulator. It is also safe to say that the SEC has lost the nation's confidence. The Executive Branch and Congress are faced with the following critical question – do we disband the SEC, merge it out of existence, or fix it?

Rebuilding the SEC:

I come before you not to bury the SEC but to assist you in helping to tear down and rebuild an SEC capable of effectively regulating capital markets in the 21st century. I promise to be blunt in my assessment of where the SEC is today and where it needs to go in the short term and long term. No punches will be pulled regardless of the SEC's embarrassment. Until the SEC admits to and embraces its failures, it will not be able to recover and rebuild. "*Denial*" is not just a river in Egypt, it's the mindset that the SEC has adopted. It has blamed everything on a lack of staff and resources while refusing to admit to its underlying problems. I know that I am tired of their lame excuses and I suspect that Congress and the American public are also tired of the SEC's shameless attempts to deflect blame. It's high time and past time for some personal responsibility on the part of the SEC's senior staff. Our nation's capital markets didn't fall so far and so fast without a lot of help from regulators who failed to regulate. At the very least the SEC's senior staff should be making profuse apologies to Mr. Madoff's victims. Instead all I've heard are SEC promises to look into what happened with my repeated SEC Submissions which told the SEC exactly where to look to find the fraud.

In my dealings with the SEC I have noted many deficiencies and will point those out in enough detail so that the new management team can fix them in the next four years. I believe the one over-arching deficiency is that the SEC is a group of 3,500 chickens tasked to chase down and catch foxes which are faster, stronger and smarter than they are. It's painfully apparent that few foxes are being caught and that Bernie Madoff, like too many other securities fraudsters, had to turn himself in because the chickens couldn't catch him even when told exactly where to look. As currently staffed, the SEC would have trouble finding first base at Fenway Park if seated in the Red Sox dugout and given an afternoon to find it. Taxpayers have not gotten their money's worth from the SEC and this agency's failures to regulate may end up costing taxpayers trillions in government bailouts.

Dramatically Upgrading SEC Employee Qualifications & Educational Budgets:

Amazingly, the SEC does not give its employees a simple entrance exam to test their knowledge of the capital markets! Therefore is it any wonder when SEC staffers don't know a put option from a call option, a convertible arbitrage strategy from a long/short strategy, the left side of the balance sheet from the right side, or an interest only security from a principle only security. By failing to hire industry savvy people, the SEC immediately sets their employees up for failure and so it should not be surprising that the SEC has become a failed regulator.

A good way for Congress to find out exactly what I mean when I say the SEC doesn't have enough staff with industry credentials is to query the SEC senior staff that come before your Committee. Ask them – "Do you have any financial industry professional certifications?" "Have you ever worked on a trading desk?" "What accounting, business or finance degrees do you hold?" "What financial instruments have you traded in a professional capacity?"

If Congress decides to keep the SEC in existence, then upgrading its staff, increasing its resources, and wholly revamping its compensation model is in order. In order to attract competent staff, a test of financial industry knowledge equivalent to the Chartered Financial Analysts Level I exam should be administered to each prospective employee to ensure that new employees have a thorough understanding of both sides of a balance sheet, an income statement, the capital markets, the instruments that are traded and the formulas incorporated within these instruments. Talented Certified Public Accountants (CPA's), Chartered Financial Analysts (CFA's), Certified Financial Planners (CFP's), Certified Fraud Examiners (CFE's), Certified Internal Auditors (CIA's), Chartered Alternative Investment Analysts (CAIA's), MBA's, finance Ph.D.'s and others with industry backgrounds need to be recruited to replace current staffers. One thing the incoming SEC Chair should do right away is order a skills inventory of the current SEC staff to measure the exact skills shortfalls with which she is now faced. My bet is that Ms. Shapiro will find that she has too many attorneys and too few professionals with any sort of relevant financial background.

I recommend that the Chair ask the SEC senior staff to provide her with a complete skills listing of the current SEC staff. Knowing how many SEC employees hold accounting, business, and finance degrees versus how many hold law degrees would be a useful first step in quantifying the mismatches between skills on hand versus skills required to properly regulate. Determining how many SEC employees have ever worked on a trading desk would be particularly illuminating for the new Chair. Ditto for how many SEC employees are CAIA's, CIA's, CPA's, CFA's, CFE's, CFP's, and FRM's. My bet is that the SEC staff is critically short of employees with credible industry experience.

I caution the SEC to avoid focusing on any one of the above professional certifications at the expense of the rest because all are relevant and necessary. The SEC also needs to avoid having too many people with educational and professional backgrounds that are too alike. Diversity will ensure that group-think is kept at bay and that the SEC embraces multiple relevant skill sets. Right now the SEC is over-lawyered. Hopefully it can transition away from this toxic mix as quickly as possible.

I would like to see the SEC expand its tuition reimbursement program to pay 100% of relevant post-graduate education courses with one year of additional government service for each year of graduate education. Currently, the SEC does not allow its staff time out of the office to attend industry luncheons, dinners, cocktail parties etc. nor does it pay for their attendance at these low cost learning events. SEC staffers need to be encouraged to attend industry conferences, particularly those venues where brand new securities are being featured, so that they are not caught flat-footed and behind the curve when these securities enter the marketplace. Because people tend to say and do things when they are traveling that they would never do at home, conferences are the ideal venue for the SEC to find out what’s happening in the industry and, more importantly, what’s about to happen. Sending SEC staff to conferences with a written information collection plan, under the supervision of a senior person, with the goal of obtaining information and marketing literature about new products and querying attendees about frauds within the industry is a cost-effective solution to keeping the SEC on level ground with the industry it regulates.

Large cities with robust financial centers have financial analyst societies and economic clubs which hold educational meetings of just the sort the SEC staff needs. For example, in my hometown, the Boston Security Analysts Society has 5,000 members and holds educational lunches at least twice weekly, but the SEC won't reimburse its staff to attend these luncheons even though firms within the industry do. New York and Washington also have sizeable analysts societies but rarely does anyone see SEC staff attending these educational events and we all know it isn't because the SEC has no need for greater industry knowledge. Either the SEC is anti-intellectual and intentionally maintaining staff uneducated about the capital markets or it is merely being ignorant. In either case, not to budget for it's staff's education is indefensible in the 21st century. SEC employees are knowledge workers, not unthinking, replaceable cogs and deserve to have the required educational resources available to them to do their jobs.

To further illustrate the anti-intellectual bias of the SEC, consider what the SEC staff has printed on their business cards. If you're expecting to see Certified Public Accountant, Certified Financial Planner, Certified Fraud Examiner, Certified Internal Auditor, Financial Risk Manager, Chartered Financial Analyst, Chartered Alternative Investment Analyst, or some other sort of highly sought after professional designation, you will be sorely disappointed. For some unfathomable reason, most of the very few credentialed SEC staffers do not have their professional designations printed on their business cards. Why not? One would almost think that the SEC's top leadership was going out of its way to drive good people out of the SEC and destroy the morale of those who stay. The all too few SEC staffers I know with industry credentials have all told me they are not allowed to have these designations printed on their business cards. The only reason for this that makes sense is that if the SEC allowed its few credentialed staff to put these credentials on their business cards it would expose the overall lack of talent within the SEC. Therefore, one thing I would immediately recommend is that relevant industry credentials be printed on the Staff's business cards ASAP. Not only is this good for morale, but it also tells you which staff are worth keeping and which ones need to be told to find new jobs because their skills aren't relevant and don't meet either the SEC's or the investing public's needs.

Another shocking revelation is that MAR Hedge published an expose on BM on May 1, 2001 while Barron's published their copycat BM expose on May 7, 2001 but the SEC doesn't pay for subscriptions to industry publications for its staff so their staff likely never read these damning articles which each contained numerous red flags. That's right, if the SEC staff want to read industry publications they have to pay for them on their own because the SEC won't pay for them. I remember that after reading both of these Madoff expose articles, Neil Chelo, Frank Casey and I felt 100% certain that the SEC would be shutting down BM within days. What we didn't know at the time was that the SEC doesn't read industry publications. We were shocked.

If you walk into any sizeable investment industry firm, it will have a library of professional publications for the staff to use as a resource. Typical journals on hand would be the Journal of Accounting, Journal of Portfolio Management, Financial Analysts Journal, Journal of Investing, Journal of Indexing, Journal of Financial Economics, and the list goes on and on. But, if you walk into an SEC Regional Office, you won't see any of these journals nor will you see an investment library worthy of the name. If an SEC Regional Office does have an investment library, it is usually the effort of one lone, highly motivated, employee who stocks a bookshelf on his/her own time, paying for the publications him or herself. This begs the question, where do SEC staffers actually go to research an investment strategy, find out which formulas to use to determine investment performance, or figure out what a CDO squared is?

Apparently all the SEC staff uses is Google and Wikipedia because both are free. Lots of luck figuring out today's complex financial instruments using free web resources. No wonder industry predators run circles around the SEC's staff. It's easy to fool people from an ignorant regulator that goes out of its way to ensure that its staff remains uneducated and under-resourced.

The SEC has exactly the wrong staff for the 21^{st} century and a staff that's incapable of comprehending the financial instruments it is charged with regulating. Even if the SEC did provide a sensible publications budget for its staff so that staff could subscribe to the Wall Street Journal, Barron's, Business Week, and formed research libraries containing all the important financial journals, its staff would still need to understand what instruments are being regulated and which formulas are being used. The faulty recruitment of unnecessary and inefficient and incompetent human resources would remain.

To properly regulate the finance industry, the SEC needs to hire people who know how to take apart complex financial instruments and put them back together again. If an SEC staffer doesn't know derivatives math, portfolio construction math, arbitrage pricing theory, the Capital Asset Pricing Model, both normal and non-normal statistics, financial statement analysis, balance sheet metrics, or performance presentation formulas then they shouldn't be hired other than to fill administrative or clerical positions.

For instance, a person I know rather well in the Boston office, with over 10 years of industry experience, a double major under-graduate degree in economics and math from an Ivy League school, with an MBA degree and a Chartered Financial Analysts designation wanted to leave her job as a senior analyst at a large mutual fund company in order to have another child. She wanted out of the rat race where 60 hour work weeks were both common and expected so she applied for a job with the SEC. During her interview she was told that she was 1) overqualified with too much industry experience, 2) over educated and 3) that she wouldn't be happy inspecting paperwork and would likely quit in frustration so the SEC didn't plan on offering her the job. This is deeply problematic as it underscores the lack of a proper recruitment policy to equip the SEC with appropriate personnel for the work with which it is mandated and the expertise expected in order to appropriately monitor our financial institutions and their numerous transactions. The SEC apparently is only interested in administrative verification, to ensure compliance with existing (outdated) securities laws. Is it any wonder, given the current SEC staff, that major financial felonies go unpunished while minor paperwork transgressions are flagged for attention?

Besides upgrading its staff at the junior and mid-levels, the SEC needs to recruit foxes to join the SEC staff in senior, very high paying positions that offer lucrative incentive pay for catching foxes and bringing them to justice. The revolving door between industry and regulators can be precluded if the SEC recruits highly successful industry practitioners who have succeeded financially during their long careers and now want to serve the American Public by fighting securities abuses. The ideal candidates would all have gray hair (or no hair at all) and the SEC would be the capstone on their already illustrious careers. The main hiring criteria would be that each candidate would have to submit a written list of securities frauds that he/she would attack and list the estimated dollar recoveries for each of these frauds. These "foxes" would then be brought on board specifically to lead mission-oriented task forces dedicated to closing down these previously undiscovered frauds, restoring trust in the marketplace, thereby lowering the cost of capital and minimizing the regulatory burdens for honest American businesses. My theory is that it's better to target your enforcement efforts at known fraudsters while leaving honest American businesses alone other than for occasional but thorough spot inspection visits. The fraudsters would be terrified but most businesses would be relieved if the SEC adopted the proposed regulatory scheme.

In summary, the SEC needs to stop hiring more of the same people it's already been hiring. What the SEC needs to do is test its staff, identify who to retain, get rid of those who either don't have the proper skills sets for their specific mandates at a 21st century level or don't want to obtain those skills, hire foxes from industry to lead the enforcement and examination teams, increase the pay levels, and expand its educational budgets to ensure that the SEC becomes a forward leaning, learning organization that is more than a match for the industry it regulates.

The SEC needs to adopt Industry Compensation Guidelines in order to compete:

Compensation at the SEC needs to be both increased and expanded to include incentive compensation tied to how much in enforcement revenues each office collects. Industry pays a base salary plus a year-end bonus that is tied directly to revenues brought into the firm. The SEC needs to adopt the industry's compensation guidelines in order to compete for talent. Of course, the SEC Commissioners would continue to approve the levels of the fines for enforcement actions because it would be a clear conflict of interest to have the enforcement and examinations staff set the fines that lead to their own compensation. Each SEC Regional Office should get back some pre-set percentage of the fines it brings in, and I recommend a 5% level initially, toward that office's bonus pool. Regional enforcement teams that do great work and bring in a $100 million case settlement deserve to be compensated for their excellence. And, to prevent taxpayers from having to pony up these multi-million dollar bonus pools, I recommend that fines be triple the amount of actual damages, that the guilty transgressors pay the actual costs of the government's investigation, and that SEC staff bonuses also be paid for by the guilty transgressors.

In expensive financial centers' like New York, Boston, Chicago, Los Angeles, and San Francisco, cost of living adjustments bringing base compensation to the $200,000 level make sense plus the award of annual year-end bonuses but only when merited. In the lower cost regions, a $100,000 - $150,000 base compensation would be fair, adjusted to local prevailing wage and cost data. This would be enough to attract the nation's best, brightest and most experienced industry practitioners. All compensation over and above the base compensation amount would come from each regional office's bonus pool and be tied directly to the fines (revenues) that each office generates. People who do not perform and bring in good quality cases that result in settlement awards to the government will get asked to leave and make room for people who can come in and produce solid cases.

To be effective, the SEC cannot afford to be less talented and educated than the industry, and I would argue it can't even strive to be as good as the industry, it needs to be better! If the incoming Chair sets her sights too low, that's an admission of defeat and our capital markets can't afford to have this agency continue to fail. If our regulators continue to fail, then our capital markets won't recover because investors won't return until they are assured of a fair deal with full disclosure.

I would also institute quantifiable metrics to measure the new, 21st Century regulatory effectiveness. Obvious metrics are revenue from fines, dollar damages to investors recovered, dollar damages to investors prevented, fine revenues per employee per regional office, and the number of complaints from Congress to the regulators complaining about the severity of the fines or the thoroughness of the government's investigations. Let me tell you a story about a very competent and talented SEC attorney in the Boston Regional Office who says that every time he receives a phone call from Washington SEC Headquarters calling him off an investigation, it's for one reason and one reason only – because that is the only way the predator financial institution he is currently investigating can escape justice and escape making restitution to the victims. If the number of Congressional complaints ever went down year after year it could only have one of three meanings: 1) better members of Congress, 2) the SEC is doing such a magnificent job of fraud detection that white collar crime actually drops or 3) a worse job by the SEC that year.

Raise the Enforcement Bar to Incorporate Good Ethics into the SEC's Mission focus:

Just because it is not illegal doesn't mean the SEC should ignore unethical behavior in the marketplace, which it has been doing for several decades now by trusting the industry to self-regulate its way to good behavior. The SEC must change its mission toward ensuring full transparency, fair play, and zero tolerance for unethical financial dealings. Note that I didn't say the SEC's mission should tend away from "enforcing the nation's securities laws." Given that there is no way to keep a set of securities laws on the books that is up to date and fully accounts for all of the bad behavior that financial predators can and will engage in, the SEC needs to recognize that securities laws are not the be all and end all of regulation, they are merely the absolute bare minimum standards which market participants must follow. Securities laws will never be fully up to date or always relevant. The current crisis will see that new, more relevant laws are enacted, but after these crises pass, securities laws will once again quickly become obsolete until the next crises appears. We need to end this cycle of overdependence on a series of rapidly outdated securities laws as our basis for enforcement and err on the side of protecting our investors.

The SEC's main focus is to mindlessly check to see if registered firms paperwork is in order and complies with the law as written. If a firm happens to be a financial predator and is engaged in market-timing or selling auction rate securities, the SEC's lawyers will not be concerned because market-timing and auction rate securities aren't illegal, merely unethical. If that firm's paperwork meets legal requirements, the SEC will give these financial predators a free pass just like it has always done. You will note that the SEC has said that the market-timing of mutual funds was not illegal, which may explain why the SEC turned away the Putnam whistleblower, Peter Scannell in 2003. The long-term, buy and hold mutual fund investors who lost that billions in returns to market-timers as a result of these actions and omissions, certainly would agree that this activity was unethical and they deserved to have this money returned to their retirement accounts. Auction rate securities issuers and investors ended up similarly disappointed thanks to the SEC's willingness to foster an "anything goes" climate on Wall Street. Enough of the securities' lawyers robotic simple compliance audits, let's shift the 21st century's capital markets to a higher plane, and start to insist on ethical capital markets that give all investors a fair deal with full transparency.

The bare minimum requirement of compliance with securities' law does not serve the higher standards and needs of today's financial markets and the pace of modern market practices. Policy standards and requirements including, good ethics, fair dealings, full transparency, and full disclosure need to be adopted and enforced. The SEC needs to shift its focus away from the lowest common denominator, mere securities law enforcement, and upgrade it to change we can believe in by ensuring full transparency, fair play and zero tolerance for unethical financial dealings.

Revamping the Examination Process:

I am not sure how many of you have ever undergone an SEC inspection visit. I was a portfolio manager, then chief investment officer, at a multi-billion dollar equity derivatives asset management firm, and equity derivatives was considered a "high risk " area by the SEC. My firm received SEC inspection visits every three years like clockwork. I've been through these examinations and will tell you about their many obvious flaws. First, the SEC never once was able to send in an examiner with any derivatives knowledge. It was a good thing my firm was honest because if we weren't, we could have pulled a Madoff on them and they would have been none the wiser. Second, the Sec audit teams are very young and they rarely have any industry experience. Third, the teams come in with a typed up list of documents and records they wish to examine. They hand this list to the inspected firm's compliance officer (CO). The CO then takes them to a conference room and the firm provides the pile of documents and records which the SEC team inspects diligently. So, if a firm were so inclined, it could keep a second set of falsified but pristine records yet commit the equivalent of mass financial murder and get away with it, just as long as the firm had at least one set of (falsified) books and records that were in compliance.

Now let's examine what is wrong with the examination process described above. First, the team only interacts with the inspected firm's compliance team, not the traders, not the portfolio managers, not the client service officers, not the marketing staff, not the information technology department and not management. The problem with this process is that the SEC examiners only examine paperwork but neglect the tremendous human intelligence gathering opportunities that are sitting right outside the conference room. What these SEC examiners need to be doing is sending one or two people out on the trading floors and into the portfolio manager's offices to ask leading, probing questions. During every single such unscripted interview, the SEC examiner should ask, "*Is there anything going on here that is suspicious, unethical or even illegal that I should know about? Are you aware of any suspicious, unethical or even illegal activity at any competing firms that we should be aware of?* And, during that interview, the SEC examiner should be handing out his/her business card, asking that person to call them personally if they ever run across anything the SEC should be looking into either at their firm or any other firm. Unless everybody at a particular firm is dishonest, if fraud is present, at least these standard internal auditing techniques will result in a materially significant number of new enforcement cases. These are internal auditing techniques that well trained accountants, internal auditors, and fraud examiners use when conducting audits or investigations. But at present, the SEC staff is so untrained, it's almost as if this concept of talking to a firm's employees is advanced rocket science. It is my belief that SEC examiners are so inexperienced and unfamiliar with financial concepts that they are literally afraid to interact with real finance industry professionals and choose to remain isolated in conference rooms inspecting pieces of paper.

From her first day in office, the incoming SEC Chair needs to get these examiners to focus on interacting with industry professionals and querying them on what's going on in their firms and their competitors' firms. Sitting like ducks in the inspected firm's conference room and getting fed controlled bits of paper by the firm's compliance staff isn't getting the job done. As currently constituted, the current examination process is an insult to common sense, a waste of taxpayers' money, and it can't be good for SEC employees' morale either. This also reinforces the need to increase the pay scale and add incentive compensation such that more qualified people apply for and take SEC jobs. Unless and until the SEC puts real finance professionals on those examination teams, their odds of finding the next Bernie Madoff range from slim to none.

When a financial analyst is about to visit a company to determine whether or not to invest in that company's stock, the first thing he/she does is go to a Bloomberg and analyze the firm's capital structure, it's financial statements, financial statement ratios, look up the firm's weighted cost of capital, and start running horizontal and vertical analyses of the financial statements looking for trends and outliers. The trained analyst will also use his/her Bloomberg to read all the news stories on the company, look at the firm's SEC filings, and use all of the information above to build a set of questions he/she needs to answer in order to arrive at an intelligent investment decision. The analyst will also obtain Wall Street analyst research reports and read them all to see what information other analysts' research on this company's main strengths and weaknesses.

Unfortunately, the SEC staff examiner doesn't do this. The main reason is lack of training on use of a Bloomberg machine. In the rare event the staff has know how, most SEC

Regional Offices are lucky to have even one Bloomberg machine for the entire region's use. Whereas your typical investment firm would have one Bloomberg per analyst, trader and portfolio manager, the SEC unwisely only funds one per office! For SEC compliance and examinations' the use and need for Bloomberg machines are an inherent industry requirement. The work in brief cannot be done without it. Those Bloomberg machines are the lifeblood of the industry, they contain much of the data an SEC staffer would need for any fraud analysis of a company.

Here is a quick example so that you understand how vitally important a Bloomberg machine is to securities enforcement. If you type in a company's stock ticker symbol, say ABC then hit "WACC" equity go, ABC Company's weighted cost of capital would pop up on your screen. Let's say ABC Company a weighted average cost of capital of 10% between its outstanding debt which pays an average of 6% interest and its equity which has a 14% cost associated with it and the mix between debt and equity is 50/50 [(.5 x 6%) + (.5 x 14%) = 10% cost of capital]. Assume that ABC Company is a Defense Contractor and bids "cost plus 3%" on an Iraqi War contract yet the company's cost of capital is 10%. This is a clear sign that ABC Company is likely cheating the Defense Department on that contract since no company would willingly accept any contracts which fall under its cost of capital. Working for 3% when a firm's cost of capital is 10% would quickly lead the firm into bankruptcy since that contract would be costing the firm a minus 7% return if the costs being passed onto the government were accurate. A good SEC examiner would immediately suspect ABC Company was padding the costs in its Iraqi War contract and alert the DOD's Defense Criminal Investigation Service to conduct a fraud audit. If everyone in industry is using Bloombergs except for the SEC, it is little wonder the SEC can't find fraud. The staff does not have the tools and training necessary to do their jobs.

In case you are still not convinced, take the following challenge. Name one major securities fraud case that the SEC busted wide open on its own without the felon first turning himself in? Give up? The last major pre-emptive SEC strike was Ivan Boesky, for insider trading violations over two decades ago. Today's SEC staff are more like financial crime scene investigators, coming in after the fraud scheme has already collapsed, toe-tagging the victims, trying to figure out who the bad guys were and how the fraud scheme occurred. To date the SEC's inability or unwillingness to regulate and more importantly to implement regulation with adequate tools and training have potentially cost us trillions in the recent financial crisis.

An Alternative Course of Action: Disbanding the SEC

Fortunately, the US already has two very competent securities' regulators who do a truly fantastic job and at an unbelievably low cost. Unfortunately, they are the New York Attorney General's office (NYAG) and the Massachusetts Securities Division (MSD). The NYAG and MSD have busted open the Wall Street analysts' bogus stock recommendations scandal, the mutual fund market-timing scandals, the auction rate securities scandals and a whole host of other industry violations. Where has the SEC been beforehand while all of these frauds were being committed? Sitting safely on the sidelines watching the fraud go by, daring not to get involved for fear of upsetting their masters on Wall Street. And this is the nicer, kinder explanation. Many investors may claim the SEC has been intentionally missing in action so as to aid and abet financial industry fraud to ensure that predatory financial institutions remain safe from investors. From an investors' perspective, the only two regulators that have stood up and made investors whole are the NYAG and MSD. These two regulators need to be publicly commended for the great job they are doing on behalf of investors everywhere.

Therefore, one alternative solution for Congress to consider is to disband the SEC and give its budget to the NYAG and MSD to hire staff and keep doing what they've been doing which is a darn good job of protecting investors. One reason these two states have competent regulators is that New York City is the world's largest financial center while Boston is the world's fourth largest financial center. London is No. 2 while Tokyo is No. 3. Somehow, I doubt that the NYAG and MSD would be hiring many people from the SEC, choosing instead to find competent employees with industry experience locally to do the job more efficiently. From an efficiency standpoint, the NYAG and MSG employ far fewer people at much lower cost and do a much better job of securities regulation than the SEC. If the state regulators are providing more regulatory bang for the buck, an option would be to fund them and zero out the SEC's budget. After all, we let poorly performing private companies fail, why not let poorly performing government agencies fail too?

Congress should always keep its options open regarding further funding of the SEC. If this agency continues to fail to regulate, holding the threat of disbandment over their heads by giving its budget to state securities regulators is the ideal high card for the Congress to keep in its pocket to ensure that the SEC understands it can either improve or disappear. The SEC's most committed staffers will not allow their agency to fail, nor will they allow anyone more senior to them within the agency to lead it down the wrong path. Plus, the threat of extinction does have a certain way of focusing attention and accomplishing goals more quickly than would otherwise be the case. Hopefully this alternative path will impose Congress's will over the SEC such that the agency meets all Congressional deadlines and mandates.

An Alternative Course of Action: Assigning the NYAG & MSD to enforce large, industry-wide cases and let the SEC conduct the routine, paperwork inspections.

This is similar to the enforcement reality already in effect where the NYAG and MSD discover the truly big industry-wide frauds and conduct nationwide enforcement actions to recover investor assets. The SEC seems to be a captive agency that purposely ignores the large frauds, focusing only on the minor transgressions it can find during the normal, routine examination process. This alternative course of action formalizes the reality on the ground today.

Congress could fund the NYAG and MSG so that it could do more of the large securities fraud enforcement cases at which it has developed great expertise. The SEC could keep its current budget and continue to police up the misdemeanors it seems to do passably well.

This alternative has the advantage of playing to each regulator's strengths. The NYAG and MSD don't have the SEC's thousands of employees with which to conduct nationwide inspections of regulated firms. However, the NYAG and MSD do have a deep bench of experienced litigators and investigators with pit bull tenacity. As they say, it's not the size of the dog in the fight, it's the size of the fight in the dog that matters. The SEC has 3,500 employees and can continue to muddle along, handling the low-level securities violations it has a known appetite for while avoiding the large fraud cases which it doesn't seem to have either the heart nor the skill to attack.

Recommendations for the New SEC Chair:

Given the SEC's current crisis situation it cannot be managed toward greatness, it needs to be led there. No amount of management can save the SEC. You manage budgets and resources but you have to lead people, and the best place to lead from is the front, setting the example for everyone behind you to follow. It will take a first-rate job of leadership, hard work and a bigger budget to turn around this agency but I know it can be done. Ms. Shapiro has been given every good leader's dream, to take command of an organization that has nowhere to go but up.

If, by year-end 2009 there is not a dramatically measurable improvement in the number of cases brought and SEC staff morale has not improved, then a replacement Chair needs to be hired. President Obama needs to go through regulatory agency heads like Lincoln went through generals in order to give the American people the government we deserve and the government we've been paying for all along. Our President needs to keep hiring and firing until he, like Lincoln, has found leaders who can create winning organizations. We can't afford any more 9-11's, Hurricane Katrina's or any other massive governmental failures like the near collapse of our nation's financial system.

At this point the SEC desperately needs new leadership at the very top. I feel very sorry for the staff in the eleven (11) Regional Offices for not receiving the proper training, resources, and support from their headquarters over a period of decades. What the SEC headquarters no longer needs is a building full of career bureaucrats shuffling paper. The new SEC Chair needs to come in and clean house with a wide broom, sweeping out the top ranks and bringing in a new, results oriented senior leadership team to replace the one that has failed us so miserably.

My recommendation to the incoming SEC Chairman is to spend one week each month at each of the eleven (11) different Regional Offices during the first year, spending each day that week with a different examination team looking at how they do their jobs. After each day's work has ended, I would take that team out to dinner for a full de-briefing, asking them what tools, training and resources they need to do their jobs better. Once I got back to Washington, I'd crack the whip and make sure my senior staff pushed those tools and resources down to my examination teams on an expedited basis. Senior staff that can't deliver resources to the Regional Offices quickly enough need to be identified and terminated. Examination teams are the tip of the spear and the SEC can only be as good as those teams in the field are, so they must take absolute top priority.

The new SEC Commissioner should consider moving the SEC out of Washington because Washington is a political center not a financial center, so you won't find the most qualified finance people there for the job at hand. Since New York is the world's largest financial center and Boston is the world's fourth largest financial center, moving the SEC to either West Chester County, NY or Connecticut, in between those two major financial centers makes a lot of sense. If the SEC wants to attract the top talent, relocating its headquarters to somewhere between Rye, NY and New Haven, CT is where this agency will best attract the foxes with industry experience it so desperately needs.

If the SEC's senior staff is as bad as it appears to be, then recognize that quickly and move to replace these people expeditiously. Far better to clean house at the top in order to show the new leadership team is serious about bailing out this sinking ship and getting it turned around in the opposite direction. Plus, I would rather have empty desks in Washington versus keeping the dead wood on board; because allowing dead wood to linger sends the wrong message to the Regional Offices. While senior staff positions remain unfilled, promote lower ranking employees into senior roles on an acting basis to discover the up and coming future leaders of this agency. You will identify good talent using this method.

Reinvigorating and reforming the Office of Risk Assessment is another task on the new SEC Commissioner's plate because the SEC needs to put its best, most experienced finance professionals there. New inspection checklists have to be devised for every new financial product, structured product, derivative security, hybrid security, corporate entity – and all before these products are sold into the marketplace! Being even one day late to regulate is simply unacceptable. Examination audit checklists also need to be totally rebuilt so that obvious frauds such as the Madoff Ponzi scheme are never missed again. Base audit checklists for each type of firm that's out there need to be developed. Then, specific additional audit checklists that test for new and different, even never before seen frauds, have to be developed and tested in the field. The Office of Risk Assessment needs to be continually thinking of how to create fraudulent products, how to cook the books more creatively, how to launder money more effectively, and then design effective counter-measures for the examination teams to use.

I also recommend that the SEC Chair require that the examination teams add at least one or more audit steps on top of whatever checklists they've been given using their own imagination and creativity. Those examination team-created audit steps that uncover fraud can then be adopted system-wide. This agency needs every employee making contributions in order to achieve greatness. I would expect the new Chair to demand contributions from all levels of the agency and to listen to all ideas from staff, no matter what their rank or pay grade.

To further increase the SEC's auditing effectiveness, I would organize a "Center for All Lessons Learned (CALL)" similar to what the US Army has been using with great effectiveness for decades. CALL will collect and sort through every fraud that the SEC finds. These frauds would be diagnosed for both common and unique elements so that the odds of future frauds going unchecked are further reduced. I recommend that the SEC adopt the Association of Certified Fraud Examiner's Fraud Tree contained in Volume I of the Certified Fraud Examiner's Manual for use because it lists hundreds of different financial frauds and categorizes them into easy to understand categories and sub-categories. In other words, the SEC needs to shed its "*keystone cops modus operandi*" and quickly turn itself into a "<u>*learning, winning organization*</u>" that instills confidence in all SEC employees, regulated firms and the investing public. CALL would be a password protected, on-line web based resource for all SEC employees to use and, more importantly, to contribute to themselves. The SEC needs to be able to learn at a faster pace than the bad guys they are fighting, and the only way to increase the SEC's decision-making quickly is to demand that all levels of the organization pitch in and contribute their lessons learned. The old top down, command from above approach doesn't work in the modern era and must be abandoned if the SEC is to achieve greatness. The SEC currently has a staff of 3,500 and every single one of those thirty-five hundred brains needs to be turned on and contributing.

Another Office needs to be formed within the SEC similar to the National Transportation Safety Board's accident investigation teams. I would call this the Office the "National Financial Safety Board." MIT Professor Andrew Lo has been advocating this low cost approach to sending in inspection teams after each financial institution blow up to diagnose exactly what went wrong and in what sequence that led these institutions to fail. Whenever a public company, broker/dealer, hedge fund, or registered investment advisor blows up, lets send in an SEC investigation team to collect the valuable lessons learned and add them to the SEC's knowledge base. I recommend that this office's knowledge base be made publicly available on the SEC's website for companies, accountants, and investors to use in preventing whatever blowups can be prevented by avoiding the mistakes of companies that have failed. From the Madoff case alone we have plenty of useful lessons for the public – for example – never allocate more than 20% to any one investment manager, never put 100% of your eggs in one basket, make sure the investment manager uses an independent third party custodian, the proper allocation to hedge funds ranges from 0% - 25% of total assets, etc.

Currently the size and frequency of the blowups is increasing at an alarming rate and the SEC needs to act quickly to turn those numbers in the opposite direction because we can't continue in the direction we've been going for much longer. This National Financial Safety Board would not prevent all future blowups from happening, but if it made our nation's financial system safer and the blow-ups less frequent and of smaller size, then we will all benefit. It is clear that we can't afford 2009 to be worse than 2008 because we barely survived 2008's financial disasters. The time to act on this is now.

Finally, I would add one more Directorate, the Office of the Whistleblower, to centralize the handling and investigation of whistleblower tips. Currently, the SEC's eleven (11) Regional Offices handle whistleblower complaints on an individualized, ad hoc basis. Every whistleblower who comes in with a tip is handled differently and no one tracks the whistleblower with the particular complaint she has brought with the object of the complaint, a particular company or individual. One would think that if ABC Company has received five complaints this year and its nearest competitors received no complaints this year, that this would be meaningful information and merit close scrutiny. Complaints from within industry or by investors have got to be the cheapest, most effective way to identify fraudsters, yet this valuable resource is currently ignored by the SEC. There can be no good reason for dismissing this valuable tool.

If my experience is any guide, the treatment accorded whistleblowers ranges from dismissive to outright unwelcome yet whistleblowers are the best, and cheapest source of great and not so great cases. The great cases cannot be culled from among the many cases submitted if SEC staff does not answer the phone or read its mail. Whistleblowers are the single largest source for fraud detection according to the Association of Certified Fraud Examiner's (ACFE) 2008 Report to the Nation (Chapter 3, page 22, www.acfe.com). According to the ACFE, whistleblower tips were responsible for detecting 54.1% of fraud schemes at public companies whereas external audits account for a meager 4.1% of fraud cases detected (note: the SEC would be considered an external auditor). Therefore whistleblowers are a full thirteen (13) times more effective than the SEC's external audits yet there is no Office of the Whistleblower. Who wouldn't want the SEC to become thirteen (13) times more effective?

The Internal Revenue Service (IRS) started its Office of the Whistleblower in December 2006 and in two short years has grown this office to a staff of 17. The IRS now receives the largest cases with the absolute best quality of evidence in its history. Consider the cost of 17 IRS employees versus the billions in additional tax revenues they'll be responsible for bringing into the US Treasury.

The IRS offers bounty payments to whistleblowers of 15% - 30% for cases that lead to successful recoveries to the US Treasury. These bounty payments do not come out of the IRS's budget nor do the taxpayers pay these bounties. All bounty payments are made by the guilty defendants. Therefore this is a no cost program that funds itself and allows the IRS Staff to cherry pick from the cases that literally walk in the door, selecting the credible cases for immediate investigation.

I recommend that the SEC expand and reinvigorate its almost never used whistleblower bounty program. Section 21A(e) of the 1934 Act allows the SEC to pay a bounty of up to 30% to whistleblowers but only for insider-trading theory cases. The way this works is, the SEC can fine the guilty defendant triple the amount of its ill-gotten gains or losses avoided for insider trading and can award up to ten percent (10%) of the penalty amount to the whistleblower (triple damages x 10% maximum bounty award = 30% potential maximum reward).

Unfortunately, unlike the IRS's Whistleblower Program and the False Claims Act, the SEC's reward payments are not mandatory and the SEC can refuse to pay these rewards without explanation. If Congress would expand this program to include all forms of securities' violations and make the reward payments mandatory, hundreds of cases would likely walk in the door each year, and many of these would be high quality cases that would lead to billions in investor recoveries similar to the billions that the False Claims Act (31 USC Sections 3729-3733) already provides each year.

We have two major government agencies, the Department of Justice and the Internal Revenue Service, that use whistleblower programs to identify cases that they would otherwise know nothing about. Todate false claims act recoveries total over $22 Billion since 1986. For every $1 spent in enforcement, the False Claims Act returns $15 in recoveries from fraudsters. This proves that such a program works and is not a speculative enterprise on the part of the government. . We need the SEC to become as effective as the Department of Justice and the Internal Revenue Service at fraud enforcement.

I recommend that each tip, upon receipt, be logged in, given a case number, and for credible tips with real evidence behind them, the whistleblower and whistleblower's counsel be put in contact with the relevant SEC operating unit that is best able to investigate the complaint. Hopefully this will prevent a repeat of my experiences during the Madoff Case, where over the years I kept submitting better and more detailed case filings but ran into trouble because Boston's SEC Regional Office believed me but New York's SEC Regional Office apparently did not. Standardizing the treatment of whistleblowers to ensure that they are not ignored or mistreated should be a priority for the SEC. An annual reporting to Congress of whistleblower complaints and the SEC's follow-up actions should be mandatory.

Let me add one more important point concerning the issue of self-regulation and whistleblowing: consider that perhaps hundreds of finance professionals around the globe knew that Madoff was a fraudster or at least suspected that he was. How many of these people contacted the SEC with their suspicions? Unfortunately, I may have been the only one. If a whistleblower wanted to, how would they know who to contact at the SEC since there is no "Office of the Whistleblower?" I believe that by adding such an office, we would see honest firms sending in evidence against their crooked competitors. Getting rid of the shysters is in everyone's best interest and restoring trust in the US capital markets is imperative if we are to restore our nation's economy to health. If I'm the CEO of an honest firm and I hire new employees who worked across the street at a competitor and then find out from these new employees that my competitor is dishonest, it would be in my economic self-interest and in the interest of good public policy to turn them into the SEC.

If self-regulation is ever going to work, we need to find ways to advertise it, reward it, and measure it. Currently, the SEC is doing none of the above. Every tool, every resource, and every person has to be brought to bear in the fight against white-collar crime. Government has coddled, accepted, and ignored white-collar crime for too long. It is time the nation woke up and recognized that it's not the armed robbers or drug dealers who cause us the most economic harm, it's the white-collar criminals living in the most expensive homes and who have the most impressive resumes who harm us the most. They steal our pensions, bankrupt our companies, and destroy thousands of jobs, ruining countless lives. No agency is better situated than the SEC to attack high-level white-collar crime. Therefore, the SEC is too important to allow too continue to fail.

Thank you for the opportunity to present my recommendations on how to rebuild the SEC into the world's best securities regulator, it has been a singular honor for me to appear before you today.

Year	NASD	NYSE
2001	Mary L. Schapiro President	Richard Grasso
2002	Mary L. Schapiro President	Richard Grasso
2003	Mary L. Schapiro President	Richard Grasso / John Reed
2004	Mary L. Schapiro President	John A. Thain
2005	Mary L. Schapiro President	John A. Thain
2006	Mary L. Schapiro CEO James S. Shorris EVP Head of Enforcement	John A. Thain
2007*	Mary L. Schapiro CEO Susan L. Merrill, EVP Chief of Enforcement	John A. Thain Duncan L. Niederauer, CEO
2008	Mary L. Schapiro CEO of FINRA	

* NASD and NYSE regulators merge to create FINRA

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	2000	2001	2002	2003	2004	2005	2006	2007	2008
SEC Chairman	**Arthur Levitt**	**Harvey Pitt**	**Harvey Pitt**	**William H. Donaldson**	**William H. Donaldson**	**Christopher Cox**	**Christopher Cox**	**Christopher Cox**	**Christopher Cox**
New York Office	**Wayne M. Carlin** Regional Director	**Wayne M. Carlin** Regional Director	**Wayne M. Carlin** Regional Director	**Mark Schonfeld** Regional Director	**Mark Schonfeld** Regional Director	**Mark Schonfeld** Regional Director	**Mark Schonfeld** Regional Director	**Mark Schonfeld** Regional Director	**James A. Clarkson** Acting Regional Director
Boston Office	**Juan M. Marcelino** District Administrator	**Juan M. Marcelino** District Administrator	**Juan M. Marcelino** District Administrator	**Peter Bresnan** Acting District Administrator	**Walter G. Ricciardi** District Administrator	**Walter G. Ricciardi** District Administrator	**David P. Bergers** District Administrator	**David P. Bergers** District Administrator	**David P. Bergers** District Administrator

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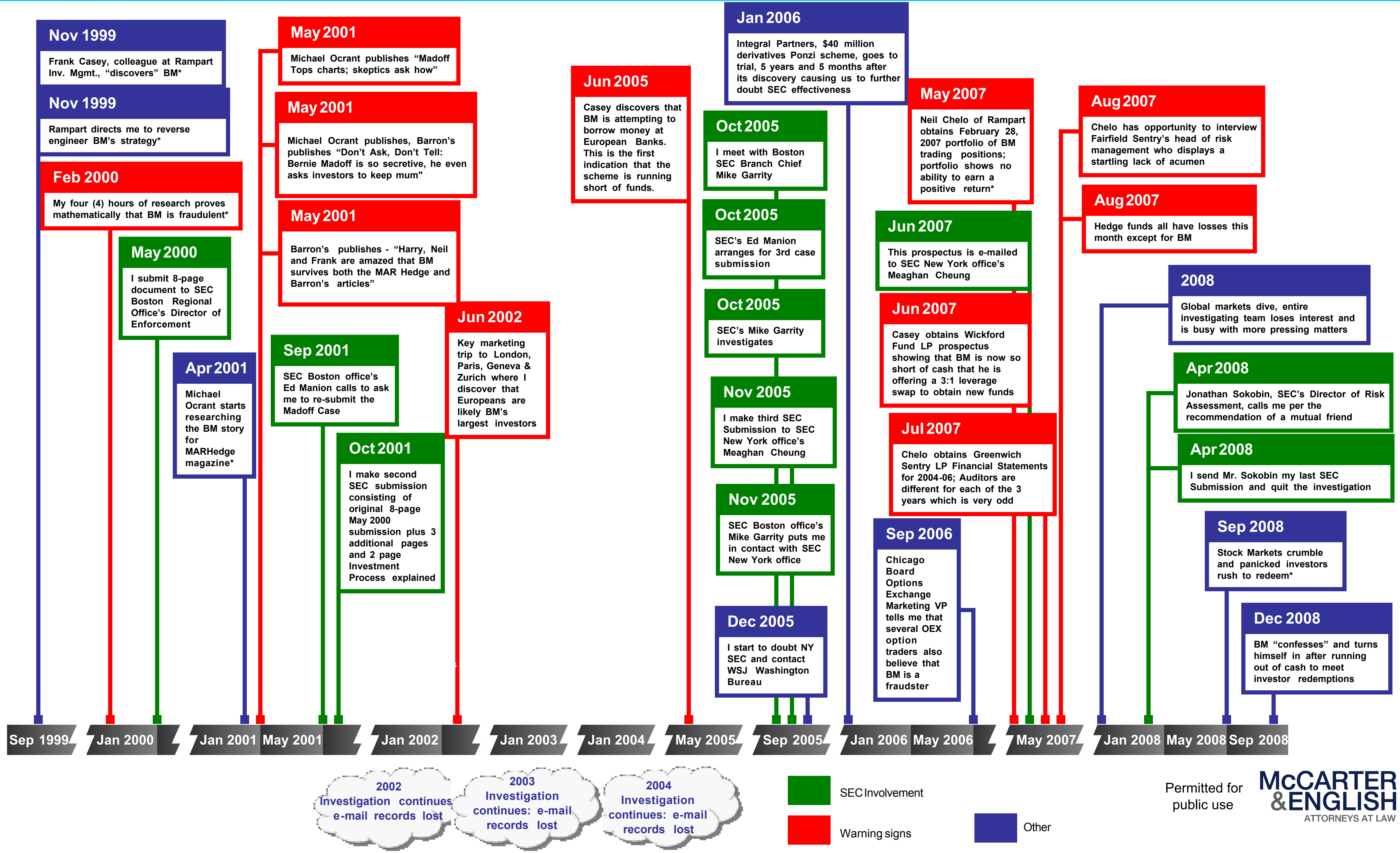
Timeline of Harry Markopolos' Investigation of Madoff Investment Scheme



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McCarter & English (Boston)

112. Attachment 4: Pages 6 and 7 from an offering Memorandum by Fairfield Sent~~er~~ry that was faxed on 3/21/01

113. Attachment 5: May 1, 2001 Article in MAR Hedge

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12/28/2008

Documents included in this PDF File:

1. My formal 8-page presentation to the SEC in May 2000, which includes Exhibit 1.

My comments:

1. At this point in time I have the Ponzi scheme pegged between $3 - $7 billion. But I had just started investigating a few months prior, which is why my range between low and high amounts invested is so large.
2. Ed Manion, CFA, a member of the Boston SEC's staff arranged this meeting, made the introductions and was in the room for the interview.
3. A senior Boston SEC enforcement attorney, Jim Adelman, walked into the room introduced himself and told me that he was about to leave the SEC for a private sector job in industry so that he wouldn't be meeting with me; and that another SEC attorney would be handling the meeting in his place. The second SEC attorney who came into the room was the SEC's New England Regional Director of Enforcement, Attorney Grant Ward. I made my formal presentation to him, leaving him with the documents referenced above. All I can recall is that this fellow didn't understand much, if anything, that I was presenting. He did not seem to have any formal background in finance or the capital markets. How he came to hold that senior of a position at the SEC was a real eye-opener and should have been my first clue that turning in this case to the SEC was a bad idea.
4. I never heard back from the SEC's New England Regional Director of Enforcement, another sign of what was in store for me.
5. Ed Manion and I would chat about Madoff from time to time but I never heard back from the SEC in a formal sense. Mr. Manion and I were curious about what the SEC was doing or if they were even doing anything. We both knew the case would be sent to the SEC's New York Office for investigation. If it hadn't been for Mr. Manion's support and encouragement throughout this entire 8½ year ordeal, I never would have continued to cooperate with the SEC.

Harry Markopolos

Harry Markopolos, CFA, CFE
Chartered Financial Analyst
Certified Fraud Examiner

This was my formal presentation to the SEC's Boston Office

- **Objective:** In 25 minutes or less, I will prove one of three scenario regarding Madoff's Hedge fund operation:

1 They are incredibly talented and/or lucky and I'm an idiot for wasting your time

2 The returns are real, but they are coming from some process other than the one being advertised, in which case an investigation is in order.

3 The entire fund is nothing more than a Ponzi Scheme.

- **Disclosures**

1 My firm has several years of experience with the exact product line being offered by Madoff. We called it PEP for Protected Equity Program. It delivered about 2/3rds of the market return with only 1/3rd of the risk. Unfortunately, people wanted higher returns in the long running bull market and the product was discontinued for lack of customer interest. I find it astounding that Madoff claims to provide 80% of the market's return with only 1/3rd of the risk. These kind of numbers seem beyond the bounds of what is reasonable for such a strategy. In down months, our PEP program experienced losses, albeit smaller losses than the market, whereas Madoff reports only 3 losing months out of 87, a claim I believe impossible to attain with the strategies he advertises.

2 My firm's marketing department has asked our investment department to duplicate Madoff's "split-strike conversion" strategy in the hopes of duplicating their return stream. We know from bitter experience that this is impossible but they won't listen to my firm's investment professionals. Therefore, I don't consider the two firms to be competitors. However, I would like to prove Madoff a fraud so that I don't have to listen to any more nonsense about split-strike conversions being a risk-free absolute return strategy.

3 My firm does not know I am here. I do not want my name released to anyone without my explicit permission.

4 If there is a reward for uncovering fraud, I certainly deserve to be compensated. There is no way the SEC would uncover this on their own. I have almost 13 years in the business and have traded similar type strategies.

5 I used the "Mosaic Theory" of acquiring bits and pieces of information over the past three months to arrive at the conclusions presented herein. I have no inside knowledge or smoking gun" piece of hard evidence.

6 I have not traded on the information being presented.

7 My only hard evidence, is Exhibit 1, a one page document entitled "MANAGER B; The Broyhill All-Weather Fund, L.P." I have chosen to break down Exhibit 1 into four parts, A, B, C, D and have labeled them accordingly

8 Some of my presentation is based upon third party representations made by people affiliated with hedge fund, fund of funds, who have considerable assets invested with Madoff. They continually brag about their returns, how they are generated from access to order flow, and how Madoff gains almost perfect market knowledge based upon access to order flow. I have included the hearsay remarks in the last section of my prepared remarks, since I realize the information while useful in painting a broad picture, is not enough by itself to base an SEC enforcement action upon.

need sell 3 short 5% OTM calls Δ .333 = -.999

Long stock +1

◆ **Exhibit 1 Exposed**

need to buy 3 long 5% OTM puts Δ -.333 = +.999

1 **Returns can't be coming from net long exposure to the market:** Part A, a split-strike conversion is long 30 – 35 stocks that track the 100 stock OEX index, short out-of-the-money (Delta < .5) OEX index call options, and long out-of-the-money (delta < -.5) OEX index put options. Part A describes a strategy that is net long stock. This means that if the market drops, this strategy loses money. However, in Part D, they show a .06 Correlation to the S&P 500's Beta. Equating Beta to Delta, we must infer that Madoff is not really net long, but somehow delta hedging with options. **Conclusion:** Madoff's returns cannot be coming from the market's action as evidenced by their reported .06 correlation (Part D) to the S&P 500 index.

2 **Not enough options exist in open interest:** Somewhere between \$3 - \$7 plus billion are allocated to this strategy, of which Broyhill Asset Management, LLC represents only \$350 million. Call option open interest on the Chicago Board Option Exchange as of the Tuesday, May 2, 2000 close was only 102,745 contracts, representing \$7.9 billion (102,745 contracts x \$100 contract multiplier x 776.75 closing OEX index value on May 2nd). May 2nd's OEX put option open interest was \$9.5 billion (122,731 put contracts x \$100 contract multiplier x 776.75 closing OEX index value on May 2nd) . Part A, 1st paragraph, last sentence, explicitly states, "The amount of calls that are sold and puts that are bought represent a dollar amount equal to the basket of shares purchased." However, these are all out-of-the-money options (Part A, 1st paragraph, 2nd to last sentence), and delta hedging takes place, which would require lots of options trading and lots of options in open interest. More low delta calls and puts would need to be utilized to delta hedge than currently exist in open interest. **Conclusion:** This hedging cannot be taking place as described. And, if only \$3 billion are allocated to this strategy, then there still aren't enough options in open interest for this type of hedging to occur, since Madoff would be at least 1/3rd of the open interest, and we know that's not the case. If a firm gets to be too big a part of any contracts open interest, it will be squashed like a bug by the market-makers.

3 **Performance Chart is Misleading:** Part C. Notice the Cumulative Performance Chart of Manager B is almost a straight line, rising at roughly a 45 degree angle. This chart absolutely cannot be cumulative in the common usage of the term for reporting purposes, which means "geometric returns." This chart must be some sort of arithmetic average sum, since a true cumulative return line, given the returns presented in Part B, would be exponentially rising (i.e. curved upward, at an increasing rate). **Conclusion:** The chart in Part C is misleading and the manager is misrepresenting results.

4 **Where exactly do the returns come from?:** Part B. Hopefully I've at least raised doubt in your mind that Madoff's returns cannot be coming from the market if the correlation to the S&P 500 Beta is only .06. I think I proved quite convincingly that there are not enough OEX options in existence to hedge a \$3 - \$7 billion portfolio. In Part A, second paragraph, last sentence, reads, "The collection of dividends on the basket of stocks constitutes an integral part of the strategy." The word "integral" sounds good, but the OEX index yields only .94%

a year. **Question:** If his returns did not come from the stock market (.06 correlation to the S&P 500) and they didn't come from the options hedging (not enough contracts exist), then where did the returns come from if the underlying index yields only .94%?

5. My firm's experience with its PEP Product do not support Madoff's claims in Part B. I find it astounding that Madoff claims to provide 80% of the market's return with only 1/3rd of the risk. My firm's ten years of actual return history with its PEP product or products similar to PEP and to Madoff, realized about 2/3rds of the markets return with about 1/3rd of the risk. Madoff's number of losing months seems beyond the bounds of what is reasonable for such a strategy. In down months, our PEP program experienced losses, albeit smaller losses than the market, whereas Madoff reports only 3 losing months out of 87, a claim I believe impossible to obtain using option income strategies. In August 1998, in the midst of the Russian Default and the Long Term Capital Management twin crises, the S&P 500 dropped 14.58%, yet Madoff earned .30%. In January 2000, the S&P 500 dropped 5.09%, yet Madoff earned 2.72%. Our current product test portfolios do not support this, and we sell, higher priced individual call options in our strategy, which should earn more money in down markets than the lower priced index calls supposedly sold by Madoff.

6. Madoff's returns are not consistent with a publicly traded option income fund: Part B. Only 3 down months vs. the market's down 26 months during the 87 month time period presented. The low .06 correlation in Part D supports this, but the method given for return generation are not possible or even plausible. Obviously there are not enough options in existence to delta hedge Madoff's long stock position. Madoff's returns are not consistent with the only Option Income Fund that I know of that still trades on an exchange. A comparison of annual returns is listed below (data courtesy of Bloomberg, GATEX equity DES, page 3):

Year	Gateway	Madoff	S&P 500
1993	7.40	14.55	10.06
1994	5.57	13.12	1.33
1995	11.04	16.68	37.62
1996	10.83	15.96	22.96
1997	12.04	16.52	33.38
1998	12.26	15.83	28.58
1999	12.97	16.69	21.04
Annualized	10.27	15.62	19.58

Conclusion: The Madoff hedge fund returns are inconsistent with a publicly traded mutual fund using a similar stated return methodology. These returns are also inconsistent with a fund having a .06 (i.e. very little net long market exposure) correlation to the S&P 500.

♦ **HEARSAY** from several sources, all of whom are fund of fund operators with investment with Madoff's hedge fund. As you know, every Ponzi Scheme has to be "a hook" or "a story" about how really great returns are being generated.

1. **Non-existence of ECN's prior to 1998:** Madoff makes verbal claims to his investors that access to their internal order flow, which Madoff pays for, is a substantial part of the return generating process. If this is true, then where did the returns come from in the years 1993 – 1998, prior to the ascendance of ECN's? Presumably, prior to 1998, Madoff only had access to order flow on the NASDAQ which he paid for. He would have no such advantage pre-1998, on the stocks listed (Part A, 1st paragraph, sentences 3 & 4).

2. **Payment for Order Flow:** People I know who have invested with Madoff are being told that the returns are really coming from access to the Madoff B/D's internalization of order flow. If Madoff chooses to transfer the profits from the "free options" associated with his internalization of order flow to his hedge fund clients, we can easily measure the value of having access to internal order flow by using the Black Scholes Model. Current realized annualized volatility of the stocks within the OEX index is approximately 50%, the current treasury bill rate is 5.80%, the average stock price is approximately $46. Using the current index date, the value of an at-the-money call option over the relevant time intervals of 1 minute, 5 minutes, 10 minutes, and 15 minutes appears in the chart below.

1 minute	5 minutes	10 minutes	15 minutes
3 cents	7 cents	10 cents	12 cents

- Note: cap-weighted OEX component volatility is approximately 50% annualized. I used a 253 day trading year. The SEC should be able to duplicate these results using Black-Scholes
- There is value to having access to order flow. This is in the academic literature. If I know my customers are heavy buyers of ABC Stock at 50, I can, with relative safety, purchase ABC Stock at 50.125, and risk only a 1/8th loss on the trade with some high probability. If the stock rises, I win. If it drops, I lose, but only a little. The pattern or returns is positively skewed and leads to excellent short term profits if the process can be frequently repeated.

Conclusion: Madoff's returns may be accurate, but maybe he is generating them by subsidizing his hedge fund returns by disadvantaging his broker/dealer's customer order flow. In other words, he's not providing "best execution" to his B/D customers. Is this disclosed and do his B/D customers know they are being disadvantaged? Is payment for order flow a conflict of interest when a manager takes the "free options" granted by access to order flow?

Even Worse Possibility: Madoff engages in "ticket-splitting" whereby bad fills go to the customers and good fills are allocated to the Hedge Fund. Only a close review of the time stamps and comparison to the customer records will reveal whether this is happening.

3. **Madoff is really only borrowing money from its investors at 15 ½ %:** We've had two investors tell us that Madoff is actually making a lot more money on its trades than 15 ½ % per year and that they only pass along the 15 ½ % returns as "the cost of money." My

response is why pay 15.5% interest for such a stable, low volatility investment strategy? Surely a rate of LIBOR + some more reasonable spread would result in much lower interest rates. That is of course, unless you wanted to avoid having rating agencies such as Moody's or S&P come in and look at your firm.

4. **Madoff subsidizes down months:** Hard to believe, but I've heard two investors tell me that they don't believe Madoff can make money in big down months either. However, they tell me that Madoff "subsidizes" their investors in down months, so that they will be able to show low volatility of returns. These types of stories are typical of Ponzi Schemes. These investors tell me, with straight faces, that Madoff only books winning tickets in their accounts and "eats" the losers in months where the market sells off hard.

5. **Madoff has perfect market-timing ability:** One investor told me that Madoff went 100% to cash in July 1998 and December 1999, ahead of market declines. He told me that he knows this because Madoff faxes his trade tickets to his firm and the custodial bank. However, Madoff also owns the B/D that generates the trade tickets, so that collusion between Madoff's B/D and Madoff's hedge fund could take place.

6. **Madoff does not allow outside performance audits:** One London based fund of funds representing Arab money, during the due diligence process, asked to send in a team of Big Six accountants to verify performance. They were told no, that only Madoff's brother is allowed to audit performance for reasons of secrecy. Amazingly, this London based fund of funds invested over $200 million of their Arab client's money anyway, because the low volatility of returns was so attractive.

Concluding Remarks:

I am an expert in the field. I have doubts about Madoff's returns being true based upon the discrepancies noted in Exhibit 1. Combining the discrepancies I've noted in Exhibit 1, with the hearsay I've heard, seems to fit in with the patterns commonly found in Ponzi Schemes. Having a broker/dealer subsidiary that is also an ECN, which is then able to generate false trading tickets would also be a huge advantage. Not allowing external auditors in to verify performance would also be something a Ponzi Scheme operator would do. I have no hard evidence of fraud, just suspicions that things are not what they seem inside of Madoff. If he is generating those excellent returns, and he may well be, it is not with index option based strategies. I believe an SEC visit is warranted.

I have reviewed my suspicions with a world famous and extremely well published market professional. He concurs that this needs to be looked at. I have reviewed my suspicions with the head of one of the top professional finance organizations in the world and he concurs that this needs to be looked at. Not a single derivatives professional at my firm believes Madoff's performance numbers, yet only I have chosen to speak out, and at great risk to my professional career.

N	Month	Net Return		S&P 500 Price Index	S&P 500 Price Return	S&P 500 Price Return
1	January-93	1.44%		438.78		
2	February-93	1.17%		443.38	1.05%	
3	March-93	1.96%		451.67	1.87%	
4	**April-93**	**-1.44%**		440.19	-2.54%	
5	May-93	2.14%		450.19	2.27%	
6	June-93	1.01%		450.53	0.08%	
7	July-93	1.41%		448.13	-0.53%	
8	August-93	3.01%		463.56	3.44%	
9	September-93	0.02%		458.93	-1.00%	
10	October-93	2.09%		467.83	1.94%	
11	November-93	0.22%		461.79	-1.29%	
12	December-93	0.71%	14.55%	466.45	1.01%	7.06%
13	January-94	1.76%		481.61	3.25%	
14	**February-94**	**-0.03%**		467.14	-3.00%	
15	March-94	1.84%		445.77	-4.57%	
16	April-94	1.86%		450.91	1.15%	
17	May-94	0.88%		456.41	1.22%	
18	June-94	0.36%		444.27	-2.66%	
19	July-94	1.98%		458.26	3.15%	
20	August-94	0.70%		475.50	3.76%	
21	September-94	0.71%		462.71	-2.69%	
22	October-94	2.02%		472.35	2.08%	
23	**November-94**	**-0.44%**		453.69	-3.95%	
24	December-94	0.79%	13.12%	459.27	1.23%	-1.54%
25	January-95	1.83%		470.42	2.43%	
26	February-95	1.03%		487.39	3.61%	
27	March-95	1.09%		500.71	2.73%	
28	April-95	1.81%		514.71	2.80%	
29	May-95	2.07%		533.40	3.63%	
30	June-95	0.57%		544.75	2.13%	
31	July-95	1.19%		562.06	3.18%	
32	August-95	0.08%		561.88	-0.03%	
33	September-95	2.15%		584.41	4.01%	
34	October-95	1.88%		581.50	-0.50%	
35	November-95	1.12%		605.37	4.10%	
36	December-95	0.73%	16.68%	615.93	1.74%	34.11%
37	January-96	1.75%		636.02	3.26%	
38	February-96	0.85%		640.43	0.69%	
39	March-96	1.71%		645.50	0.79%	
40	April-96	0.72%		654.17	1.34%	
41	May-96	1.83%		669.12	2.29%	
42	June-96	0.27%		670.63	0.23%	
43	July-96	2.37%		639.95	-4.57%	
44	August-96	0.35%		651.99	1.88%	
45	September-96	1.33%		687.31	5.42%	
46	October-96	1.35%		705.27	2.61%	
47	November-96	1.93%		757.02	7.34%	
48	December-96	0.47%	15.96%	740.74	-2.15%	20.26%
49	January-97	3.08%		786.16	6.13%	

N	Month	Net Return		S&P 500 Price Index	S&P 500 Price Return	S&P 500 Price Return
50	February-97	0.92%		790.82	0.59%	
51	March-97	0.90%		757.12	-4.26%	
52	April-97	1.85%		801.34	5.84%	
53	May-97	0.90%		848.28	5.86%	
54	June-97	1.50%		885.14	4.35%	
55	July-97	0.87%		954.29	7.81%	
56	August-97	0.43%		899.47	-5.74%	
57	September-97	2.23%		947.28	5.32%	
58	October-97	0.51%		914.62	-3.45%	
59	November-97	1.77%		955.40	4.46%	
60	December-97	0.46%	16.52%	970.43	1.57%	31.00%
61	January-98	1.04%		980.28	1.02%	
62	February-98	1.58%		1049.34	7.04%	
63	March-98	2.11%		1101.75	4.99%	
64	April-98	0.45%		1111.75	0.91%	
65	May-98	2.15%		1090.82	-1.88%	
66	June-98	1.58%		1133.84	3.94%	
67	July-98	1.05%		1120.67	-1.16%	
68	August-98	0.30%		957.28	-14.58%	
69	September-98	1.11%		1017.01	6.24%	
70	October-98	2.26%		1098.67	8.03%	
71	November-98	1.00%		1163.63	5.91%	
72	December-98	0.18%	15.83%	1229.23	5.64%	26.67%
73	January-99	2.41%		1279.64	4.10%	
74	February-99	0.17%		1238.33	-3.23%	
75	March-99	2.50%		1286.37	3.88%	
76	April-99	1.42%		1335.18	3.79%	
77	May-99	1.15%		1301.84	-2.50%	
78	June-99	2.27%		1372.71	5.44%	
79	July-99	0.46%		1328.72	-3.20%	
80	August-99	1.06%		1320.41	-0.63%	
81	September-99	0.94%		1282.71	-2.86%	
82	October-99	1.28%		1362.93	6.25%	
83	November-99	1.50%		1388.91	1.91%	
84	December-99	0.41%	16.69%	1469.25	5.78%	19.52%
85	January-00	2.72%		1394.46	-5.09%	
86	February-00	0.17%		1366.42	-2.01%	
87	March-00	2.90%		1498.58	9.67%	

	Madoff	S&P500	Comps
Monthly Standard Deviation	0.83%	3.86%	4.6 X's
Average Monthly Return	1.24%	1.51%	1.2 X's
Annual Standard Deviation	4.32%	12.88%	3.0 X's
Average Annual Return	15.62%	19.58%	1.25 X's
Return / Risk Ratio	**3.62**	**1.52**	
# of down Months	3	26	8.7 X's
Percentage Down Months	3.4%	29.9%	

Exhibit 1

MANAGER B

The Broyhill All-Weather Fund, L.P.

(A)

Strategy Which is pure Madoff where Broyhill markets Madoff

The Manager's investment objective is long term growth on a consistent basis with low volatility. The investment advisor inv exclusively in the U.S. and utilizes a strategy often referred to as a "split-strike conversion." Generally this style invo purchasing a basket of 30 to 35 large-capitalization stocks with a high degree of correlation to the general market (e.g. Amer Express, Boeing, Citicorp, Coca-Cola, Dupont, Exxon, General Motors, IBM Merck, McDonald's). To provide the desired he the manager then sells out-of-the-money OEX index call options and buys out-of-the-money OEX index put options. The am of calls that are sold and puts that are bought represent a dollar amount equal to the basket of shares purchased.

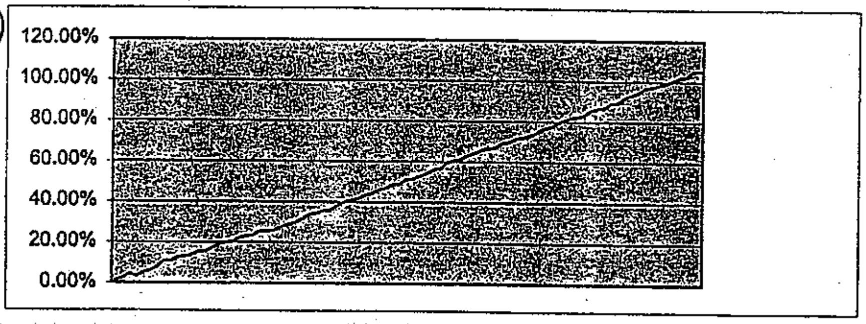
A proprietary computer system continuously optimizes the basket of stocks to replicate and enhance the performance of account relative to the overall market (S&P). The put and call option positions are actively managed as strike prices and matu dates are adjusted relative to general market movements and valuations. The collection of dividends on the basket of stc constitutes an integral part of the strategy.

Net Monthly Percent Returns

(B)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sept	Oct	Nov	Dec	YTD
1993	1.44%	1.17%	1.96%	-1.44%	2.14%	1.01%	1.41%	3.01%	0.02%	2.09%	0.22%	0.71%	14.55%
1994	1.76%	-0.03%	1.84%	1.86%	0.88%	0.36%	1.98%	0.70%	0.71%	2.02%	-0.44%	0.79%	13.12%
1995	1.83%	1.03%	1.09%	1.81%	2.07%	0.57%	1.19%	0.08%	2.15%	1.88%	1.12%	0.73%	16.68%
1996	1.75%	0.85%	1.71%	0.72%	1.83%	0.27%	2.37%	0.35%	1.33%	1.35%	1.93%	0.47%	15.96%
1997	3.08%	0.92%	0.90%	1.85%	0.90%	1.50%	0.87%	0.43%	2.23%	0.51%	1.77%	0.46%	16.52%
1998	1.04%	1.58%	2.11%	0.45%	2.15%	1.58%	1.05%	0.30%	1.11%	2.26%	1.00%	0.18%	15.83%
1999	2.41%	0.17%	2.50%	1.42%	1.15%	2.27%	0.46%	1.06%	0.94%	1.28%	1.50%	0.41%	16.69%
2000	2.72%	0.17%	2.90%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	5.88%

(C)



Cumulative Performance of Manager B

(D) Background

The Broyhill All-Weather Fund, L.P., has allocated funds to a Single Manager Limited Partnership (the "Partnership"). T Partnership's parent company is a public company and together with its subsidiaries provides investment consulting advice financial institutions, endowments, and public funds of over $2.3 billion in client assets. The General Partner does not mana the assets directly but allocates them to Manager B.

Annual Compound Return	15.50%
Annualized Standard Deviation	4.32%
Correlation to S&P 500 Beta	0.06
% Positive Months	96.55%
Sharp Ratio	3.54

Manager B
Assets Under Management
$ 350,000,000

N W E S

Broyhill Asset Management, LLC

October 2001 SEC Transmittal Cover Page

Date: 12/28/2008

Documents included in the PDF File:

1. My Original 8-page May 2000 SEC Submission
2. A 3-page update including a diagram of how I believe Madoff is operating his Ponzi Scheme
3. A 2-page fax I received on March 29, 2001 from a source that I can't remember that is marked Re: Madoff Investment Process explained.

My comments:

1. In May 2000 I pegged Madoff running between a $3 - $7 billion plus Ponzi Scheme. By October 2001, after identifying additional hedge fund of fund third party marketers for Madoff, I felt confident enough to up the amount of money involved to between $12 - $20 billion.

2. In my diagram I totally missed a key fact that, in retrospect, would have provided me with clearer proof of the fraud. Bernie Madoff self-custodied his assets under management! There was no legitimate custodian clearing his trades. One would have thought investors would have wanted to see one of the Big Three custody banks such as State Street, Mellon or Northern Trust taking custody of their assets not their asset manager! This is about as clear a breach of fiduciary duty as one can have. Letting the people who invest the money have unfettered access to the money without any internal or external controls is a recipe for fraud. How did so many regulators and fiduciaries miss this? I'm as eager to find out as anyone.

3. The 3-page update is not the same one as was submitted to the SEC. The 3-page update I submitted to the SEC had the blanks under "Reality:" point 5 filled in with actual figures that I calculated using the Black-Scholes Options Pricing Model. I probably have it in my files but can't seem to locate it given the vast amount of paper there is to go through.

4. Ed Manion, CFA, of the SEC's Boston Office called me up in October 2001 asking me to resubmit the Madoff case because he thought the SEC had dropped the ball the first time I gave them the case. I think all I did was send in my original submission along with 3 pages of new, updated material plus the 2-page Madoff Investment Process explained fax. I don't recall ever going to any in-person meetings at the SEC with this update. I think it was something where Boston just sends my fax to the New York Office and they investigate based upon what was received in the fax. I know that the SEC's New York Office never called me to come in and interview and I only heard

back from Ed Manion on the case where he was frustrated because the case didn't seem to be getting traction within the SEC.

Harry Markopolos

Harry Markopolos, CFA, CFE
Chartered Financial Analysts
Certified Fraud Examiners

This was my formal presentation to the SEC's Boston Office

- **Objective:** In 25 minutes or less, I will prove one of three scenario regarding Madoff's Hedge fund operation:

1 They are incredibly talented and/or lucky and I'm an idiot for wasting your time

2 The returns are real, but they are coming from some process other than the one being advertised, in which case an investigation is in order.

3 The entire fund is nothing more than a Ponzi Scheme.

- **Disclosures**

1 My firm has several years of experience with the exact product line being offered by Madoff. We called it PEP for Protected Equity Program. It delivered about 2/3rds of the market return with only 1/3rd of the risk. Unfortunately, people wanted higher returns in the long running bull market and the product was discontinued for lack of customer interest. I find it astounding that Madoff claims to provide 80% of the market's return with only 1/3rd of the risk. These kind of numbers seem beyond the bounds of what is reasonable for such a strategy. In down months, our PEP program experienced losses, albeit smaller losses than the market, whereas Madoff reports only 3 losing months out of 87, a claim I believe impossible to attain with the strategies he advertises.

2 My firm's marketing department has asked our investment department to duplicate Madoff's "split-strike conversion" strategy in the hopes of duplicating their return stream. We know from bitter experience that this is impossible but they won't listen to my firm's investment professionals. Therefore, I don't consider the two firms to be competitors. However, I would like to prove Madoff a fraud so that I don't have to listen to any more nonsense about split-strike conversions being a risk-free absolute return strategy.

3 My firm does not know I am here. I do not want my name released to anyone without my explicit permission.

4 If there is a reward for uncovering fraud, I certainly deserve to be compensated. There is no way the SEC would uncover this on their own. I have almost 13 years in the business and have traded similar type strategies.

5 I used the "Mosaic Theory" of acquiring bits and pieces of information over the past three months to arrive at the conclusions presented herein. I have no inside knowledge or smoking gun" piece of hard evidence.

6 I have not traded on the information being presented.

7 My only hard evidence, is Exhibit 1, a one page document entitled "MANAGER B; The Broyhill All-Weather Fund, L.P." I have chosen to break down Exhibit 1 into four parts, A, B, C, D and have labeled them accordingly

8 Some of my presentation is based upon third party representations made by people affiliated with hedge fund, fund of funds, who have considerable assets invested with Madoff. They continually brag about their returns, how they are generated from access to order flow, and how Madoff gains almost perfect market knowledge based upon access to order flow. I have included the hearsay remarks in the last section of my prepared remarks, since I realize the information while useful in painting a broad picture, is not enough by itself to base an SEC enforcement action upon.

need sell 3 short 5% OTM calls Δ .333 = -.999

Long stock +1

♦ **Exhibit 1 Exposed**

need to buy 3 long 5% OTM puts Δ -.333 = +.999

1 **Returns can't be coming from net long exposure to the market:** Part A, a split-strike conversion is long 30 – 35 stocks that track the 100 stock OEX index, short out-of-the-money (Delta < .5) OEX index call options, and long out-of-the-money (delta ~~<~~ -.5) OEX index put options. Part A describes a strategy that is net long stock. This means that if the market drops, this strategy loses money. However, in Part D, they show a .06 Correlation to the S&P 500's Beta. Equating Beta to Delta, we must infer that Madoff is not really net long, but somehow delta hedging with options. **Conclusion:** Madoff's returns cannot be coming from the market's action as evidenced by their reported .06 correlation (Part D) to the S&P 500 index.

2 **Not enough options exist in open interest:** Somewhere between \$3 - \$7 plus billion are allocated to this strategy, of which Broyhill Asset Management, LLC represents only \$350 million. Call option open interest on the Chicago Board Option Exchange as of the Tuesday, May 2, 2000 close was only 102,745 contracts, representing \$7.9 billion (102,745 contracts x \$100 contract multiplier x 776.75 closing OEX index value on May 2nd). May 2nd's OEX put option open interest was \$9.5 billion (122,731 put contracts x \$100 contract multiplier x 776.75 closing OEX index value on May 2nd) . Part A, 1st paragraph, last sentence, explicitly states, "The amount of calls that are sold and puts that are bought represent a dollar amount equal to the basket of shares purchased." However, these are all out-of-the-money options (Part A, 1st paragraph, 2nd to last sentence), and delta hedging takes place, which would require lots of options trading and lots of options in open interest. More low delta calls and puts would need to be utilized to delta hedge than currently exist in open interest. **Conclusion:** This hedging cannot be taking place as described. And, if only \$3 billion are allocated to this strategy, then there still aren't enough options in open interest for this type of hedging to occur, since Madoff would be at least 1/3rd of the open interest, and we know that's not the case. If a firm gets to be too big a part of any contracts open interest, it will be squashed like a bug by the market-makers.

3 **Performance Chart is Misleading:** Part C. Notice the Cumulative Performance Chart of Manager B is almost a straight line, rising at roughly a 45 degree angle. This chart absolutely cannot be cumulative in the common usage of the term for reporting purposes, which means "geometric returns." This chart must be some sort of arithmetic average sum, since a true cumulative return line, given the returns presented in Part B, would be exponentially rising (i.e. curved upward, at an increasing rate). **Conclusion:** The chart in Part C is misleading and the manager is misrepresenting results.

4 **Where exactly do the returns come from?:** Part B. Hopefully I've at least raised doubt in your mind that Madoff's returns cannot be coming from the market if the correlation to the S&P 500 Beta is only .06. I think I proved quite convincingly that there are not enough OEX options in existence to hedge a \$3 - \$7 billion portfolio. In Part A, second paragraph, last sentence, reads, "The collection of dividends on the basket of stocks constitutes an integral part of the strategy." The word "integral" sounds good, but the OEX index yields only .94%

a year. **Question:** If his returns did not come from the stock market (.06 correlation to the S&P 500) and they didn't come from the options hedging (not enough contracts exist), then where did the returns come from if the underlying index yields only .94%?

5. My firm's experience with its PEP Product do not support Madoff's claims in Part B. I find it astounding that Madoff claims to provide 80% of the market's return with only 1/3rd of the risk. My firm's ten years of actual return history with its PEP product or products similar to PEP and to Madoff, realized about 2/3rds of the markets return with about 1/3rd of the risk. Madoff's number of losing months seems beyond the bounds of what is reasonable for such a strategy. In down months, our PEP program experienced losses, albeit smaller losses than the market, whereas Madoff reports only 3 losing months out of 87, a claim I believe impossible to obtain using option income strategies. In August 1998, in the midst of the Russian Default and the Long Term Capital Management twin crises, the S&P 500 dropped 14.58%, yet Madoff earned .30%. In January 2000, the S&P 500 dropped 5.09%, yet Madoff earned 2.72%. Our current product test portfolios do not support this, and we sell, higher priced individual call options in our strategy, which should earn more money in down markets than the lower priced index calls supposedly sold by Madoff.

6. Madoff's returns are not consistent with a publicly traded option income fund: Part B. Only 3 down months vs. the market's down 26 months during the 87 month time period presented. The low .06 correlation in Part D supports this, but the method given for return generation are not possible or even plausible. Obviously there are not enough options in existence to delta hedge Madoff's long stock position. Madoff's returns are not consistent with the only Option Income Fund that I know of that still trades on an exchange. A comparison of annual returns is listed below (data courtesy of Bloomberg, GATEX equity DES, page 3):

Year	Gateway	Madoff	S&P 500
1993	7.40	14.55	10.06
1994	5.57	13.12	1.33
1995	11.04	16.68	37.62
1996	10.83	15.96	22.96
1997	12.04	16.52	33.38
1998	12.26	15.83	28.58
1999	12.97	16.69	21.04
Annualized	10.27	15.62	19.58

Conclusion: The Madoff hedge fund returns are inconsistent with a publicly traded mutual fund using a similar stated return methodology. These returns are also inconsistent with a fund having a .06 (i.e. very little net long market exposure) correlation to the S&P 500.

♦ **HEARSAY** from several sources, all of whom are fund of fund operators with investment with Madoff's hedge fund. As you know, every Ponzi Scheme has to be "a hook" or "a story" about how really great returns are being generated.

1. **Non-existence of ECN's prior to 1998:** Madoff makes verbal claims to his investors that access to their internal order flow, which Madoff pays ~~for, is a substantial~~ part of the return generating process. If this is true, then where did the returns come from in the years 1993 – 1998, prior to the ascendance of ECN's? Presumably, prior to 1998, Madoff only had access to order flow on the NASDAQ which he paid for. He would have no such advantage pre-1998, on the stocks listed (Part A, 1st paragraph, sentences 3 & 4).

2. **Payment for Order Flow**: People I know who have invested with Madoff are being told that the returns are really coming from access to the Madoff B/D's internalization of order flow. If Madoff chooses to transfer the profits from the "free options" associated with his internalization of order flow to his hedge fund clients, we can easily measure the value of having access to internal order flow by using the Black Scholes Model. Current realized annualized volatility of the stocks within the OEX index is approximately 50%, the current treasury bill rate is 5.80%, the average stock price is approximately $46. Using the current index date, the value of an at-the-money call option over the relevant time intervals of 1 minute, 5 minutes, 10 minutes, and 15 minutes appears in the chart below.

1 minute	5 minutes	10 minutes	15 minutes
3 cents	7 cents	10 cents	12 cents

- Note: cap-weighted OEX component volatility is approximately 50% annualized. I used a 253 day trading year. The SEC should be able to duplicate these results using Black-Scholes
- There is value to having access to order flow. This is in the academic literature. If I know my customers are heavy buyers of ABC Stock at 50, I can, with relative safety, purchase ABC Stock at 50.125, and risk only a 1/8th loss on the trade with some high probability. If the stock rises, I win. If it drops, I lose, but only a little. The pattern or returns is positively skewed and leads to excellent short term profits if the process can be frequently repeated.

Conclusion: Madoff's returns may be accurate, but maybe he is generating them by subsidizing his hedge fund returns by disadvantaging his broker/dealer's customer order flow. In other words, he's not providing "best execution" to his B/D customers. Is this disclosed and do his B/D customers know they are being disadvantaged? Is payment for order flow a conflict of interest when a manager takes the "free options" granted by access to order flow?

Even Worse Possibility: Madoff engages in "ticket-splitting" whereby bad fills go to the customers and good fills are allocated to the Hedge Fund. Only a close review of the time stamps and comparison to the customer records will reveal whether this is happening.

3. **Madoff is really only borrowing money from its investors at 15 ½ %:** We've had two investors tell us that Madoff is actually making a lot more money on its trades than 15 ½ % per year and that they only pass along the 15 ½ % returns as "the cost of money." My

response is why pay 15.5% interest for such a stable, low volatility investment strategy? Surely a rate of LIBOR + some more reasonable spread would result in much lower interest rates. That is of course, unless you wanted to avoid having rating agencies such as Moody's or S&P come in and look at your firm.

4. **Madoff subsidizes down months:** Hard to believe, but I've heard two investors tell me that they don't believe Madoff can make money in big down months either. However, they tell me that Madoff "subsidizes" their investors in down months, so that they will be able to show low volatility of returns. These types of stories are typical of Ponzi Schemes. These investors tell me, with straight faces, that Madoff only books winning tickets in their accounts and "eats" the losers in months where the market sells off hard.

5. **Madoff has perfect market-timing ability:** One investor told me that Madoff went 100% to cash in July 1998 and December 1999, ahead of market declines. He told me that he knows this because Madoff faxes his trade tickets to his firm and the custodial bank. However, Madoff also owns the B/D that generates the trade tickets, so that collusion between Madoff's B/D and Madoff's hedge fund could take place.

6. **Madoff does not allow outside performance audits:** One London based fund of funds representing Arab money, during the due diligence process, asked to send in a team of Big Six accountants to verify performance. They were told no, that only Madoff's brother is allowed to audit performance for reasons of secrecy. Amazingly, this London based fund of funds invested over $200 million of their Arab client's money anyway, because the low volatility of returns was so attractive.

Concluding Remarks:

I am an expert in the field. I have doubts about Madoff's returns being true based upon the discrepancies noted in Exhibit 1. Combining the discrepancies I've noted in Exhibit 1, with the hearsay I've heard, seems to fit in with the patterns commonly found in Ponzi Schemes. Having a broker/dealer subsidiary that is also an ECN, which is then able to generate false trading tickets would also be a huge advantage. Not allowing external auditors in to verify performance would also be something a Ponzi Scheme operator would do. I have no hard evidence of fraud, just suspicions that things are not what they seem inside of Madoff. If he is generating those excellent returns, and he may well be, it is not with index option based strategies. I believe an SEC visit is warranted.

I have reviewed my suspicions with a world famous and extremely well published market professional. He concurs that this needs to be looked at. I have reviewed my suspicions with the head of one of the top professional finance organizations in the world and he concurs that this needs to be looked at. Not a single derivatives professional at my firm believes Madoff's performance numbers, yet only I have chosen to speak out, and at great risk to my professional career.

N	Month	Net Return		S&P 500 Price Index	S&P 500 Price Return	S&P 500 Price Return
1	January-93	1.44%		438.78		
2	February-93	1.17%		443.38	1.05%	
3	March-93	1.96%		451.67	1.87%	
4	**April-93**	**-1.44%**		440.19	-2.54%	
5	May-93	2.14%		450.19	2.27%	
6	June-93	1.01%		450.53	0.08%	
7	July-93	1.41%		448.13	-0.53%	
8	August-93	3.01%		463.56	3.44%	
9	September-93	0.02%		458.93	-1.00%	
10	October-93	2.09%		467.83	1.94%	
11	November-93	0.22%		461.79	-1.29%	
12	December-93	0.71%	14.55%	466.45	1.01%	7.06%
13	January-94	1.76%		481.61	3.25%	
14	**February-94**	**-0.03%**		467.14	-3.00%	
15	March-94	1.84%		445.77	-4.57%	
16	April-94	1.86%		450.91	1.15%	
17	May-94	0.88%		456.41	1.22%	
18	June-94	0.36%		444.27	-2.66%	
19	July-94	1.98%		458.26	3.15%	
20	August-94	0.70%		475.50	3.76%	
21	September-94	0.71%		462.71	-2.69%	
22	October-94	2.02%		472.35	2.08%	
23	**November-94**	**-0.44%**		453.69	-3.95%	
24	December-94	0.79%	13.12%	459.27	1.23%	-1.54%
25	January-95	1.83%		470.42	2.43%	
26	February-95	1.03%		487.39	3.61%	
27	March-95	1.09%		500.71	2.73%	
28	April-95	1.81%		514.71	2.80%	
29	May-95	2.07%		533.40	3.63%	
30	June-95	0.57%		544.75	2.13%	
31	July-95	1.19%		562.06	3.18%	
32	August-95	0.08%		561.88	-0.03%	
33	September-95	2.15%		584.41	4.01%	
34	October-95	1.88%		581.50	-0.50%	
35	November-95	1.12%		605.37	4.10%	
36	December-95	0.73%	16.68%	615.93	1.74%	34.11%
37	January-96	1.75%		636.02	3.26%	
38	February-96	0.85%		640.43	0.69%	
39	March-96	1.71%		645.50	0.79%	
40	April-96	0.72%		654.17	1.34%	
41	May-96	1.83%		669.12	2.29%	
42	June-96	0.27%		670.63	0.23%	
43	July-96	2.37%		639.95	-4.57%	
44	August-96	0.35%		651.99	1.88%	
45	September-96	1.33%		687.31	5.42%	
46	October-96	1.35%		705.27	2.61%	
47	November-96	1.93%		757.02	7.34%	
48	December-96	0.47%	15.96%	740.74	-2.15%	20.26%
49	January-97	3.08%		786.16	6.13%	

N	Month	Net Return		S&P 500 Price Index	S&P 500 Price Return	S&P 500 Price Return
50	February-97	0.92%		790.82	0.59%	
51	March-97	0.90%		757.12	-4.26%	
52	April-97	1.85%		801.34	5.84%	
53	May-97	0.90%		848.28	5.86%	
54	June-97	1.50%		885.14	4.35%	
55	July-97	0.87%		954.29	7.81%	
56	August-97	0.43%		899.47	-5.74%	
57	September-97	2.23%		947.28	5.32%	
58	October-97	0.51%		914.62	-3.45%	
59	November-97	1.77%		955.40	4.46%	
60	December-97	0.46%	16.52%	970.43	1.57%	31.00%
61	January-98	1.04%		980.28	1.02%	
62	February-98	1.58%		1049.34	7.04%	
63	March-98	2.11%		1101.75	4.99%	
64	April-98	0.45%		1111.75	0.91%	
65	May-98	2.15%		1090.82	-1.88%	
66	June-98	1.58%		1133.84	3.94%	
67	July-98	1.05%		1120.67	-1.16%	
68	August-98	0.30%		957.28	-14.58%	
69	September-98	1.11%		1017.01	6.24%	
70	October-98	2.26%		1098.67	8.03%	
71	November-98	1.00%		1163.63	5.91%	
72	December-98	0.18%	15.83%	1229.23	5.64%	26.67%
73	January-99	2.41%		1279.64	4.10%	
74	February-99	0.17%		1238.33	-3.23%	
75	March-99	2.50%		1286.37	3.88%	
76	April-99	1.42%		1335.18	3.79%	
77	May-99	1.15%		1301.84	-2.50%	
78	June-99	2.27%		1372.71	5.44%	
79	July-99	0.46%		1328.72	-3.20%	
80	August-99	1.06%		1320.41	-0.63%	
81	September-99	0.94%		1282.71	-2.86%	
82	October-99	1.28%		1362.93	6.25%	
83	November-99	1.50%		1388.91	1.91%	
84	December-99	0.41%	16.69%	1469.25	5.78%	19.52%
85	January-00	2.72%		1394.46	-5.09%	
86	February-00	0.17%		1366.42	-2.01%	
87	March-00	2.90%		1498.58	9.67%	

	Madoff	S&P500	Comps
Monthly Standard Deviation	0.83%	3.86%	**4.6 X's**
Average Monthly Return	1.24%	1.51%	**1.2 X's**
Annual Standard Deviation	4.32%	12.88%	**3.0 X's**
Average Annual Return	15.62%	19.58%	**1.25 X's**
Return / Risk Ratio	**3.62**	**1.52**	
# of down Months	3	26	**8.7 X's**
Percentage Down Months	3.4%	29.9%	

Exhibit 1

MANAGER B

The Broyhill All-Weather Fund, L.P.

(A)

Strategy Which is pure Madoff where Broyhill markets Madoff

The Manager's investment objective is long term growth on a consistent basis with low volatility. The investment advisor invests exclusively in the U.S. and utilizes a strategy often referred to as a "split-strike conversion." Generally this style involves purchasing a basket of 30 to 35 large-capitalization stocks with a high degree of correlation to the general market (e.g. American Express, Boeing, Citicorp, Coca-Cola, Dupont, Exxon, General Motors, IBM Merck, McDonald's). To provide the desired hedge, the manager then sells out-of-the-money OEX index call options and buys out-of-the-money OEX index put options. The amount of calls that are sold and puts that are bought represent a dollar amount equal to the basket of shares purchased.

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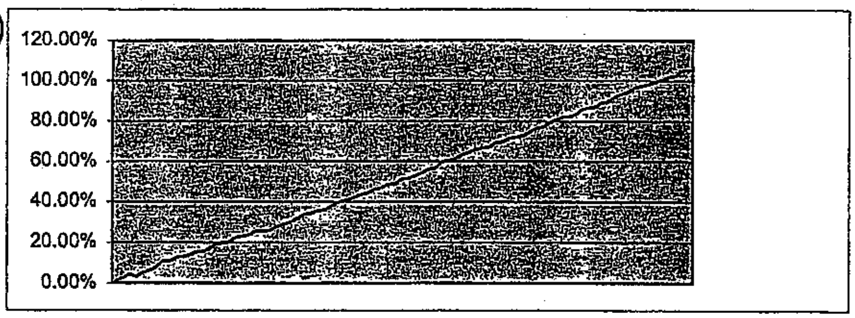
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sept	Oct	Nov	Dec	YTD
1993	1.44%	1.17%	1.96%	-1.44%	2.14%	1.01%	1.41%	3.01%	0.02%	2.09%	0.22%	0.71%	14.55%
1994	1.76%	-0.03%	1.84%	1.86%	0.88%	0.36%	1.98%	0.70%	0.71%	2.02%	-0.44%	0.79%	13.12%
1995	1.83%	1.03%	1.09%	1.81%	2.07%	0.57%	1.19%	0.08%	2.15%	1.88%	1.12%	0.73%	16.68%
1996	1.75%	0.85%	1.71%	0.72%	1.83%	0.27%	2.37%	0.35%	1.33%	1.35%	1.93%	0.47%	15.96%
1997	3.08%	0.92%	0.90%	1.85%	0.90%	1.50%	0.87%	0.43%	2.23%	0.51%	1.77%	0.46%	16.52%
1998	1.04%	1.58%	2.11%	0.45%	2.15%	1.58%	1.05%	0.30%	1.11%	2.26%	1.00%	0.18%	15.83%
1999	2.41%	0.17%	2.50%	1.42%	1.15%	2.27%	0.46%	1.06%	0.94%	1.28%	1.50%	0.41%	16.69%
2000	2.72%	0.17%	2.90%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	5.88%

(C)



Cumulative Performance of Manager B

(D)

Background

The Broyhill All-Weather Fund, L.P., has allocated funds to a Single Manager Limited Partnership (the "Partnership"). The Partnership's parent company is a public company and together with its subsidiaries provides investment consulting advice to financial institutions, endowments, and public funds of over $2.3 billion in client assets. The General Partner does not manage the assets directly but allocates them to Manager B.

Annual Compound Return	15.50%
Annualized Standard Deviation	4.32%
Correlation to S&P 500 Beta	0.06
% Positive Months	96.55%
Sharp Ratio	3.54

Manager B
Assets Under Management
$ 350,000,000

N W E S

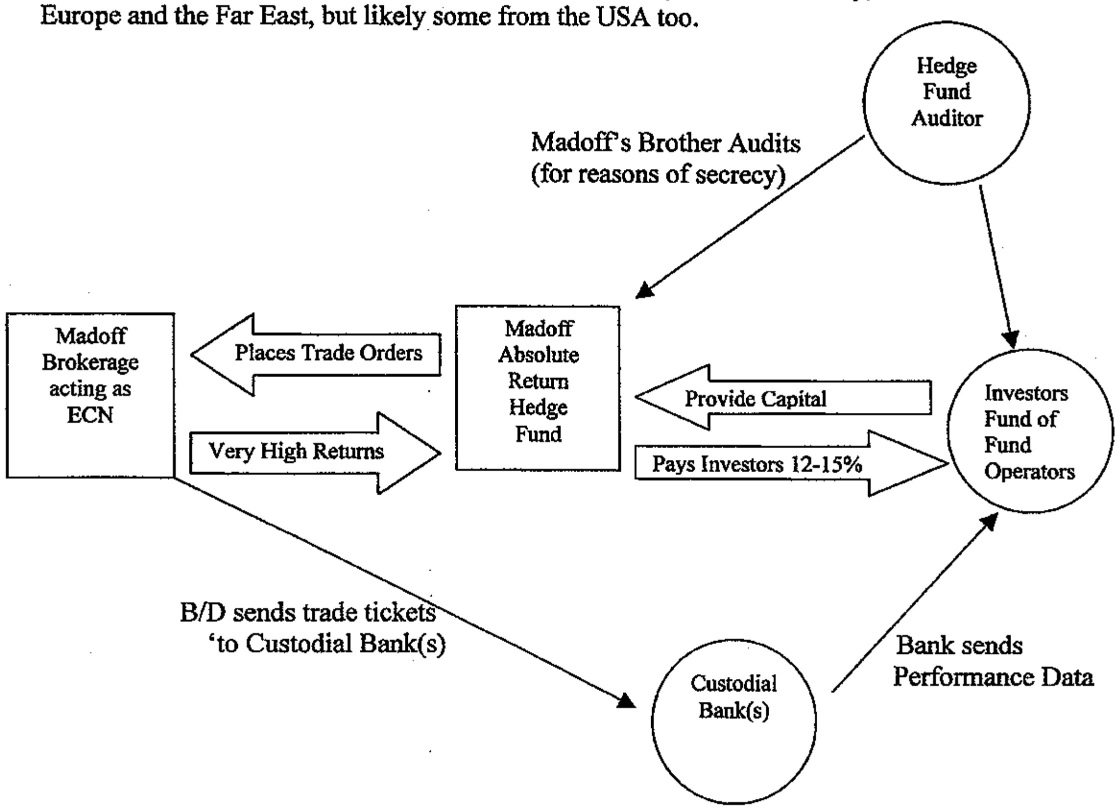
Broyhill Asset Management, LLC

♦ **Location**: New York Region

♦ **Who**: Madoff Hedge Fund

♦ **How Much is Involved**: between $12- $20 billion

♦ **Investors (unknowing victims):** fund of funds, mainly off-shore money, lots of it from Europe and the Far East, but likely some from the USA too.



♦ **Product Line**: Absolute Return, earns 15% a year, at a steady pace of 1 – 1.5% a month, makes money in all market conditions (up markets, flat markets, down markets) using U.S. equities.

A. Generally this style involves buying a 30 – 35 stock replicating basket that corresponds to the S&P 100 (OEX). In other words, they buy large-capitalization names, and weight them so that they track the OEX index fairly closely.
B. They use their broker-dealer's order flow to judge which stocks are going up, and which stocks are going down. They then selectively buy the stocks, sell out-of-the-money OEX index calls against them, and buy a protective out-of-the-money OEX index put.
C. They collect dividends on the stocks. The OEX currently yields about .94%.

D. Earned over 15 ½% a year for over seven years with extremely low standard deviation of 4.3% versus the S&P 500 which earned over 19 ½% but with 12.9% annual standard deviation over the same time period. This program, earned 80% of the market's return with only one third of the risk. Think about it! Is this really possible, or is it too good to be true? **(I have attached an excel spreadsheet comparing and contrasting Madoff's program to the S&P 500 index.)**

E. Only 3 down months vs. the market's down 26 months during the same period, with a worst down month of only – 1.44% (April 1993) vs. the market's worst down month of –14.58% (August 1998).

F. Has a Return to Risk Ratio of 3.62, earning 3.62% for every 1% of risk (15.62% annual return divided by 4.32% annual standard deviation = 3.62) whereas the market he's trying to replicate only has a ratio of 1.52 (19.58% annual return divided by 12.88% annual standard deviation

G. The reason given for these unbelievable returns comes from access to their Broker/Dealer's Order flow. Knowing the quantity of shares bid for at given price levels, Madoff's broker dealer arm can take advantage of the knowledge to trade against in setting up their positions. In other words, they can buy stock ahead of customers at a slightly higher price, safe in the knowledge that at a slightly lower price they have one of their customer's bids. If they buy a stock and it drops immediately, they just sell it to their customers.

Reality:

1) These numbers really are too good to be true. And every time I've thought a company's or a manager's numbers were "too good to be true," there has been fraud involved. Yes, access to order flow is worth something but this worth can be measured in pennies per share.
2) Having your buy-side subsidiary front-run your broker/dealer arm's customers while buying stock seems illegal.
3) Yes, Madoff can make more intelligent short-term bets via their access to order flow. However, short-term forecastabilty does not lead to long-term knowledge of where the stocks that he buys are headed. Short-term he may know there are a lot of IBM shares to buy, but that doesn't lead to knowledge of where IBM will be trading next month.
4) Madoff's out-of-the-money OEX index puts do offer protection against systemic market declines. However, his 30 – 35 stock portfolio has individual company risk in it and should experience more frequent and more sizeable losses than what his performance record indicates.
5) Assuming Madoff
   A. has perfect knowledge of order flow over a time horizon of ___ minutes.
   B. The average stock is priced at $46, has an annualized standard deviation of 45%

Then the value of Madoff's knowledge, using the Black-Scholes options pricing model is __ cents.

1) This same investor (in item 4 above) has brokerage statements sent directly to their custodian in order to verify performance. However, this manager has a brokerage arm and it is this brokerage arm that is mailing the statements. Outside brokers are not used in order to maintain secrecy. *[lack of independent oversight]*

2) Another investor, this one based in Europe and investing money on behalf of an Arab country, asked to send in a team of Big Six auditors during the due-diligence process to verify performance. They were told that "only my brother is allowed to audit us, due to the proprietary investment process we employ." This European Fund of Funds invested a few hundred million of their Arab client's money anyway because of the steady returns. *[Shades of Barings Bank and Nick Leeson, where there is no independent oversight.]*

3) A marketing executive who has placed client money with this firm, tells us that this manager actually is merely borrowing money at 12% - 15%, and keeping the rest of the returns for itself. This has been confirmed by another investor. Both of these sources also say that when the market has a steep sell-off, this manager books only winning trades in their accounts, and subsidizes their steady 1 – 1 ½ % returns per month during those periods *[How is this legal? Why not borrow money at Libor plus some small spread instead?]*

What I can do to help the SEC

♦ I can provide you with detailed questions for your audit teams. In fact, I would be willing to accompany a team undercover under certain conditions (new identity, disguise, proper compensation) and willing to sign a non-disclosure agreement and serve under the command & control of the SEC. In return, I need complete anonymity. I would take a leave of absence from my firm. Only my wife would know where I am, but I would have no contact with her or anyone else that I know while on assignment. I feel that my personal safety of myself and my family may be in danger if I assist the SEC.

♦ I can provide the SEC with simple mathematical formulas that value short-term "free options" that result when a party has access to order flow. I can prove that long-term strategies that purport to profit from these "free short-term options " will not meet the steady 1 – 1.5% returns supposedly generated by the firm in question.

To: [redacted]
2 pages
Re: Madoff Investment Process explained

inter alia, a statement of its net capital appreciation of net capital depreciation.

USE OF PROCEEDS

The entire net proceeds from the sale of the interests will be available to the Partnership. The Partnership incurred approximately $5,000 in connection with the initial offering of Interests for the admission of Limited Partners (such costs consisting primarily of legal fees and blue sky filing fees. The General Partners do not intend to pay any commissions or fees to broker-dealers in connection with the offering. However, in the event any fees or commissions are paid, they will be paid by the General Partners rather than the Partnership. The General Partners have not established any maximum amounts for such fees and commissions, none of which have been paid or earned to date.

The Partnership's funds are allocated to an account at Bernard L. Madoff Investment Securities (see "INVESTMENT PROGRAM"). Funds not so allocated will be maintained in cash. Bernard L. Madoff Securities is employed solely as an agent of the Partnership. It has no ownership interest in the Partnership and no role in the overall management of the Partnership.

The Partnership will not make any loans to affiliated entities nor will it invest in any foreign government securities.

INVESTMENT PROGRAM

The Partnership seeks to obtain capital appreciation of its assets through the utilization of nontraditional options trading strategies. The General Partners have established a discretionary account for the Partnership at Bernard L. Madoff Investment Securities ("BLM"), a registered broker-dealer in New York, New York, which utilizes a strategy described as "split strike conversion". This strategy has defined risk and profit parameters which may be ascertained when a particular position is established. All investment decisions in the account at BLM are effected by persons associated with BLM. The firm, which employs approximately 160 people, acts primarily as a market maker in stocks and convertible securities. Most of the stocks for which it acts as a market maker are also listed on the New York Stock Exchange. Set forth below is a description of the "split strike conversion" strategies.

The establishment of a typical position entails (i) the purchase of equity shares, (ii) the sale of a related out of the money call option representing an amount of underlying shares equal to the number of equity shares purchased, and (iii) the purchase of a related put option which is at or out of the money. A call option is out of the money when its strike price is greater than the current price of the stock; a put option is out of the money when the strike price is lower than the current price of the stock.

The logic of this strategy is that once a long stock position has been established, selling a call against such long position will increase the standstill rate of return, while allowing upward movement to the short call strike price. The purchase of an at or out of the money put, funded with part or all of the call premium, protects the equity position from downside risk.

Equity index options are also utilized in this trading methodology. Such a strategy involves buying a group of equity securities that together will highly correlate to the S&P 100 Index (the "OEX"). Equivalent contract value dollar amounts of out of the money OEX call options are sold, and out of the money OEX put options are purchased, against the basket of stocks. The basket typically consists of approximately 35 stocks in the S&P 100 Index.

A bullish or bearish bias of the positions can be achieved by adjustment of the strike prices in the OEX puts and calls. The further away the strike prices are from the price of the S&P 100 Index, the more bullish the strategy. However, the dollar value underlying the put options always approximates the value of the basket of stocks.

The Partnership bears the cost of all brokerage fees and commissions charged in connection with the account at BLM. All interest earned on credit balances is credited to the Partnership.

BLM acts as a principal in connection with its sale of securities to the Partnership, and the purchase of securities from the Partnership. BLM acts as a market-maker in the stocks purchased and sold by the Partnership. These market making activities enable BLM to trade with the Partnership as principal. See "CERTAIN RISK FACTORS".

The options transactions executed for the benefit of Sentry are effected, primarily, in the over-the-counter, not on a registered options exchange.

There can be no assurance that the investment objectives of the Partnership will be achieved. THE PARTNERSHIP'S INVESTMENT PROGRAM IS SPECULATIVE AND ENTAILS SUBSTANTIAL RISKS. MARKET RISKS ARE INHERENT IN ALL SECURITIES TO VARYING DEGREES. NO ASSURANCE CAN BE GIVEN THAT THE PARTNERSHIP'S INVESTMENT OBJECTIVE WILL BE REALIZED. (SEE "CERTAIN RISK FACTORS".)

2002 Madoff Case Activity Cover Letter

Date of Analysis: 12/28/2008

Documents Attached in this PDF file are:

1. The 7-page trip itinerary I took with Access International Advisors Limited to London, Paris, Geneva and Zurich from June 19 – June 29, 2002 to market my firm's Statistical Options Arbitrage Hedge Fund Strategy to European banks, private client banks, family offices and Hedge Fund, Fund of Funds.
2. December 24, 2008 Bloomberg News Story about the suicide of Thierry de La Villehuchet, managing partner of Access International Advisors.
3. December 23, 2008 New York Times Story about the suicide of Thierry de La Villehuchet, managing partner of Access International Advisors.

My comments:

1. At the time, Access was approximately a $1.2 billion hedge fund, fund of funds (HFOF) with a roughly 45% ($540 Million) allocation to Madoff.
2. Access was majority owned by a group of French noblemen who were both wealthy and had a royal lineage. The one common bond these French noblemen seemed to share was that their ancestors served as Napoleon's Field Marshalls. The four partners at the time were Thierry de La Villehuchet, Patrick Littaye, Phillippe Junot, and Tim Ng.
3. In my opinion, Thierry de La Villehuchet never knew that Madoff was a fraud. I spent a lot of time with the man while we were in Europe and I found him to be a wonderful salesman without any discernable quantitative finance skills. I believe he was another innocent Madoff victim who was, like everyone else, wiped out financially by Madoff.
4. Philippe Junot's ancestor may have been one of Napoleon's Admirals and I believe that Francois De Flaghac's ancestor was a general under Napoleon. All of these family names appear on the Arch de Triumph in Paris under Napoleon's name. I believe that Access's Prince Michel of Yugoslavia is a cousin to England's Prince Charles because he went to the polo fields to meet with Prince Charles, Prince William and Prince Harry while we were in London and told me they were his cousins. Therefore it is my belief that Access likely had several royal families as clients invested in Madoff.
5. The Access team would begin each meeting with the following: *"Harry is just like Bernie Madoff only with higher returns and higher risk."* And every time they said this it was all I could do not to jump up and say, *"hey you morons, Bernie's a Ponzi so I have higher returns than his and lower risk because my returns are real while Bernie's are a fraud!!"*

However, since most of the firms we were meeting with bragged that they had "special access" to Bernie and that, "while Madoff is closed to new investors, we have special access to Madoff and he'll accept new money from our firm." I quickly figured out that if all of these firms were special then, of course, Madoff had to be a Ponzi scheme and he was playing hard to get as part of his hook. It was during this trip that I knew that Madoff wasn't front-running, he was pure Ponzi.

6. If I had jumped up and told everyone I met in Europe that Madoff is a fraud, I would not have gotten past the first meeting because the Access people would have dumped me on the nearest curb and then told Madoff that I was dissing him before his investors. Madoff would then likely have had me killed – and he had literally 20 billion reasons why. So in the interest of my personal safety I used this marketing trip as an intelligence collecting activity. I certainly was in no position to admit that I had already turned in Madoff twice to the SEC, once in May 2000 and again in October 2001. As it was, I felt I was living on borrowed time and feared for my life.
7. Based upon this trip, I believe that the Madoff losses in Europe may turn out to be larger than those in the United States. I have two reasons for this belief. First, European culture is such that high-born families, particularly royal families, are much more reluctant to admit they were taken to the cleaners by a common born, American swindler. Second, Europe does not have a robust class action bar or English common law system set up to handle fraud recoveries like we do here in the US.
8. In reviewing my trip itinerary and running the names versus the list of known Madoff victims, I believe that several French and Swiss firms have Madoff losses that they have not yet admitted to. If possible, I would like the legal attaché's in our French and Swiss embassies to forward my list of probable Madoff investors to the appropriate host nation authorities for immediate investigation. In the wake of the massive regulatory failure on the part of the SEC to close down Madoff at $3 - $7 billion when I first reported this fraud in May 2000, it is imperative that the US be proactive and warn the French and Swiss authorities to prevent further loss of confidence in the US capital markets.

Respectfully submitted,

Harry Markopolos

Harry Markopolos, CFA, CFE
Chartered Financial Analyst
Certified Fraud Examiner

ACCESS INTERNATIONAL ADVISORS LIMITED

Suite 61 Grosvenor Close, Shirley Street P.O. Box N-7521 Nassau, Bahamas

GLT 06.18.02

Schedule for Harry Markopolos

Rampart

Wednesday 19 2002	**BOSTON/ LONDON**

6 pm Departure from Boston British Airways Flight 212 Terminal E

Thursday, 20 2002	**LONDON**

5.35 am Arrival London Heathrow Terminal 4

Franklin Hotel
28 Egerton Gardens
London SW 32 DB
Tel : 44 207 584 55 33
Fax : 44 207 584 54 49

Friday 21, 2002	**LONDON / PARIS**

8.30 am Libre

10.30 am **Barclays** *Michel of Yugoslavia will attend the meeting*
Meeting with Eleonor Dashicourt
Murray House London EC3N 4HH UK
44 20 7977 3635

12.30 pm Libre

2.30 pm Libre

4.30 pm Libre

6 pm Departure form London Heathrow Air France Flight 2071 Terminal 2
E Ticket CXBBRX

8.10 pm Arrival Paris De Gaulle Aerogare 2, Terminal F

Hotel Elysee Matigon
3 rue de ponthieu 75008
+33 (1) 42 25 73 01
+33 (1) 42 56 01 39

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Suite 61 Grosvenor Close, Shirley Street P.O. Box N-7521 Nassau, Bahamas

Saturday 22, 2002 **PARIS**

Hotel Elysee Matigon
3 rue de Ponthieu 75008
+33 (1) 42 25 73 01
+33 (1) 42 56 01 39

Sunday 23, 2002 **PARIS**

Hotel Elysee Matigon
3 rue de Ponthieu 75008
+33 (1) 42 25 73 01
+33 (1) 42 56 01 39

Monday 24, 2002 **PARIS**

8.30 am

10.30 am **AGF Asset management** *Francois de Flaghac will attend the meeting*
Meeting with Jean Francois Vert
14 rue Havely 75009
0153244508

12.30 pm Lunch with Christophe Schmitz, Luc Lauriau and Thierry de La Villehuchet

3 pm **Mr Bertrand Savatier** *Mr Cyrille d'Avout will attend the meeting*
John Locke Investments
Cyrille Finances
2 rue des Italiens

5 pm **Oddo Asset Management** *Mr Cyrille d'Avout will attend the meeting*
Meeting with Philippe Oddo
12 Boulevard De La Madeleine 75009 Paris
Tel 33 1 44 51 83 83
Fax: 33 1 44 51 83 70

Hotel Elysee Matigon
3 rue de ponthieu 75008
+33 (1) 42 25 73 01
+33 (1) 42 56 01 39

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Tuesday 25, 2002	PARIS

8.30 am	**Alterinvest** Meeting with Etienne Vernier 42 Avenue Montaigne 33 1 53 67 53 27 33 1 53 67 53 28	*Thierry de La Villehuchet will attend the meeting*
10.30 am	**Altigest** Meeting with Mr Lescoat 23 rue d'Antin 75002 33 1 42 66 15 43 Meeting with Mr Lescoat	*Thierry de La Villehuchet will attend the meeting*
12.30 pm	**SV International** Meeting with Mr Voisin 64 Bd Pereire 75017 33 1 40 54 80 00	*Thierry de La Villehuchet will attend the meeting*
3 pm	**GT Finances** Meeting with Mr Moreau 16 Place De La Madeleine 33 1 53432041	*Patrick Littaye will attend the meeting*
4.30 pm	**Tethys** Meetin with Jean Paul Delattre 5 Rue Du 8 Mai 1945 Clichy 92586 CEDEX France Office 33 1 47 56 87 46	*Patrick Littaye will attend the meeting*
6 pm	**Société Générale** Meeting with Laurent Le Saint and Laurent Minveille 2 place de la coupole La defence 92078 01 42 13 67 37	*Francois de Flaghac will attend the meeting*

Hotel Elysee Matigon
3 rue de ponthieu 75008
+33 (1) 42 25 73 01
+33 (1) 42 56 01 39

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Wednesday 26, 2002	PARIS/GENEVA

8 am	Departure Paris de Gaulle Air France flight 1642 Aerogare 2 Terminal F **E Ticket CXBBRX**
9.10 am	Arrival Geneva
10 am	
11.30 am	
1 pm	
2.30 pm	**Dexia Asset Management** *Francois de Flaghac will attend the meeting* Meeting with Jean Sebastien Debusschere 2 Rue Jargommant Geneve 1207 41 22 7079011
4 pm	**Fund Invest** *Thierry de La Villehuchet will attend the meeting* Meeting with Roer Galor 22, rue de Villereuse Genève Office 41 5929212
5.30 pm	**SCS Alliance** *Thierry de La Villehuchet will attend the meeting* Meeting with Mr Saba 11 route de Florissant 41 22 839 01 00
8 pm	Diner Hotel Metropole

Hotel Metropole
34 Quai General Guisan
+41 (22) 318-3200
+41 (22) 311-1350

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Suite 61 Grosvenor Close, Shirley Street P.O. Box N-7521 Nassau, Bahamas

Thursday 27, 2002 **GENEVA**

8.30 am	**Aforge** Meeting with Mr Hervieux Causse 7 Rue Francois Versonnex 41 22 7078240	*Thierry de La Villehuchet will attend the meeting*
10 am	**HSBC** Meeting with Mr Messier 2 place du lac 41 22 7055555	*Michel of Yugoslavia will attend the meeting*
11.30 am	**Fix Family office** Meeting with Mme Ayca Pars 7-9 Rue De La Croix D'or Geneve Office 41 22 3178866	*Michel of Yugoslavia will attend the meeting*
1 pm	Libre	
2.30 pm	**JP Morgan** Meeting with Mr Ribordi 8 Rue De La Confederation, Po Geneva 1211 41 22 7441111	*Michel of Yugoslavia will attend the meeting*
4 pm	**Banque Piguet** Meeting with Mr Tosi 5 Place De L'universite 41 22 3112700	*Philippe Junot will attend the meeting*
5.30 pm	Libre	

Hotel Metropole
34 Quai General Guisan
+41 (22) 318-3200
+41 (22) 311-1350

Prepared by ACCESS INTERNATIONAL ADVISORS, INC. for ACCESS INTERNATIONAL ADVISORS LIMITED

ACCESS INTERNATIONAL ADVISORS, INC.
509 Madison Avenue 22nd Floor New York, NY 10022
Tel: 1 (212) 223-7167 Fax: 1 (212) 223-3463
E-mail: aiausa@aiagroup.com

ACCESS INTERNATIONAL ADVISORS LIMITED

Suite 61 Grosvenor Close, Shirley Street P.O. Box N-7521 Nassau, Bahamas

Friday 28, 2002	**ZURICH**

8.10 am	Departure from Geneva Swiss AirLines Flight 2805 I WILL GIVE YOU THIS TICKET IN PARIS
9.05 am	Arrival Zurich Terminal A
11.am	***LGT Pending***
1 pm	***Romulus Pending***
2.30 pm	Libre
4 pm	Libre
5.30 pm	Libre

Hotel Baur au Lac
Talstrasse 1 8001 Zurich Suisse
Tel 41 1 220 50 20
Fax 41 1 220 50 44

Saturday 29, 2002	**Zurich New York**

3.45 pm	Departure British Air Ways Flight 715 Terminal B
4.35pm	Arrival London Heathrow Terminal 1
6.35 pm	Departure London Heathrow British Air ways Flight 239 Terminal 4
8.50 pm	Arrival Boston Terminal E

ACCESS INTERNATIONAL ADVISORS LIMITED

Suite 61 Grosvenor Close, Shirley Street P.O. Box N-7521 Nassau, Bahamas

PHONE LIST

Thierry de la Villehuchet	1 917 250 00 76
Patrick Littaye	011 33 6 20 59 68 24
Guy de La Tour du Pin	011 33 6 17 01 20 98
Michel of Yugoslavia	UK cell: 44 78 16 06 21 07 Switzerland Cell 41 76 524 72 12
Philippe Junot	011 33 6 16 60 60 00
Francois de Flaghac	011 33 1 49 53 97 16
Mr D'Avout	011 33 6 81 65 94 92
HOTEL Elysee Matigon (Paris)	011 33 (1) 42 25 73 01
HOTEL Metropole (Geneva)	011 41 22 318 33 50
HOTEL Baur au Lac (Zurich)	011 41 1 220 50 20

L'Oreal Heiress Bettencourt Said to Have Invested With Madoff

Email | Print | A A A

By Saijel Kishan and Katherine Burton

Dec. 24 (Bloomberg) -- Liliane Bettencourt, the world's wealthiest woman, entrusted part of her $22.9 billion fortune with Bernard Madoff through the fund manager found dead in New York yesterday, two people familiar with the matter said.

The 86-year-old daughter of L'Oreal SA founder Eugene Schueller was the first investor in a fund managed by Access International Advisors, the people said, speaking on condition of anonymity because her investment isn't public. The body of Access co-founder Thierry Magon de La Villehuchet, 65, was found in his Madison Avenue office yesterday. Police said he probably killed himself.

Bettencourt, a Parisian, joins wealthy individuals from around the world, including Spanish billionaire Alicia Koplowitz, U.S. moviemaker Steven Spielberg and Nobel laureate Elie Wiesel, among victims of what Madoff, 70, told investigators was a $50 billion Ponzi scheme.

"More high-profile names who have been victimized by Madoff will start to become known now," said Ron Geffner, who represents hedge funds at the New York-based law firm Sadis & Goldberg LLP. "There's a strong sense of anguish, fear and distrust."

Calls and e-mails to Fondation Bettencourt Schuelle, the foundation she started in the Parisian suburb of Neuilly-sur-

Seine, weren't returned. Bettencourt ranked 17th in Forbes' list of the world's richest people in 2008, the highest-ranking woman. Access, which oversaw $3 billion, raised money mainly from wealthy European investors.

'Extensive' Due Diligence

Access said in a Dec. 12 letter to clients that funds including its LUXALPHA SICAV-American Selection invested solely with Madoff's eponymous investment firm. The fund had $1.4 billion in assets as of Nov. 17, according to data compiled by Bloomberg.

Access says it carries out "extensive" due diligence on the funds to which it allocates money, a process that can take as long as six months and cost $100,000. It also hires private investigators to run "extensive background checks" on fund managers, including searches on professional credentials, regulatory filings and bankruptcy, according to marketing documents dated September.

New York police are working on the assumption that de La Villehuchet's death was a suicide, Commissioner Raymond Kelly said yesterday. The fund manager was found "with his feet propped up on his desk, a trash pail nearby to collect blood," and no sign of a second person, Kelly said in the interview.

Body at Desk

He had cuts made by a box-cutter in the area of his biceps and his wrist, and pills were found nearby, Kelly said at a news conference. No suicide note was found. His body was found at his desk early yesterday morning by a security guard who had been called by an employee unable to enter the office, Kelly said.

Villehuchet founded Access in 1994 with Patrick Littaye.

One of the firm's partners was **Philippe Junot**, according to the marketing documents. Junot is the former husband of **Princess Caroline** of Monaco. Prince Michel of Yugoslavia is an investor relations executive, according to the documents.

Prior to Access, De La Villehuchet was chairman and CEO of Credit Lyonnais Securities USA, the U.S. investment banking arm of the French bank. He had joined Credit Lyonnais in 1987, and before that ran Interfinance, an international broker firm specializing in French, Belgian and Italian stock markets that he founded in 1983. He worked at Banque Paribas from 1970 to 1983.

Access, which had 26 employees, said in a statement on Dec. 12 it was working with lawyers to assess its exposure to Madoff. UBS AG, LUXALPHA's administrator until this year, is no longer involved with it, said **Karina Byrne**, a UBS spokeswoman.

De La Villehuchet's death comes as lawsuits mount in connection with investors victimized by Madoff. **Fairfield Greenwich Group**, a hedge-fund firm that had $7.5 billion invested with Madoff, has been sued for allegedly failing to protect its clients' assets. Madoff was arrested on Dec. 11 and is now under house arrest at his apartment in New York.

To contact the reporters on this story: **Saijel Kishan** in New York at **skishan@bloomberg.netKatherine Burton** in New York at **kburton@bloomberg.net**

Last Updated: December 23, 2008 20:06 EST

Financier Is Found Dead in a Madoff Aftermath

By ZACHERY KOUWE and MICHAEL WILSON
Published: December 23, 2008
New York Times

Around 4 a.m. on Monday, a prominent hedge fund manager who apparently had lost $1.4 billion with Bernard L. Madoff, telephoned a longtime client in Paris, sounding upset.

Mary Altaffer/Associated Press
Journalists gathered on Tuesday at the Madison Avenue office where the body of Thierry Magon de la Villehuchet was found.

"I have to fight for my clients and myself," the money manager, R. Thierry Magon de la Villehuchet, told the client, who spoke on the condition of anonymity because of investigations into the $50 billion Ponzi scheme Mr. Madoff is suspected of orchestrating. "It's a complete nightmare."

A little more than 24 hours later, Mr. de la Villehuchet was found dead in his office on Madison Avenue. The evidence pointed to suicide, the police said on Tuesday.

Security officers discovered the body of Mr. de la Villehuchet, a co-founder of Access International Advisors, in a chair, with one of his legs propped on his desk. His wrists and his left biceps were slashed, said Paul J. Browne, a New York police spokesman. A wastebasket had been placed under his bleeding biceps, Mr. Browne said.

No suicide note was found, but sleeping pills and a box cutter were discovered under his desk.

Mr. de la Villehuchet, 65, was in his office at 7 p.m. on Monday and had asked the cleaning staff to clean up early because he would be working late.

Later that evening, one of the firm's partners asked a security guard to see if Mr. de la Villehuchet was still in his office, but the door was locked, and the guard had no key, the police said.

During the last week, as the scale of the scheme came to light, Mr. de la Villehuchet had tried unsuccessfully to recover his clients' money, the client said. Mr. de la Villehuchet told the client in Paris on Monday morning that he felt that he had betrayed clients and friends.

"He said he felt robbed," the client said.

A native of the Brittany region of France, Mr. de la Villehuchet was described by friends as a man who was devoted to his firm. He founded Access International Advisors in 1994 with Patrick Littaye after his tenure as chairman and chief executive of the United States investment banking arm of the French bank Crédit Lyonnais.

Mr. de la Villehuchet, an avid sailor and a member of the New York Yacht Club, lived in Westchester County with his wife. The couple also owned a home in Brittany. No one responded to a telephone call to Mr. de la Villehuchet's home or to messages left at Access International's offices.

Early Tuesday afternoon, several reporters and photographers gathered in front of the narrow entrance to Access International's office on Madison Avenue, a few blocks from Rockefeller Center.

Access International is one of several so-called feeder funds that funneled money from investors across the globe into Mr. Madoff's collapsed firm. The news of Mr. de la Villehuchet's death came as investors in other feeder funds with exposure to Mr. Madoff, including Fairfield Greenwich Group and Tremont Group Holdings, began suing those funds alleging negligence and breach of fiduciary duty.

Access International managed $3 billion, but its Luxalpha American Selection fund invested all of its assets with Mr. Madoff. In a letter to fund investors last week, the New York-based firm called Mr. Madoff's arrest "a shocking development" and said it was assessing the situation.

Investors in the Luxalpha fund were mostly wealthy European clients of Rothschild investment bank and UBS, which was the custodian and administrator of the Luxalpha fund until this year, when Access International took over.

UBS has said that wealthy European clients, attracted by Mr. Madoff's stellar returns, had asked the bank to set up a fund to invest with him.

Nelson D. Schwartz contributed reporting from Paris and Michael J. de la Merced from New York.

2005 Madoff Case Activity Cover Letter

Date of Analysis: 12/28/2008

1. I have organized the final three months of 2005 into chronological order in two parts:

   Part One: consists of my SEC Submissions and e-mail exchanges with SEC staff.

   Part Two: consists of my evidence gathering with Frank Casey, Neil Chelo, and discussions with Pat Burns and Wall Street Journal senior investigative reporter John R. Wilke of the Journal's Washington Bureau.

2. I currently plan on only turning over to Congress my SEC Submissions and e-mail exchanges with the SEC for 2005.

3. I would like a legal review of the case documents to determine if they should be released to Congress, to the SEC's Inspector General, to US law enforcement, to foreign law enforcement, to victim's, to the plaintiff's bar, to the defendant's bar, and to the public.

4. The reason there is only three months worth of data is that in May 2004 I purchased a Dell Pentium 4 3 Ghz PC and had all my files transferred onto it at that time by the IT director at my former employer. However, this PC arrived with Microsoft Outlook 2000 software and MS Outlook 2000 was a very poorly designed e-mail program. Unfortunately it has a 750 MB archive storage limit and if you retain too many old e-mails it slows down your e-mail system and eventually corrupts the files. Therefore, in order to maintain sped and efficiency, I deleted the archived e-mails, which was a very common thing to do back then if you were a MS Outlook 2000 user.

5. However, in my basement is my previous PC, a NEC Pentium 2 300 Mhz machine. My local PC expert is due in on Wednesday, December 30, 2008 to attempt to recover all Madoff related e-mails. If the hard drive is still operational and if the software issues can be overcome, I hope to be able to recover whatever Madoff related e-mails might exist on this machine.

6. Unfortunately, the vast majority of any Madoff related e-mails would have been sent and received from my work PC at Rampart. Worse, Rampart was a high-speed derivatives asset management firm that allocated a significant percentage of its annual revenues towards always upgrading its servers and

PC's to the latest and greatest technology. Where I worked, in portfolio trading, we always had the highest speed PC's and servers supporting our investment decision-making process. While I have requested that Rampart, my former employer, attempt to locate my old e-mails from 1999 – August 2004, I have no idea if they have complied with my request or if those old e-mails even exist any longer.

Harry Markopolos

Harry Markopolos, CFA, CFE
Chartered Financial Analyst
Certified Fraud Examiner

Harry Markopolos

From: "Harry Markopolos" [redacted]
To: "Meaghan Cheung" [redacted]
Sent: Friday, November 04, 2005 11:58 AM
Attach: Resubmitted Madoff SEC Meeting.doc
Subject: Resubmitted Madoff SEC Meeting.doc

Meaghan,

1. Per a conversation with Mike Garrity of the Boston SEC this morning, attached is my 21-page report on why I believe that Madoff Investment Securities, LLC is the world's largest Ponzi Scheme. I made a presentation to Mike on October 25th, 2005 and he thought it would be more efficient if this case were sent directly to New York.

2. My contact information is: work #[redacted]nd Email:[redacted] My full name is Harry Markopolos, CFA. You can contac[redacted]Bergers, Esq., Boston's chief of enforcment, or Mike Garrity, branch chief for references on past work I have submitted to the SEC's Boston office.

3. You and the team leader on the case are always welcome to contact me. If you'd like to meet at your offices in New York, I can arrange other business and make a trip to NYC with about a week's notice.

I look forward to speaking with you at your convenience,

Regards,

Harry Markopolos, CFA
Financial Fraud Investigator
[redacted]

From: "Garrity, Michael" <GARRITYM@SEC.gov>
To: <harrymm@comcast.net>
Subject: Our Friends in New York
Date: Fri, 4 Nov 2005 14:54:17 +0000

Harry:

Here are the names and numbers we talked about this morning:

Doria Bachenheimer, 212-336-0024 (staff attorney); Meaghan Chung (212-336-0050 (branch chief).

Thanks.

mike garrity

#250

[Back]

From: "Garrity, Michael" [redacted]
To: [redacted]
Subject: RE: Our Friends in New York
Date: Fri, 4 Nov 2005 19:06:25 +0000

Cheungm@sec.gov

Glad you connected.

Thanks again.

Mike

From: harry[redacted]
Sent: Friday, [redacted]
To: Garrity, Michael
Subject: Re: Our Friends in New York

Mike,

I spoke to Meaghan Cheung late this morning, revealed my identity to her, agreed that she and her team leader would know my identity, and e-mailed her my revised 21-page report. She has my contact information and I expect to teleconference with her later today after she's read my report and come up with questions to ask. From now on I will be dealing strictly with New York on this matter.

Thank you very much for your assistance in moving this forward and getting it to the right folks in the New York Region,

Harry Markopolos, CFA
Financial Fraud Investigator
[redacted]

> -------------- Original message --------------
> Harry:
>
> Here are the names and numbers we talked about this morning:
>
> Doria Bachenheimer, 212-336-0024 (staff attorney); Meaghan Chung (212-336-0050 (branch chief).
>
> Thanks.
>
> mike garrity

[Back]

The World's Largest Hedge Fund is a Fraud

October 25, 2005 Presentation to the SEC
(modified and resubmitted November 4, 2005)
Madoff Investment Securities, LLC
www.madoff.com

Opening Remarks:

I am the original source for the information presented herein. There was no whistleblower or insider involved in compiling this report. I used the Mosaic Theory to assemble my set of observations. My observations were collected first-hand by listening to fund of fund investors talk about their investments in a hedge fund run by Madoff Investment Securities, LLC, a SEC registered firm. I have also spoken to the heads of various Wall Street equity derivative trading desks and every single one of the senior managers I spoke with told me that Bernie Madoff was a fraud. Of course, no one wants to take undue career risk by sticking their head up and saying the emperor isn't wearing any clothes....

I am a derivatives expert and have traded or assisted in the trading of several billion $US in options strategies for hedge funds and institutional clients. I have experience managing split-strike conversion products both using index options and using individual stock options, both with and without index puts. Very few people in the world have the mathematical background needed to manage these types of products but I am one of them. I have outlined a detailed set of Red Flags that make me very suspicious that Bernie Madoff's returns aren't real and, if they are real, then they are certainly generated by front-running.

Due to the sensitive nature of the case I detail below, its dissemination within the SEC must be limited to those with a need to know. The firm involved is located in the New York Region.

As a result of this case, several careers on Wall Street and in Europe will be ruined. Therefore, I have not signed nor put my name on this report. I request that my name not be released to anyone outside this SEC region without my express written permission. The fewer people who know who wrote this report the better. I am worried about the personal safety of myself and my family. Under no circumstances is this report or its contents to be shared with any other regulatory body without my express permission. This report has been written solely for the SEC's internal use.

As far as I know, none of the hedge fund, fund of funds (FOF's) mentioned in my report are engaged in a conspiracy to commit fraud. I believe they are naïve men and women with a notable lack of derivatives expertise and little or no quantitative finance ability.

There are 2 possible scenarios that involve fraud by Madoff Securities:

1. Scenario # 1 **(Unlikely):** I am submitting this case under Section 21A(e) of the 1934 Act in the event that the broker-dealer and ECN depicted is actually providing the stated returns to investors but is earning those returns by front-running customer order flow. Front-running qualifies as insider-trading since it relies upon material, non-public information that is acted upon for the benefit of one party to the detriment of another

party. Section 21A(e) allows the SEC to pay up to 10% of the total fines levied for insider-trading.

2. Scenario # 2 **(Highly likely)** Madoff Securities is the world's largest Ponzi Scheme. In this case there is no SEC reward payment due the whistle-blower so basically I'm turning this case in because it's the right thing to do. Far better that the SEC is proactive in shutting down a Ponzi Scheme of this size rather than reactive.

Who: The politically powerful Madoff family owns and operates a New York City based broker-dealer, ECN, and what is effectively the world's largest hedge fund. Bernard "Bernie" Madoff, the family patriarch started the firm.

According to the www.madoff.com website, "*Bernard L. Madoff was one of the five broker-dealers most closely involved in developing the NASDAQ Stock Market. He has been chairman of the board of directors of the NASDAQ Stock Market as well as a member of the board of governors of the NASD and a member of numerous NASD committees. Bernard Madoff was also a founding member of the International Securities Clearing Corporation in London.*

His brother, Peter B. Madoff *has served as vice chairman of the NASD, a member of its board of governors, and chairman of its New York region. He also has been actively involved in the NASDAQ Stock Market as a member of its board of governors and its executive committee and as chairman of its trading committee. He also has been a member of the board of directors of the Security Traders Association of New York. He is a member of the board of directors of the Depository Trust Corporation.*

What:

1. The family runs what is effectively the world's largest hedge fund with estimated assets under management of <u>at least $20 billion to perhaps $50 billion</u>, but no one knows exactly how much money BM is managing. That we have what is effectively the world's largest hedge fund operating underground is plainly put shocking. But then again, we don't even know the size of the hedge fund industry so none of this should be surprising. A super-sized fraud of this magnitude was bound to happen given the lack of regulation of these off-shore entities. My best guess is that approximately $30 billion is involved.
2. However the hedge fund isn't organized as a hedge fund by Bernard Madoff (BM) yet it acts and trades exactly like one. BM allows third party's to private label hedge funds that provide his firm, Madoff Securities, with equity tranch funding. In return for equity tranch funding, BM runs a trading strategy whose returns flow to the third party hedge funds and their investors who put up equity capital to fund BM's broker-dealer and ECN operations. *BM tells investors it earns its fees by charging commissions on all of the trades done in their accounts.*

   Red Flag # 1: *Why would a US broker-dealer organize and fund itself in such an unusual manner? Doesn't this seem to be an unseemly way of operating under the regulator's radar screens? Why aren't the commissions charged fully disclosed to investors? Can a SEC Registered Investment Advisor both charge commissions and charge a principle fee* *for trades? **MOST IMPORTANTLY**, why would BM settle for charging only undisclosed commissions when he could earn standard hedge fund fees of 1% management fee + 20% of the profits? Doing some simple math on BM's 12% average annual return stream to investors, the hedge fund, before fees, would have to be earning average annual returns of 16%. Subtract out the 1% management fee and investors are down to 15%. 20% of the profits would be (.20 x 15% = 3% profit participation) 3%, so investors would be left with the stated 12% annual returns listed in Attachment 1 (Fairfield Sentry Ltd. Performance Data). Total fees to the third party FOF's would amount to 4% annually. Now why would BM leave 4% in average annual fee revenue on the table unless he were a Ponzi Scheme? Or, is he charging a whole lot more than 4% in undisclosed commissions?*

3. The third parties organize the hedge funds and obtain investors but 100% of the money raised is actually managed by Madoff Investment Securities, LLC in a purported hedge fund strategy. The investors that pony up the money don't know that BM is managing their money. That Madoff is managing the money is purposely kept secret from the investors. Some prominent US based hedge fund, fund of funds, that "invest" in BM in this manner include:
   A. Fairfield Sentry Limited (Arden Asset Management) which had $5.2 billion invested in BM as of May 2005; 11th Floor, 919 Third Avenue; New York, NY 10022; Telephone 212.319.606; The Fairfield Greenwich Group is a global family of companies with offices in New York, London and Bermuda, and representative offices in the U.S., Europe and Latin America. Local operating entities are authorized or regulated by a variety of government agencies, including Fairfield Greenwich Advisors LLC, a U.S. SEC registered investment adviser, Fairfield Heathcliff Capital LLC, a U.S. NASD member broker-dealer, and Fairfield Greenwich (UK) Limited, authorized and regulated by the Financial Services Authority in the United Kingdom.
   B. Access International Advisors; www.aiagroup.com; a SEC registered investment advisor, telephone # 212.223.7167; Suite 2206; 509 Madison Avenue, New York, NY 10022 which had over $450 million invested with BM as of mid-2002. The majority of this FOF's investors are European, even though the firm is US registered.
   C. Broyhill All-Weather Fund, L.P. had $350 million invested with BM as of March 2000.
   D. Tremont Capital Management, Inc. Corporate Headquarters is located at 555 Theodore Fremd Avenue; Rye, New York 10580; T: (914) 925-1140 F: (914) 921-3499. Tremont oversees on an advisory and fully discretionary basis over $10.5 billion in assets. Clients include institutional investors, public and private pension plans, ERISA plans, university endowments, foundations, and financial institutions, as well as high net worth individuals. Tremont is owned by Oppenhiemer Funds Inc. which is owned by Mass Mutual Insurance Company so they should have sufficient reserves to make investors whole. Mass Mutual is currently under investigation by the Massachusetts Attorney General, the Department of Justice, and the SEC.
   E. During a 2002 marketing trip to Europe every hedge fund FOF I met with in Paris and Geneva had investments with BM. They all said he was their best manager! A partial list of money managers and Private Banks that invest in BM is included at the end of this report.
4. Here's what smells bad about the idea of providing equity tranch funding to a US registered broker-dealer:

A. The investment returns passed along to the third party hedge funds are equivalent to BM borrowing money. These 12 month returns from 1990 – May 2005 ranged from a low of 6.23% to a high of 19.98%, with an average 12 month return during that time period of 12.00%. No Broker-Dealer that I've ever heard of finances its operations at that high of an implied borrowing rate (source: Attachment 1; Fairfield Sentry Limited return data from December 1990 – May 2005).
B. BD's typically fund in the short-term credit markets and benchmark a significant part of their overnight funding to LIBOR plus or minus some spread.
C. **Red Flag # 2**: *why would a BD choose to fund at such a high implied interest rate when cheaper money is available in the short-term credit markets? One reason that comes to mind is that BM couldn't stand the due diligence scrutiny of the short-term credit markets.*

5. The third party hedge funds and fund of funds that market this hedge fund strategy that invests in BM don't name and aren't allowed to name Bernie Madoff as the actual manager in their performance summaries or marketing literature.
   Red Flag # 3: ***Why the need for such secrecy?*** *If I was the world's largest hedge fund and had great returns, I'd want all the publicity I could garner and would want to appear as the world's largest hedge fund in all of the industry rankings. Name one mutual fund company, Venture Capital firm, or LBO firm which doesn't brag about the size of their largest funds' assets under management. Then ask yourself, why would the world's largest hedge fund manager be so secretive that he didn't even want his LP's to know he was managing their money?*
6. The third party FOF's never tell investors who is actually managing their money and describe the investment strategy as: This hedge fund's objective is long term growth on a consistent basis with low volatility. The investment advisor invests exclusively in the U.S. and utilizes a strategy often referred to as a "split-strike conversion." Generally this style involves purchasing a basket of 30 – 35 large-capitalization stocks with a high degree of correlation to the general market (e.g. American Express, Boeing, Citigroup, Coca-Cola, Dupont, Exxon, General Motors, IBM, Merck, McDonalds). To provide the desired hedge, the manager then sells out-of-the-money OEX index call options and buys out-of-the-money OEX index put options. The amount of calls that are sold and puts that are bought represent a dollar amount equal to the basket of shares purchases.
7. I personally have run split-strike conversion strategies and know that BM's approach is far riskier than stated in 6 above. BM sells call options on individual stocks, rather than OEX Index call options, apparently to generate higher cash flows as individual stock call premiums are higher priced to compensate for the higher individual stock risks (individual stocks can more further and faster than stock indexes). Therefore BM's strategy of buying individual stocks, selling individual call options and buying index put options is a lot riskier and has a lot lower return potential than what is stated in the third party FOF marketing materials (in other words their marketing is a fraudulent representation of both the returns and the risks of this type of strategy). His strategy is wholly inferior to an all index approach and is wholly incapable of generating returns in the range of 6.23% to 19.98%. <u>BM's strategy should not be able beat the return on US Treasury Bills</u> Due to the glaring weakness of the strategy:

A. Income Part of the strategy is to buy 30 – 35 large-cap stocks, sell out-of-the-money individual stock call options against each of the 30-35 stocks. For each 100 shares of GM sell 1 out-of-the-money GM call option.

1. We earn income from the stock's dividends. Let's attribute a 2% average return to this source of funds for the 14 ½ year time period. This explains 2% of the 12% average annual returns and leaves 10% of the returns unexplained.
2. We earn income from the sale of equity call options against each 100 shares of stock that we own.

Red Flag # 4: *BM would have to sell short-dated, out-of-the-money calls against each of the 30-35 stocks. However, his winning stocks would quickly be called away leaving him with only the stocks in his stock basket that either didn't go up much, stayed the same, or went down. In other words this strategy is penalized for picking great stocks because those are the ones that get called away when you sell calls against them! This is the only strategy I know of where picking great stocks actually hurts performance! There's no way selling individual call options against these stocks offsets the stocks that go down in price. At best selling call options can return perhaps 2% annual returns. We've now explained 4% (2% dividend income + 2% call option premium) of the 12% average annual returns, leaving 8% unexplained.*

B. Protection Part of the strategy is to buy out-of-the-money OEX index put options. This costs you money each and every month. This hurts your returns and is the main reason why BM's strategy would have trouble earning 0% average annual returns much less the 12% returns stated in Fairfield Sentry Ltd.'s performance summary. Even if BM earns a 4% return from the combination of 2% stock dividends and 2% from the sale of call options, the cost of the puts would put this strategy in the red year in and year out. No way he can possibly be earning 12%. The math just doesn't support this strategy if he's really buying index put options.

Red Flag # 5: *Assuming BM bought 3 month out-of-the-money OEX put options that are 3% out-of-the-money, and that he paid 3% for them, then the market would have to drop 6% in order for his investors to recoup their cost on the puts. More importantly, the individual stock call options sold against each stock holding would not earn enough of a return to offset losses in the stocks during periods of significant market decline. Yet BM had only ONE MONTHLY LOSS OF 6 BASIS POINTS during 1997's Asian Currency Crises, the 1998 Russian & LTCM Crises and the market blood bath of 2000 – 2002. According to Fairfield Sentry Limited's return data (Attachment 1), BM posted a* ***-0.06%*** *loss in August 2002. These return numbers are way too good to be true! And, in my experience, whenever a hedge fund has posted returns that are too good to be true they've turned out not to be true.*

C. The OEX index (S&P 100) closed at 544.50 on Friday, October 17, 2005 meaning that each put option hedged $54,450 dollars worth of stock ($100 contract multiplier x 544.50 index value = $54,450 in stock hedged). As of that same date, the total open interest for all OEX index put options was 339,810 contracts meaning that a total of $18,502,654, 500 in stock was being hedged by the use of OEX index puts (339,810 total put contracts in existence as of Oct 17th x $54,450 hedge value of 1 OEX index put = $18, 502,654,500 in stock hedged).

Red Flag # 6: *At my best guess level of BM's assets under management of $30 billion, or even at my low end estimate of $20 billion in assets under management, BM would have to be over 100% of the total OEX put option contract open interest in order to hedge his stock holdings as depicted in the third party hedge funds marketing literature. In other words, there are not enough index option put contracts in existence to hedge the way BM says he is hedging!*

D. Mathematically I have proven that BM cannot be hedging using listed index put options. One hedge fund FOF has told me that BM uses only Over-the-Counter options and trades exclusively thru UBS and Merrill Lynch. I have not called those two firms to check on this because it seems implausible that a BD would trade $20 - $50 billion worth of index put options per month over-the-counter thru only 2 firms. That plus the fact that if BM was really buying OTC index put options, then there is no way his average annual returns could be positive!! At a minimum, using the cheapest way to buy puts would cost a fund 8% per year. To get the put cost down to 8%, BM would have to buy a one-year at-the-money put option and hold it for one-year. No way his call sales could ever hope to come even fractionally close to covering the cost of the puts.

Red Flag # 7: *The counter-party credit exposures for UBS and Merrill would be too large for these firms credit departments to approve.*

Red Flag # 8: *OTC options are more expensive to trade than listed options. Trading in the size of $20 - $50 billion per month would be impossible and the bid-ask spreads would be so wide as to preclude earning any profit whatsoever. These Broker/Dealers would need to offset their short OTC index put option exposure to a falling stock market by hedging out their short put option risk by either buying listed put options or selling short index futures and the derivatives markets are not deep and liquid enough to accomplish this without paying a penalty in prohibitively expensive transaction costs.*

Red Flag # 9: *Extensive and voluminous paperwork would be required to keep track of and clear each OTC trade.*

E. My experience with split-strike conversion trades is that the best a good manager is likely to obtain using the strategy marketed by the third-party FOF's is T-bills less management fees. And, if the stock market is down by more than 2%, the return from this strategy will range from a high of zero return to a low of a few percent depending upon your put's cost and how far out-of-the-money it is.

F. In 2000 I ran a regression of BM's hedge fund returns using the performance data from Fairfield Sentry Limited. BM had a .06 correlation to the equity market's return which confirms the .06 Beta that Fairfield Sentry Limited lists in its return numbers.

Red Flag # 10: *It is mathematically impossible for a strategy using stock, individual stock call options and index put options to have such a low correlation to the market where its returns are supposedly being generated from. This makes no sense! The strategy depicted retains single-stock downside risk since they own only index put options and not single stock put options. Therefore if one or more stocks in their portfolio were to tank on bad news, BM's index put would offer little protection and their portfolio should feel the pain. However, BM's performance numbers show only 7 extremely small losses during 14 ½ years and* *these numbers are too good to be true. The largest one month loss was only -55 basis points (-0.55%) or just over one-half of one percent! And BM never had more than a one month losing streak! Either BM is the world's best stock and options manager that the SEC and the investing public has **never** heard of or he's a fraud.*

8. **Red Flag # 11** *Two press articles do doubt Bernie Madoff's returns and they are:*
    A. The May 7, 2001 edition of Barron's, in an article entitled, ***"Don't Ask, Don't Tell; Bernie Madoff is so secretetive, he even asks his investors to keep mum,"*** written by Erin Arvedlund, published an expose about Bernie Madoff a few years ago with no resulting investigation by any regulators. Ms. Arvedlund has since left Barron's. I have attached a copy of the Barrons' article which lists numerous red flags.
    B. Michael Ocrant, formerly a reporter for MAR Hedge visited Bernie Madoff's offices and wrote a very negative article that doubted the source of BM's returns. He reported to a colleague that he saw some very unusual things while at Madoff's offices. The SEC should contact him. Michael Ocrant is currently serving as the Director of Alternative Investments; Institutional Investor; New York, NY 10001; Telephone # 212-224-3821 or 212-213-6202; Email: mocrant@iiconferences.com

9. Fund of funds with whom I have spoken to that have BM in their stable of funds continually brag about their returns and how they are generated thanks to BM's access to his broker-dealer's access to order flow. They believe that BM has perfect knowledge of the market's direction due to his access to customer order flow into his broker-dealer. **Red Flag # 12:** *Yes, BM has access to his customer's order flow thru his broker-dealer but he is only one broker out of many, so it is impossible for him to know the market's direction to such a degree as to only post monthly losses once every couple of years. All of Wall Street's big wire houses experience trading losses on a more regular frequency that BM. Ask yourself how BM's trading experience could be so much better than all of the other firms on Wall Street. Either he's the best trading firm on the street and rarely ever has large losing months unlike other firms or he's a fraud.*
10. **Red Flag # 13:** *I believe that BM's returns can be real ONLY if they are generated from front-running his customer's order flow. In other words, yes, if he's buying at a penny above his customer's buy orders, he can only lose one penny if the stock drops but can make several pennies if the stock goes up. For example, if a customer has an order to buy 100,000 shares of IBM at $100, BM can put in his own order to buy 100,000 share of IBM at $100.01. This is what's known as a right-tail distribution and is very similar to the payoff distribution of a call option. Doing this could easily generate returns of 30% - 60% or more per anum. He could be doing the same thing by front-running customer sell orders. However, if BM's returns are real but he's generating them from front-running there are two problems with this:*
    A. *Problem # 1: front-running is one form of insider-trading and is illegal*
    B. *Problem # 2: generating real returns from front-running but telling hedge fund investors that you are generating the returns via a complex (but unworkable) stock and options strategy is securities fraud.*

Some time ago, during different market conditions, I ran a study using the Black-Scholes Option Pricing Model to analyze the value of front-running with the goal of putting a monetary value on front-running where the insider knew the customer's order and traded ahead of it. When I ran the study the model inputs were valued at: OEX component stocks annualized volatility on a cap-weighted basis was 50% (during a bear market period), the T-bill rate was 5.80%, and the average stock price was $46. I then calculated the value of an at-the-money call options over time intervals of 1 minute, 5 minutes, 10 minutes, and 15 minutes. I used a 253 trading day year. The SEC should be able to duplicate these results:

1 minute option = 3 cents worth of trade information value
5 minute option = 7 cents worth of trade information value
10 minute option = 10 cents worth of trade information value
15 minute option = 12 cents worth of trade information value

Conclusion: Bernie Madoff used to advertise in industry trade publications that he would pay 1 cent for other broker's order flow. If he was paying 1 cent for order flow and front-running these broker's customers, then he could easily be earning returns in the 30% - 60% or higher annually. In all time intervals ranging from 1 minute to 15 minutes, having access to order flow is the monetary equivalent of owning a valuable call option on that order. The value of these implicit call options ranges between 3 – 12 times the one penny per share paid for access to order flow. If this is what he's doing, then the returns are real but the stated investment strategy is illegal and based solely on insider-trading.

NOTE: I am pretty confident that BM is a Ponzi Scheme, but in the off chance he is front-running customer orders and his returns are real, then this case qualifies as insider-trading under the SEC's bounty program as outlined in Section 21A(e) of the 1934 Act. However, if BM was front-running, a highly profitable activity, then he wouldn't need to borrow funds from investors at 12% implied interest. Therefore it is far more likely that BM is a Ponzi Scheme. Front-running is a very simple fraud to commit and requires only access to inside information. The elaborateness of BM's fund-raising, his need for secrecy, his high 12% average cost of funds, and reliance on a derivatives investment scheme that few investors (or regulators) would be capable of comprehending lead to a weight of the evidence conclusion that this is a Ponzi Scheme.

11. **Red Flag # 14:** *Madoff subsidizes down months! Hard to believe (and I don't believe this) but I've heard two investors tell me that they don't believe Madoff can make money in big down months either. They tell me that Madoff "subsidizes" their investors in down months, so that they will be able to show a low volatility of returns. These types of stories are commonly found around Ponzi Schemes. These investors tell me that Madoff only books winning tickets in their accounts and "eats the losses" during months when the market sells off hard. The problem with this is that it's securities fraud to misstate either returns or the volatility of those returns. These FOF professionals who heard BM tell them that he subsidizes losses were professionally negligent in not turning BM into the SEC, FSA and other regulators for securities fraud.*

Red Flag # 15: *Why would a fund of funds investor believe any broker-dealer that commits fraud in a few important areas – such as misstating returns and misstating volatility of returns – yet believe him in other areas? I'd really like to believe in the tooth fairy, but I don't after catching my mother putting a quarter underneath my pillow one night.*

12. **Red Flag # 16**: *Madoff has perfect market-timing ability. One investor told me, with a straight face, that Madoff went to 100% cash in July 1998 and December 1999, ahead of market declines. He said he knows this because Madoff faxes his trade tickets to his firm and the custodial bank. However, since Madoff owns a broker-dealer, he can generate whatever trade tickets he wants. And, I'll bet very few FOF's ask BM to fax them trade tickets.*
13. **Red Flag # 17**: *Madoff does not allow outside performance audits. One London based hedge fund, fund of funds, representing Arab money, asked to send in a team of Big 4 accountants to conduct a performance audit during their planned due diligence. They were told "No, only Madoff's brother-in-law who owns his own accounting firm is allowed to audit performance for reasons of secrecy in order to keep Madoff's proprietary trading strategy secret so that nobody can copy it. Amazingly, this fund of funds then agreed to invest $200 million of their client's money anyway, because the low volatility of returns was so attractive!! Let's see, how many hedge funds have faked an audited performance history?? Wood River is the latest that comes to mind as does the Manhattan Fund but the number of bogus hedge funds that have relied upon fake audits has got to number in the dozens.*
14. **Red Flag # 18:** *Madoff's returns are not consistent with the one publicly traded option income fund with a history as long as Madoff's. In 2000, I analyzed the returns of Madoff and measured them against the returns of the Gateway Option Income Fund (Ticker GATEX). During the 87 month span analyzed, Madoff was down only 3 months versus GATEX being down 26 months. GATEX earned an annualized return of 10.27% during the period studied vs. 15.62% for Bernie Madoff and 19.58% for the S&P 500.*
15. **Red Flag # 19**: *There have been several option income funds that went IPO since August 2004. None of them have the high returns that Bernie Madoff has. How can this be, they use similar strategies only they should be making more than BM in up months because most of these option income funds don't buy expensive index put options to protect their portfolios. Thus the publicly traded option income funds should make more money in up markets and lose more than Madoff in down markets. Hmm....that Madoff's returns are so high yet he buys expensive put options is just another reason to believe he is running the world's largest Ponzi Scheme. A good study for the SEC would be to compare 2005 performance of the new option income funds to Bernie Madoff while accounting for the cost of Bernie's index put option protection. There's no way Bernie can have positive returns in 2005 given what the market's done and where volatility is.*
16. **Red Flag # 20**: *Madoff is suspected of being a fraud by some of the world's largest and most sophisticated financial services firms. Without naming names, here's an abbreviated tally:*
    A. A managing director at Goldman, Sachs prime brokerage operation told me that his firm doubts Bernie Madoff is legitimate so they don't deal with him.

B. From an Email I received this past June 2005 I now suspect that the end is near for BM. All Ponzi Schemes eventually topple of their own weight once they become too large and it now appears that BM is having trouble meeting redemptions and is attempting to borrow sizeable funds in Europe.

ABCDEFGH and I had dinner with a savvy European investor that studies the HFOF market. He stated that both RBC and Socgen have removed Madoff some time ago from approved lists of individual managers used by investors to build their own tailored HFOFs.

More importantly, Madoff was turned down, according to this source, for a borrowing line from a Euro bank, I believe he said Paribas. Now why would Madoff need to borrow more funds? This Euro Investor said that Madoff was in fact running "way over" our suggested $12-14 billion (Fairfield Sentry is running $5.3 BB by themselves!) . Madoff's 12 month returns is about 7% net of the feeder fund's fees. Looks like he is stepping down the pay out.

C. An official from a Top 5 money center bank's FOF told me that his firm wouldn't touch Bernie Madoff with a ten foot pole and that there's no way he's for real.

17. **Red Flag # 21:** *ECN's didn't exist prior to 1998. Madoff makes verbal claims to his third party hedge FOF's that he has private access to ECN's internal order flow, which Madoff pays for, and that this is a substantial part of the return generating process. If this is true, then where did the returns come from in the years 1991 – 1997, prior to the ascendance of the ECN's? Presumably, prior to 1998, Madoff only had access to order flow on the NASDAQ for which he paid 1 cent per share for. He would have no such advantage pre-1998 on the large-cap, NYSE listed stocks the marketing literature says he buys (Exxon, McDonalds, American Express, IBM, Merck, etc...).*

18. **Red Flag # 22:** *The Fairfield Sentry Limited Performance Chart (Attachment 1) depicted for Bernie Madoff's investment strategy are misleading. The S&P 500 return line is accurate because it is moving up and down, reflecting positive and negative returns. Fairfield Sentry's performance chart is misleading, it is almost a straight line rising at a 45 degree angle. This chart cannot be cumulative in the common usage of the term for reporting purposes, which means "geometric returns." The chart must be some sort of arithmetic average sum, since a true cumulative return line, given the listed monthly returns would be exponentially rising (i.e. curving upward at an increasing rate). My rule of thumb is that if the manager misstates his performance, you can't trust him. Yet somehow Madoff is now running the world's largest, most clandestine hedge fund so clearly investors aren't doing their due diligence.*

19. **Red Flag # 23:** *Why is Bernie Madoff borrowing money at an average rate of 12.00% per anum and allowing these third party hedge fund, fund of funds to pocket their 1% and 20% fees bases upon Bernie Madoff's hard work and brains? Does this make any sense at all? Typically FOF's charge only 1% and 10%, yet BM allows them the extra 10%. Why? And why do these third parties fail to mention Bernie Madoff in their marketing literature? After all he's the manager, don't the LP's have a right to know who's managing their money?*

20. **Red Flag # 24:** *Only Madoff family members are privy to the investment strategy. Name one other prominent multi-billion dollar hedge fund that doesn't have outside, non-family professionals involved in the investment process. You can't because there aren't any. Michael Ocrant, the former MAR Hedge Reporter listed above saw some highly suspicious red flags during his visit to Madoff's offices and should be interviewed by the SEC as soon as possible.*

21. **Red Flag # 25:** *The Madoff family has held important leadership positions with the NASD, NASDAQ, SIA, DTC, and other prominent industry bodies therefore these organizations would not be inclined to doubt or investigate Madoff Investment Securities, LLC. The NASD and NASDAQ do not exactly have a glorious reputation as vigorous regulators untainted by politics or money.*

22. **Red Flag # 26:** *BM goes to 100% cash for every December 31st year-end. This allows for "cleaner financial statements" according to one source. Any unusual transfers or activity near a quarter-end or year-end is a red flag for fraud. Recently, the BD REFCO Securities engaged in "fake borrowing" with Liberty, a hedge fund, that made it appear that Liberty owed REFCO over $400 million in receivables. This allowed REFCO to mask its true debt position and made all of their equity ratios look better than they actually were.*

23. **Red Flag # 27:** *Several equity derivatives professionals will all tell you that the split-strike conversion strategy that BM runs is an outright fraud and cannot possibly achieve 12% average annual returns with only 7 down months during a 14 ½ year time period. Some derivatives experts that the SEC should call to hear their opinions of how and why BM is a fraud and for some insights into the mathematical reasons behind their belief, the SEC should call:*

A. Leon Gross, Managing Director of Citigroup's world-wide equity derivatives research unit; [redacted] New York, NY [redacted] Tel# [redacted] or [redacted] or leon.j.gross@citigroup.com [Leon can't believe that the SEC hasn't shut down Bernie Madoff yet. He's also amazed that FOF's actually believe this stupid options strategy is capable of earning a positive return much less a 12% average annual return. He thinks the strategy would have trouble earning 1% much less 12%. Leon is a free spirit, so if you ask him he'll tell you but you'd understand it better if you met him at his workplace in a private conference room. He talks derivatives at a high level, so ask simple "yes or no" type questions to start off the interview then drill down.]

B. Walter "Bud"Haslett, CFA; Write Capital Management, LLC; Suite [redacted] NJ [redacted] Tel#: [redacted] or bud.haslett@[redacted] www.writecapital.com [Bud's firm runs myriad options related strategies and he knows all of the math.]

C. Joanne Hill, Ph.D.; Vice-President and global head of equity derivatives research, Goldman Sachs (NY), [redacted] New York [redacted] Tel# [redacted]

24. **Red Flag # 28:** *BM's Sharpe Ratio of 2.55 (Attachment 1: Fairfield Sentry Ltd. Performance Data) is UNBELIEVABLY HIGH compared to the Sharpe Ratios experienced by the rest of the hedge fund industry. The SEC should obtain industry hedge fund rankings and see exactly how outstanding Fairfield Sentry Ltd.'s Sharpe Ratio is.*

Conclusions:

1. Bernie Madoff is running the world's largest unregistered hedge fund. He's organized this business as "hedge fund of funds private labeling their own hedge funds which Bernie Madoff **secretly** runs for them using a split-strike conversion strategy getting paid only trading commissions which are not disclosed." If this isn't a regulatory dodge, I don't know what is. This is back-door marketing and financing scheme that is opaque and rife with hidden fees (he charges only commissions on the trades). If this product isn't marketed correctly, what is the chance that it is managed correctly? I say that where there's one cockroach in plain sight, many more are lurking behind the corner out of plain view.

2. There are too many red flags to ignore.

3. Mathematically this type of split-strike conversion fund should never be able to beat US Treasury Bills much less provide 12.00% average annual returns. I and other derivatives professionals on Wall Street will swear up and down that a split-strike conversion strategy cannot earn an average annual return anywhere near 12%.

4. I have presented 174 months (14 ½ years) of Fairfield Sentry's return numbers dating back to December 1990. Only 7 months or 4% of the months saw negative returns. Classify this as "definitely too good to be true!" No major league baseball hitter bats .960, no NFL team has ever gone 96 wins and only 4 losses over a 100 game span, and you can bet everything you own that no money manager is up 96% of the months either. It is inconceivable that BM's largest monthly loss could only be -0.55% and that his longest losing streaks could consist of 1 slightly down month every couple of years. Nobody on earth is that good of a money manager unless they're front-running.

5. BM would have to be trading more than 100% of the open interest of OEX index put options every month. Every large derivatives dealer on Wall Street will tell you that Bernie Madoff is a fraud. Go ask the heads of equity derivatives trading at Morgan Stanley, Goldman Sachs, JP Morgan and Citigroup their opinions about Bernie Madoff. They'll all tell the SEC that they can't believe that BM hasn't been caught yet.

6. The SEC is slated to start overseeing hedge funds in February 2006, yet since Bernie Madoff is not registered as a hedge fund but acting as one but via third party shields, the chances of Madoff escaping SEC scrutiny are very high. If I hadn't written this report, there's no way the SEC would have known to check the facts behind all of these third party hedge funds.

Potential Fall Out if Bernie Madoff turns out to be a Ponzi Scheme:

1. If the average hedge fund is assumed to be levered 4:1, it doesn't take a rocket scientist to realize that there might be anywhere from a few hundred billion on up in selling pressure in the wake of a \$20 - \$50 billion hedge fund fraud. With the hedge fund market estimated to be \$1 trillion, having one hedge fund with 2% - 5% of the industry's assets under management suddenly blow up, it is hard to predict the severity of the resulting shock wave. You just know it'll be unpleasant for anywhere from a few days to a few weeks but the fall out shouldn't be anywhere near as great as that from the Long Term Capital Management Crises.

2. Hedge fund, fund of funds with greater than a 10% exposure to Bernie Madoff will likely be faced with forced redemptions. This will lead to a cascade of panic selling in all of the various hedge fund sectors whether equity related or not. Long –short and market neutral managers will take losses as their shorts rise and their longs fall. Convertible arbitrage managers will lose as the long positions in underlying bonds are sold and the short equity call options are bought to close. Fixed income arbitrage managers will also face losses as credit spreads widen. Basically, most hedge funds categories with two exceptions will have at least one big down month thanks to the unwinding caused by forced redemptions. Dedicated Short Funds and Long Volatility Funds are the two hedge fund categories that will do well.

3. The French and Swiss Private Banks are the largest investors in Bernie Madoff. This will have a huge negative impact on the European capital markets as several large fund of funds implode. I figure one-half to three-quarters of Bernie Madoff's funds come from overseas. The unwinding trade will hurt all markets across the globe but it is the Private European Banks that will fare the worst.

4. European regulators will be seen as not being up to the task of dealing with hedge fund fraud. Hopefully this scandal will serve as a long overdue wake-up call for them and result in increased funding and staffing levels for European Financial Regulators.

5. In the US Fairfield Sentry, Broyhill, Access International Advisors, Tremont and several other hedge fund, fund of funds will all implode. There will be a call for increased hedge fund regulation by scared and battered high net worth investors.

6. The Wall Street wire house FOF's are not invested in Madoff's strategy. As far as I know the wire house's internal FOF's all think he's a fraud and have avoided him like the plague. But these very same wire houses often own highly profitable hedge fund prime brokerage operations and these operations will suffer contained, but painful nonetheless, losses from loans to some hedge funds that go bust during the panic selling. As a result, I predict that some investment banks will pull out of the prime brokerage business deeming it too volatile from an earnings standpoint. Damage to Wall Street will be unpleasant in that hedge funds and FOF's are a big source of trading revenues. If the hedge fund industry fades, Wall Street will need to find another revenue source to replace them. Overall this will hurt Wall Street but not nearly as severely as LTCM. LTCM in

hurricane terms was a Category 5 storm. BM is only going to be a Category 2 or 3 storm where the severe damage is confined mostly to the hedge fund arena.

7. US Mutual fund investors and other long-term investors in main stream investment products will only feel a month or two's worth of pain from the selling cascade in the hedge fund arena but their markets should recover afterwards.

8. Congress will be up in arms and there will be Senate and House hearings just like there were for Long Term Capital Management.

9. The SEC's critics who say the SEC shouldn't be regulating private partnerships will be forever silenced. Hopefully this leads to expanded powers and increased funding for the SEC. Parties that opposed SEC entry into hedge fund regulation will fall silent. The SEC will gain political strength in Washington from this episode but only if the SEC is proactive and launches an immediate, full scale investigation into all of the Red Flags surrounding Madoff Investment Securities, LLC. Otherwise, it is almost certain that NYAG Elliot Spitzer will launch his investigation first and once again beat the SEC to the punch causing the SEC further public embarrassment.

10. Hedge funds will face increased due diligence from regulators, investors, prime brokers and counter-parties which is a good thing and long overdue.

Potential Fall Out if Bernie Madoff is found out to be front-running customer order flow:

1. This would be just one more black eye among many for the brokerage industry and the NYSE and NASDAQ. At this point the reputations of both the NYSE and NASDAQ are already at rock bottom, so there's likely little downside left for these two troubled organizations.

2. The industry wouldn't miss a beat other than for the liquidation of Madoff Investment Securities, LLC. Figure it will be similar to REFCO's demise only there won't be a buyer of the firm given that they cheated customers who would all be embarrassed to remain customers once the news they've been ripped off is on the front-pages. These former customers are more likely to sue for damages than remain customers. Unsecured lenders would face losses but other than that the industry would be better off.

3. At least the returns are real, in which case determining restitution could keep the courts busy for years. The Class Action Bar would be thrilled. A lot of the FOF's are registered offshore in places where the long arm of the law might not reach. My guess is that the fight for the money off-shore would keep dozens of lawyers happily employed for many years.

4. The FOF's would suffer little in the way of damage. All could be counted on to say "*We didn't know the manager was generating returns illegally. We relied upon the NYSE and NASDAQ to regulate their markets and prevent front-running therefore we see no reason to return any funds.*"

Attachments:

1. 2 page Summary of Fairfield Sentry Ltd with performance data from December 1990 – May 2005

2. Copy of the May 7, 2001 Barrons' article, ***"Don't Ask, Don't Tell; Bernie Madoff is so secretetive, he even asks his investors to keep mum,"*** written by Erin E. Arvedlund.

3. Partial list of French and Swiss money-managers and private banks with investments in Bernie Madoff's hedge fund. Undoubtedly there are dozens more European FOF's and Private Banks that are invested with BM.

Separate Attachments Not Included in this document:

4. 2 page offering memorandum, faxed March 29, 2001, for an investment in the investment program run by Madoff Investment Securities, LLC. I do not know who the source was who faxed this document since the fax heading is blank.

ATTACHMENT 1: Fairfield Sentry Performance Data

Fairfield Sentry Ltd

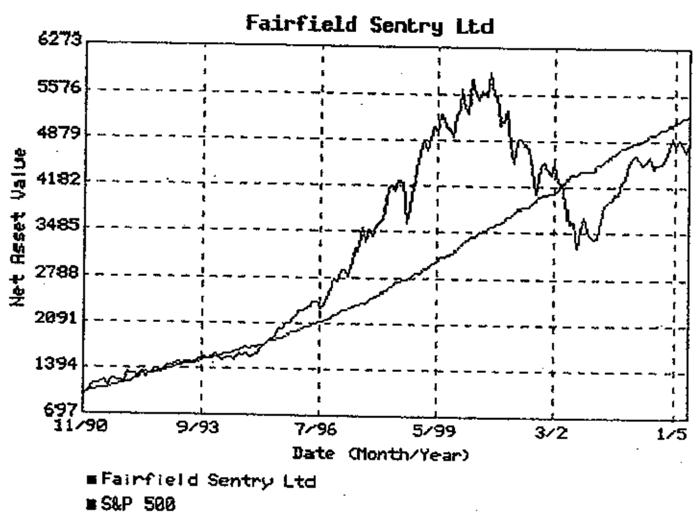
Fund Category(s):
Long/Short Equity

Strategy Description:
The Fund seeks to obtain capital appreciation of its assets principally through the utilization of a nontraditional options trading strategy described as "split strike conversion", to which the Fund allocates the predominant portion of its assets. This strategy has defined risk and profit parameters, which may be ascertained when a particular position is established. Set forth below is a description of the "split strike conversion" strategies ("SSC Investments"). The establishment of a typical position entails (i) the purchase of a group or basket of equity securities that are intended to highly correlate to the S&P 100 Index, (ii) the sale of out-of-the-money S&P 100 Index call options in an equivalent contract value dollar amount to the basket of equity securities, and (iii) the purchase of an equivalent number of out-of-the-money S&P 100 Index put options. An index call option is out-of-the-money when its strike price is greater than the current price of the index; an index put option is out-of-the-money when the strike price is lower than the current price of the index. The basket typically consists of approximately 35 to 45 stocks in the S&P 100. The logic of this strategy is that once a long stock position has been established, selling a call against such long position will increase the standstill rate of return, while allowing upward movement to the short call strike price. The purchase of an out-of-the-money put, funded with part or all of the call premium, protects the equity position from downside risk. A bullish or bearish bias of the positions can be achieved by adjustment of the strike prices in the S&P 100 puts and calls. The further away the strike prices are from the price of the S&P 100, the more bullish the strategy. However, the dollar value underlying the put options always approximates the value of the basket of stocks.

Contact Info		Fees & Structure	
Fund:	Fairfield Sentry Ltd	Fund Assets:	$5100.00million
General Partner:	Arden Asset Management	Strategy Assets:	$5300.00million
Address:	919 Third Avenue 11th th Floor New York NY 10022 USA	Firm Assets:	$8300million
		Min. Investment:	$ 0.10million
		Management Fee:	1.00%
		Incentive Fee:	20.00%
Tel:	212-319-6060	Hurdle Rate:	
Fax:		High Water Mark:	Yes
Email:	fairfieldfunds@fggus.com	Additions:	Monthly
Contact Person:	Fairfield Funds	Redemptions:	Monthly
Portfolio Manager:		Lockup:	
		Inception Date:	Dec-1990
		Money Invested In:	United States
		Open to New Investments:	Yes

Annual Returns

1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
2.83%	18.58%	14.67%	11.68%	11.49%	12.95%	12.99%	14.00%	13.40%	14.18%	11.55%	10.68%	9.33%	8.21%	7.07%	2.52%



Year To Date:	2.52%
Highest 12 Month Return:	19.98%
Lowest 12 Month Return:	6.23%
Average Annual Return:	12.00%
Average Monthly Return:	0.96%
Highest Monthly Return:	3.36%
Lowest Monthly Return:	-0.56%
Average Gain:	1.01%
Average Loss:	-0.24%
Profitable Percentage:	95.98%
Compounded Monthly Return:	0.96%
Longest Losing Streak:	**1 mo.**
Maximum Drawdown:	-0.55%

Sharpe Ratio (Rolling 12):	2.56
Sharpe Ratio (Annualized):	**2.55**
Std. Dev. (Monthly):	0.75%
Std. Dev. (Rolling 12):	2.74%
Beta:	**0.06**
Alpha:	0.91
R:	0.30
R Squared:	0.09

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
1990	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	2.83% E
1991	3.08% E	1.46% E	0.59% E	1.39% E	1.88% E	0.37% E	2.04% E	1.07% E	0.80% E	2.82% E	0.08% E	1.63% E
1992	0.49% E	2.79% E	1.01% E	2.86% E	-0.19%	1.29% E	0.00% E	0.92% E	0.40% E	1.40% E	1.42% E	1.43% E
1993	0.00% E	1.93% E	1.86% E	0.06% E	1.72% E	0.86% E	0.09% E	1.78% E	0.35% E	1.77% E	0.26% E	0.45% E
1994	2.18% E	-0.36%	1.52% E	1.82% E	0.51% E	0.29% E	1.78% E	0.42% E	0.82% E	1.88% E	-0.56%	0.66% E
1995	0.92% E	0.76% E	0.84% E	1.69% E	1.72% E	0.50% E	1.08% E	-0.16%	1.70% E	1.60% E	0.51% E	1.10% E
1996	1.49% E	0.73% E	1.23% E	0.64% E	1.41% E	0.22% E	1.92% E	0.27% E	1.22% E	1.10% E	1.58% E	0.48% E
1997	2.45% E	0.73% E	0.86% E	1.17% E	0.63% E	1.34% E	0.75% E	0.35% E	2.39% E	0.55% E	1.56% E	0.42% E
1998	0.91% E	1.29% E	1.75% E	0.42% E	1.76% E	1.28% E	0.83% E	0.28% E	1.04% E	1.93% E	0.84% E	0.33% E
1999	2.06% E	0.17% E	2.29% E	0.36% E	1.51% E	1.76% E	0.43% E	0.94% E	0.73% E	1.11% E	1.61% E	0.39% E
2000	2.20% E	0.20% E	1.84% E	0.34% E	1.37% E	0.80% E	0.65% E	1.32% E	0.25% E	0.92% E	0.68% E	0.43% E
2001	2.21% E	0.14% E	1.13% E	1.32% E	0.32% E	0.23% E	0.44% E	1.01% E	0.73% E	1.28% E	1.21% E	0.19% E
2002	0.03% E	0.60% E	0.46% E	1.16% E	2.12% E	0.26% E	3.36% E	-0.06%	0.13% E	0.73% E	0.16% E	0.06% E
2003	-0.27%	0.04% E	1.97% E	0.10% E	0.95% E	1.00% E	1.44% E	0.22% E	0.93% E	1.32% E	-0.08%	0.32% E
2004	0.94% E	0.50% E	0.05% C	0.43% C	0.66% C	1.28% C	0.08% C	1.33% E	0.53% E	0.03% E	0.79% E	0.24% E
2005	0.51% E	0.37% E	0.85% C	0.14% C	0.63% C	N/A	N/A	N/A	N/A	N/A	N/A	N/A

END ATTACHEMENT # 1 FAIRFIELD SENTRY LTD. PERFORMANCE DATA

Attachment 2: Barron's Article dated May 7, 2001

"Don't Ask, Don't Tell"

Bernie Madoff is so secretive, he even asks investors to keep mum

By ERIN E. ARVEDLUND
Barron's | Monday, May 7, 2001

Two years ago, at a hedge-fund conference in New York, attendees were asked to name some of their favorite and most-respected hedge-fund managers. Neither George Soros nor Julian Robertson merited a single mention. But one manager received lavish praise: Bernard Madoff.

Folks on Wall Street know Bernie Madoff well. His brokerage firm, Madoff Securities, helped kick-start the Nasdaq Stock Market in the early 1970s and is now one of the top three market makers in Nasdaq stocks. Madoff Securities is also the third-largest firm matching buyers and sellers of New York Stock Exchange-listed securities. Charles Schwab, Fidelity Investments and a slew of discount brokerages all send trades through Madoff.

Some folks on Wall Street think there's more to how Madoff (above) generates his enviable stream of investment returns than meets the eye. Madoff calls these claims "ridiculous."

But what few on the Street know is that Bernie Madoff also manages $6 billion-to-$7 billion for wealthy individuals. That's enough to rank Madoff's operation among the world's three largest hedge funds, according to a May 2001 report in MAR Hedge, a trade publication.

What's more, these private accounts, have produced compound average annual returns of 15% for more than a decade. Remarkably, some of the larger, billion-dollar Madoff-run funds have never had a down year.

When Barron's asked Madoff Friday how he accomplishes this, he said, "It's a proprietary strategy. I can't go into it in great detail."

Nor were the firms that market Madoff's funds forthcoming when contacted earlier. "It's a private fund. And so our inclination has been not to discuss its returns," says Jeffrey Tucker, partner and co-founder of Fairfield Greenwich, a New York City-based hedge-fund marketer. "Why Barron's would have any interest in this fund I don't know." One of Fairfield Greenwich's most sought-after funds is Fairfield Sentry Limited. Managed by Bernie Madoff, Fairfield Sentry has assets of $3.3 billion.

A Madoff hedge-fund offering memorandums describes his strategy this way: "Typically, a position will consist of the ownership of 30-35 S&P 100 stocks, most correlated to that index, the

sale of out-of-the-money calls on the index and the purchase of out-of-the-money puts on the index. The sale of the calls is designed to increase the rate of return, while allowing upward movement of the stock portfolio to the strike price of the calls. The puts, funded in large part by the sale of the calls, limit the portfolio's downside."

Among options traders, that's known as the "split-strike conversion" strategy. In layman's terms, it means Madoff invests primarily in the largest stocks in the S&P 100 index -- names like General Electric, Intel and Coca-Cola. At the same time, he buys and sells options against those stocks. For example, Madoff might purchase shares of GE and sell a call option on a comparable number of shares -- that is, an option to buy the shares at a fixed price at a future date. At the same time, he would buy a put option on the stock, which gives him the right to sell shares at a fixed price at a future date.

The strategy, in effect, creates a boundary on a stock, limiting its upside while at the same time protecting against a sharp decline in the share price. When done correctly, this so-called market-neutral strategy produces positive returns no matter which way the market goes.

Using this split-strike conversion strategy, Fairfield Sentry Limited has had only four down months since inception in 1989. In 1990, Fairfield Sentry was up 27%. In the ensuing decade, it returned no less than 11% in any year, and sometimes as high as 18%. Last year, Fairfield Sentry returned 11.55% and so far in 2001, the fund is up 3.52%.

Those returns have been so consistent that some on the Street have begun speculating that Madoff's market-making operation subsidizes and smooths his hedge-fund returns.

How might Madoff Securities do this? Access to such a huge capital base could allow Madoff to make much larger bets -- with very little risk -- than it could otherwise. It would work like this: Madoff Securities stands in the middle of a tremendous river of orders, which means that its traders have advance knowledge, if only by a few seconds, of what big customers are buying and selling. By hopping on the bandwagon, the market maker could effectively lock in profits. In such a case, throwing a little cash back to the hedge funds would be no big deal.

When Barron's ran that scenario by Madoff, he dismissed it as "ridiculous."

Still, some on Wall Street remain skeptical about how Madoff achieves such stunning double-digit returns using options alone. The recent MAR Hedge report, for example, cited more than a dozen hedge fund professionals, including current and former Madoff traders, who questioned why no one had been able to duplicate Madoff's returns using this strategy. Likewise, three option strategists at major investment banks told Barron's they couldn't understand how Madoff churns out such numbers. Adds a former Madoff investor: "Anybody who's a seasoned hedge-fund investor knows the split-strike conversion is not the whole story. To take it at face value is a bit naïve."

Madoff dismisses such skepticism. "Whoever tried to reverse-engineer \, he didn't do a good job. If he did, these numbers would not be unusual." Curiously, he charges no fees for his money-management services. Nor does he take a cut of the 1.5% fees marketers like Fairfield

Greenwich charge investors each year. Why not? "We're perfectly happy to just earn commissions on the trades," he says.

Perhaps so. But consider the sheer scope of the money Madoff would appear to be leaving on the table. A typical hedge fund charges 1% of assets annually, plus 20% of profits. On a $6 billion fund generating 15% annual returns, that adds up to $240 million a year.

The lessons of Long-Term Capital Management's collapse are that investors need, or should want, transparency in their money manager's investment strategy. But Madoff's investors rave about his performance -- even though they don't understand how he does it. "Even knowledgeable people can't really tell you what he's doing," one very satisfied investor told Barron's. "People who have all the trade confirmations and statements still can't define it very well. The only thing I know is that he's often in cash" when volatility levels get extreme. This investor declined to be quoted by name. Why? Because Madoff politely requests that his investors not reveal that he runs their money.

"What Madoff told us was, 'If you invest with me, you must never tell anyone that you're invested with me. It's no one's business what goes on here,'" says an investment manager who took over a pool of assets that included an investment in a Madoff fund. "When he couldn't explain \ how they were up or down in a particular month," he added, "I pulled the money out."

For investors who aren't put off by such secrecy, it should be noted that Fairfield and Kingate Management both market funds managed by Madoff, as does Tremont Advisers, a publicly traded hedge-fund advisory firm.

URL for this article:
http://online.barrons.com/article/SB989019667829349012.html

END ATTACHMENT # 2 BARRON'S ARTICLE

Final 7 NOV 2005 Submission
to NY SEC Branch Chief

INBOX: harrymm

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INBOX: Email 6 of 18

From: "Cheung, Meaghan S." [redacted] **[Add to Address Book] [V**
To: "Harry Markopolos" [redacted]
Subject: RE: Resubmitted Madoff SEC Meeting.doc
Date: Mon, 7 Nov 2005 18:49:02 +0000

Thanks.

From: Harry Markopolos [redacted]
Sent: Monday, November 07, 2005 1:15 PM
To: Cheung, Meaghan S.
Cc: [redacted]
Subject: Resubmitted Madoff SEC Meeting.doc

Meaghan,

1. I spent some time over the weekend further improving my analysis on why I
Investment Securities, LLC is likely a Ponzi Scheme (although there is a slight
the returns are real but accrue from front-running customer order flow).

2. I added an Attachment 4, pages 6 and 7, from an offering memorandum by
Sentry that was faxed to my office on March 21, 2001.

3. The entire report ties in to Fairfield Sentry Ltd., a third party hedge fund, fun
that has over $5 billion invested in Madoff Investment Securities, LLC. Hopefu
my entries foot to the 4 attachments a lot better than the version I sent you on I

4. I am out of the office all day on Tuesday, November 8th, but available the re
week to teleconference if you would like me to answer any questions.

5. I also added some clarifying language in the event this case involves front-r
under the SEC's Section 21A(e) of the 1934 Act bounty program for whistleblo
attorney and I spent significant time on another case where we negotiated with
Bresnans, now a deputy in the SEC's enforcement branch in Washington, rega
qualifying insider-trading cases under the Section 21A(e) bounty program. Bas
reward applies only to insider-trading theory cases.

Thank you,

Harry

[redacted]

INBOX: Email 6 of 18

(comcast

Harry Markopolos

From: "Harry Markopolos"[redacted]
To: "Meaghan Cheung"[redacted]
Cc: [redacted]
Sent: Monday, November 07, 2005 1:14 PM
Attach: Resubmitted Madoff SEC Meeting.doc
Subject: Resubmitted Madoff SEC Meeting.doc

Meaghan,

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2. I added an Attachment 4, pages 6 and 7, from an offering memorandum by Fairfield Sentry that was faxed to my office on March 21, 2001.

3. The entire report ties in to Fairfield Sentry Ltd., a third party hedge fund, fund of funds, that has over $5 billion invested in Madoff Investment Securities, LLC. Hopefully all of my entries foot to the 4 attachments a lot better than the version I sent you on Friday.

4. I am out of the office all day on Tuesday, November 8th, but available the rest of the week to teleconference if you would like me to answer any questions.

5. I also added some clarifying language in the event this case involves front-running under the SEC's Section 21A(e) of the 1934 Act bounty program for whistleblowers. My attorney and I spent significant time on another case where we negotiated with Peter Bresnans, now a deputy in the SEC's enforcement branch in Washington, regarding qualifying insider-trading cases under the Section 21A(e) bounty program. Basically the reward applies only to insider-trading theory cases.

Thank you,

Harry

CC: Attorney [redacted]

The World's Largest Hedge Fund is a Fraud

November 7, 2005 Submission to the SEC
Madoff Investment Securities, LLC
www.madoff.com

Opening Remarks:

I am the original source for the information presented herein having first presented my rationale, both verbally and in writing, to the SEC's Boston office in May, 1999 before any public information doubting Madoff Investment Securities, LLC appeared in the press. There was no whistleblower or insider involved in compiling this report. I used the Mosaic Theory to assemble my set of observations. My observations were collected first-hand by listening to fund of fund investors talk about their investments in a hedge fund run by Madoff Investment Securities, LLC, a SEC registered firm. I have also spoken to the heads of various Wall Street equity derivative trading desks and every single one of the senior managers I spoke with told me that Bernie Madoff was a fraud. Of course, no one wants to take undue career risk by sticking their head up and saying the emperor isn't wearing any clothes but....

I am a derivatives expert and have traded or assisted in the trading of several billion $US in options strategies for hedge funds and institutional clients. I have experience managing split-strike conversion products both using index options and using individual stock options, both with and without index puts. Very few people in the world have the mathematical background needed to manage these types of products but I am one of them. I have outlined a detailed set of Red Flags that make me very suspicious that Bernie Madoff's returns aren't real and, if they are real, then they would almost certainly have to be generated by front-running customer order flow from the broker-dealer arm of Madoff Investment Securities. LLC.

Due to the sensitive nature of the case I detail below, its dissemination within the SEC must be limited to those with a need to know. The firm involved is located in the New York Region.

As a result of this case, several careers on Wall Street and in Europe will be ruined. Therefore, I have not signed nor put my name on this report. I request that my name not be released to anyone other than the Branch Chief and Team Leader in the New York Region who are assigned to the case, without my express written permission. The fewer people who know who wrote this report the better. I am worried about the personal safety of myself and my family. Under no circumstances is this report or its contents to be shared with any other regulatory body without my express permission. This report has been written solely for the SEC's internal use.

As far as I know, none of the hedge fund, fund of funds (FOF's) mentioned in my report are engaged in a conspiracy to commit fraud. I believe they are naïve men and women with a notable lack of derivatives expertise and possessing little or no quantitative finance ability.

There are 2 possible scenarios that involve fraud by Madoff Securities:

1. Scenario # 1 **(Unlikely):** I am submitting this case under Section 21A(e) of the 1934 Act in the event that the broker-dealer and ECN depicted is actually providing the stated

returns to investors but is earning those returns by front-running customer order flow. Front-running qualifies as insider-trading since it relies upon material, non-public information that is acted upon for the benefit of one party to the detriment of another party. Section 21A(e) of the 1934 Act allows the SEC to pay up to 10% of the total fines levied for insider-trading. We have obtained approval from the SEC's Office of General Counsel, the Chairman's Office, and the bounty program administrator that the SEC is able and willing to pay Section 21A(e) rewards. This case should qualify if insider-trading is involved.

2. Scenario # 2 **(Highly likely)** Madoff Securities is the world's largest Ponzi Scheme. In this case there is no SEC reward payment due the whistle-blower so basically I'm turning this case in because it's the right thing to do. Far better that the SEC is proactive in shutting down a Ponzi Scheme of this size rather than reactive.

Who: The politically powerful Madoff family owns and operates a New York City based broker-dealer, ECN, and what is effectively the world's largest hedge fund. Bernard "Bernie" Madoff, the family patriarch started the firm.

According to the www.madoff.com website, "*Bernard L. Madoff was one of the five broker-dealers most closely involved in developing the NASDAQ Stock Market. He has been chairman of the board of directors of the NASDAQ Stock Market as well as a member of the board of governors of the NASD and a member of numerous NASD committees. Bernard Madoff was also a founding member of the International Securities Clearing Corporation in London.*

His brother, Peter B. Madoff *has served as vice chairman of the NASD, a member of its board of governors, and chairman of its New York region. He also has been actively involved in the NASDAQ Stock Market as a member of its board of governors and its executive committee and as chairman of its trading committee. He also has been a member of the board of directors of the Security Traders Association of New York. He is a member of the board of directors of the Depository Trust Corporation.*

What:

1. The family runs what is effectively the world's largest hedge fund with estimated assets under management of at least $20 billion to perhaps $50 billion, but no one knows exactly how much money BM is managing. That we have what is effectively the world's largest hedge fund operating underground is plainly put shocking. But then again, we don't even know the size of the hedge fund industry so none of this should be surprising. A super-sized fraud of this magnitude was bound to happen given the lack of regulation of these off-shore entities. My best guess is that approximately $30 billion is involved.
2. However the hedge fund isn't organized as a hedge fund by Bernard Madoff (BM) yet it acts and trades exactly like one. BM allows third party Fund of Funds (FOF's) to private label hedge funds that provide his firm, Madoff Securities, with equity tranch funding. In return for equity tranch funding, BM runs a trading strategy, **as agent**, whose returns flow to the third party FOF hedge funds and their investors who put up equity capital to

fund BM's broker-dealer and ECN operations. *BM tells investors it earns its fees by charging commissions on all of the trades done in their accounts.*

Red Flag # 1: *Why would a US broker-dealer organize and fund itself in such an unusual manner? Doesn't this seem to be an unseemly way of operating under the regulator's radar screens? Why aren't the commissions charged fully disclosed to investors? Can a SEC Registered Investment Advisor charge **both** commissions and charge a principle fee for trades? **MOST IMPORTANTLY**, why would BM settle for charging only undisclosed commissions when he could earn standard hedge fund fees of 1% management fee + 20% of the profits? Doing some simple math on BM's 12% average annual return stream to investors, the hedge fund, before fees, would have to be earning average annual returns of 16%. Subtract out the 1% management fee and investors are down to 15%. 20% of the profits would amount to 3% (.20 x 15% = 3% profit participation) so investors would be left with the stated 12% annual returns listed in Attachment 1 (Fairfield Sentry Ltd. Performance Data). Total fees to the third party FOF's would amount to 4% annually. Now why would BM leave 4% in average annual fee revenue on the table unless he were a Ponzi Scheme? Or, is he charging a whole lot more than 4% in undisclosed commissions?*

3. The third parties organize the hedge funds and obtain investors but 100% of the money raised is actually managed by Madoff Investment Securities, LLC in a purported hedge fund strategy. The investors that pony up the money don't know that BM is managing their money. That Madoff is managing the money is purposely kept secret from the investors. Some prominent US based hedge fund, fund of funds, that "invest" in BM in this manner include:
   A. Fairfield Sentry Limited (Arden Asset Management) which had $5.2 billion invested in BM as of May 2005; 11th Floor, 919 Third Avenue; New York, NY 10022; Telephone 212.319.606; The Fairfield Greenwich Group is a global family of companies with offices in New York, London and Bermuda, and representative offices in the U.S., Europe and Latin America. Local operating entities are authorized or regulated by a variety of government agencies, including Fairfield Greenwich Advisors LLC, a U.S. SEC registered investment adviser, Fairfield Heathcliff Capital LLC, a U.S. NASD member broker-dealer, and Fairfield Greenwich (UK) Limited, authorized and regulated by the Financial Services Authority in the United Kingdom.
   B. Access International Advisors; www.aiagroup.com; a SEC registered investment advisor, telephone # 212.223.7167; Suite 2206; 509 Madison Avenue, New York, NY 10022 which had over $450 million invested with BM as of mid-2002. The majority of this FOF's investors are European, even though the firm is US registered.
   C. Broyhill All-Weather Fund, L.P. had $350 million invested with BM as of March 2000.
   D. Tremont Capital Management, Inc. Corporate Headquarters is located at 555 Theodore Fremd Avenue; Rye, New York 10580; T: (914) 925-1140 F: (914) 921-3499. Tremont oversees on an advisory and fully discretionary basis over $10.5 billion in assets. Clients include institutional investors, public and private pension plans, ERISA plans, university endowments, foundations, and financial institutions, as well as high net worth individuals. Tremont is owned by Oppenhiemer Funds Inc. which is owned by Mass Mutual Insurance Company so they should have sufficient reserves to make investors whole. Mass Mutual is currently under investigation by the Massachusetts Attorney General, the Department of Justice, and the SEC.

E. During a 2002 marketing trip to Europe every hedge fund FOF I met with in Paris and Geneva had investments with BM. They all said he was their best manager! A partial list of money managers and Private Banks that invest in BM is included at the end of this report in Attachment 3.

4. Here's what smells bad about the idea of providing equity tranch funding to a US registered broker-dealer:
   A. The investment returns passed along to the third party hedge funds are equivalent to BM borrowing money. These 12 month returns from 1990 – May 2005 ranged from a low of 6.23% to a high of 19.98%, with an average 12 month return during that time period of 12.00%. Add in the 4% in average annual management & participation fees and BM would have to be delivering average annual returns of 16% in order for the investors to receive 12%. No Broker-Dealer that I've ever heard of finances its operations at that high of an implied borrowing rate (source: Attachment 1; Fairfield Sentry Limited return data from December 1990 – May 2005). Ask around and I'm sure you'll find that BM is the only firm on Wall Street that pays an average of 16% to fund its operations.
   B. BD's typically fund in the short-term credit markets and benchmark a significant part of their overnight funding to LIBOR plus or minus some spread. LIBOR + 40 basis points would seem a more realistic borrowing rate for a broker-dealer of BM's size.
   C. **Red Flag # 2**: *why would a BD choose to fund at such a high implied interest rate when cheaper money is available in the short-term credit markets? One reason that comes to mind is that BM couldn't stand the due diligence scrutiny of the short-term credit markets. If Charles Ponzi had issued bank notes promising 50% interest on 3 month time deposits instead of issuing unregulated Ponzi Notes to his investors, the State Banking Commission would have quickly shut him down. The key to a successful Ponzi Scheme is to promise lucrative returns but to do so in an unregulated area of the capital markets. Hedge funds are not due to fall under the SEC's umbrella until February 2006.*

5. The third party hedge funds and fund of funds that market this hedge fund strategy that invests in BM don't name and aren't allowed to name Bernie Madoff as the actual manager in their performance summaries or marketing literature. Look closely at Attachment 1, Fairfield Sentry Ltd.'s performance summary and you won't see BM's name anywhere on the document, yet BM is the actual hedge fund manager with discretionary trading authority over all funds, as agent.
   Red Flag # 3: ***Why the need for such secrecy?*** *If I was the world's largest hedge fund and had great returns, I'd want all the publicity I could garner and would want to appear as the world's largest hedge fund in all of the industry rankings. Name one mutual fund company, Venture Capital firm, or LBO firm which doesn't brag about the size of their largest funds' assets under management. Then ask yourself, why would the world's largest hedge fund manager be so secretive that he didn't even want his investors to know he was managing their money? Or is it that BM doesn't want the SEC and FSA to know that he exists?*
6. The third party FOF's never tell investors who is actually managing their money and describe the investment strategy as: This hedge fund's objective is long term growth on

a consistent basis with low volatility. The investment advisor invests exclusively in the U.S. and utilizes a strategy often referred to as a "split-strike conversion." Generally this style involves purchasing a basket of 30 – 35 large-capitalization stocks with a high degree of correlation to the general market (e.g. American Express, Boeing, Citigroup, Coca-Cola, Dupont, Exxon, General Motors, IBM, Merck, McDonalds). To provide the desired hedge, the manager then sells out-of-the-money OEX index call options and buys out-of-the-money OEX index put options. The amount of calls that are sold and puts that are bought represent a dollar amount equal to the basket of shares purchases.

7. I personally have run split-strike conversion strategies and know that BM's approach is far riskier than stated in 6 above. His strategy is wholly inferior to an all index approach and is wholly incapable of generating returns in the range of 6.23% to 19.98%. <u>BM's strategy should not be able beat the return on US Treasury Bills</u> Due to the glaring weakness of the strategy:
    A. <u>Income Part of the strategy</u> is to buy 30 – 35 large-cap stocks, sell out-of-the-money index call options against the value of the stock basket. There are three possible sources of income in this strategy.
        1) We earn income from the stock's dividends. Let's attribute a 2% average return to this source of funds for the 14 ½ year time period. This explains 2% of the 16% average gross annual returns before fees and leaves 14% of the returns unexplained.
        2) We earn income from the sale of OTC OEX index call options. Let's also assume that we can generate an additional 2% annual return via the sale of OTC out-of-the-money OEX index call options which leaves 12% of the 16% gross returns unexplained. On Friday, October 14, 2005 the OEX (S&P 100) index closed at 550.49 and there were only 163,809 OEX index call option contracts outstanding (termed the "open interest"). 163,809 call option calls outstanding x $100 contact multiplier x 550.49 index closing price = $9,017, 521,641 in stock equivalents hedged.
        3) We can earn income from capital gains by selling the stocks that go up in price. This portion of the return stream would have to earn the lion's share of the hedge fund strategy's returns. We have 12% of the return stream unexplained so far. However, the OTC OEX index puts that we buy will cost AT LEAST <8%> per year (a lot more in most years but I'm giving BM the benefit of every doubt here). Therefore, BM's stock selection would have to be earning an average of 20% per year. That would mean that he's been the world's best stock-picker since 1990 beating out such luminaries as Warren Buffet and Bill Miller. Yet no one's ever heard of BM as being a stock-picker, much less the world's best stock-picker. Why isn't he famous if he was able to earn 20% average annual returns?

        Red Flag # 4: *$9.017 billion in total OEX listed call options outstanding is not nearly enough to generate income on BM's total amount of assets under management which I estimate to range between $20 - $50 billion. Fairfield Sentry Ltd. alone has $5.1 billion with BM. And, while BM may say he only uses Over-the-Counter(OTC) index options, there is no way that this is* *possible. The OTC market should never be several times larger than the exchange listed market for this type of plain vanilla derivative.*

B. Protection Part of the strategy is to buy out-of-the-money OEX index put options. This costs you money each and every month. This hurts your returns and is the main reason why BM's strategy would have trouble earning 0% average annual returns much less the 12% net returns stated in Fairfield Sentry Ltd.'s performance summary. Even if BM earns a 4% return from the combination of 2% stock dividends and 2% from the sale of call options, the cost of the puts would put this strategy in the red year in and year out. No way he can possibly be delivering 12% net to investors. The math just doesn't support this strategy if he's really buying index put options.

Red Flag # 5: *BM would need to be purchasing at-the-money put options because he has only 7 small monthly losses in the past 14 ½ years. His largest monthly loss is only <0.55%>, so his puts would have to be at-the-money. At-the-money put options are very, very expensive. A one-year at-the-money put option would cost you <8%> or more, depending upon the market's volatility. And <8%> would be a cheap price to pay in many of the past 14 ½ years for put protection!! Assuming BM only paid< 8%> per year in put protection, and assuming he can earn +2% from stock dividends plus another +2% from call option sales, he's still under-water <4%> performance wise. <8%> put cost + 2% stock dividends + 2% income from call sales = <4%>. And, I've proven that BM would need to be earning at least 16% annually to deliver 12% after fees to investors. That means the rest of his returns would have to be coming from stock selection where he picked and sold winning stocks to include in his 35-stock basket of large-cap names. Lots of luck doing that during the past stock market crises like 1997's Asian Currency Crises, the 1998 Russian Debt / LTCM crises, and the 2000-2002 killer bear market. And index put option protection was a lot more expensive during these crises periods than 8%. Mathematically none of BM's returns listed in Attachment 1 make much sense. They are just too unbelievably good to be true.*

C. The OEX index (S&P 100) closed at 550.49 on Friday, October 14, 2005 meaning that each put option hedged $55,049 dollars worth of stock ($100 contract multiplier x 550.49 OEX closing index price = $55,049 in stock hedged). As of that same date, the total open interest for OEX index put options was 307,176 contracts meaning that a total of $16,909,731,624 in stock was being hedged by the use of OEX index puts (307,176 total put contracts in existence as of Oct 14th x $55,049 hedge value of 1 OEX index put = $16,909,731,624 in stock hedged). Note: I excluded a few thousand OEX LEAP index put options from my calculations because these are long-term options and not relevant for a split-strike conversion strategy such as BM's.

Red Flag # 6: *At my best guess level of BM's assets under management of $30 billion, or even at my low end estimate of $20 billion in assets under management, BM would have to be over 100% of the total OEX put option contract open interest in order to hedge his stock holdings as depicted in the third party hedge funds marketing literature. In other words, there are not enough index option put contracts in existence to hedge the way BM says he is hedging! And there is no* *way the OTC market is bigger than the exchange listed market for plain vanilla S&P 100 index put options.*

D. Mathematically I have proven that BM cannot be hedging using listed index put and call options. One hedge fund FOF has told me that BM uses only Over-the-Counter options and trades exclusively thru UBS and Merrill Lynch. I have not called those two firms to check on this because it seems implausible that a BD would trade $20 - $50 billion worth of index put options per month over-the-counter thru only 2 firms. That plus the fact that if BM was really buying OTC index put options, then there is no way his average annual returns could be positive!! At a minimum, using the cheapest way to buy puts would cost a fund <8%> per year. To get the put cost down to <8%>, BM would have to buy a one-year at-the-money put option and hold it for one-year. No way his call sales could ever hope to come even fractionally close to covering the cost of the puts.

Red Flag # 7: *The counter-party credit exposures for UBS and Merrill would be too large for these firms credit departments to approve. The SEC should ask BM for trade tickets showing he has traded OTC options thru these two firms. Then the SEC should visit the firms' OTC derivatives desks, talk the to heads of trading and ask to see BM's trade tickets. Then ask the director of operations to verify the tickets and ask to see the inventory of all of the stock and listed options hedging the OTC puts and calls. If these firms can't show you the off-setting hedged positions then they are assisting BM as part of a conspiracy to commit fraud. If any other brokerage firms equity derivatives desk is engaged in a conspiracy to cover for BM, then this scandal will be a doozy when it hits the financial press but at least investors would have firms with deep pockets to sue.*

Red Flag # 8: *OTC options are more expensive to trade than listed options. You have to pay extra for the customization features and secrecy offered by OTC options. Trading in the size of $20 - $50 billion per month would be impossible and the bid-ask spreads would be so wide as to preclude earning any profit whatsoever. These Broker/Dealers would need to offset their short OTC index put option exposure to a falling stock market by hedging out their short put option risk by either buying listed put options or selling short index futures and the derivatives markets are not deep and liquid enough to accomplish this without paying a penalty in prohibitively expensive transaction costs.*

Red Flag # 9: *Extensive and voluminous paperwork would be required to keep track of and clear each OTC trade. Plus, why aren't Goldman, Sachs and Citigroup involved in handling BM's order flow? Both Goldman and Citigroup are a lot larger in the OTC derivatives markets than UBS or Merrill Lynch.*

E. My experience with split-strike conversion trades is that the best a good manager is likely to obtain using the strategy marketed by the third-party FOF's is T-bills less management fees. And, if the stock market is down by more than 2%, the return from this strategy will range from a high of zero return to a low of a few percent depending upon your put's cost and how far out-of-the-money it is.

F. In 2000 I ran a regression of BM's hedge fund returns using the performance data from Fairfield Sentry Limited. BM had a .06 correlation to the equity market's return which confirms the .06 Beta that Fairfield Sentry Limited lists in its return numbers.

Red Flag # 10: *It is mathematically impossible for a strategy using index call options and index put options to have such a low correlation to the market where its returns are supposedly being generated from. This makes no sense! The strategy depicted retains 100% of the single-stock downside risk since they own only index put options and not single stock put options. Therefore if one or more stocks in their portfolio were to tank on bad news, BM's index put would offer little protection and their portfolio should feel the pain. However, BM's performance numbers show only 7 extremely small losses during 14 ½ years and these numbers are too good to be true. The largest one month loss was only -55 basis points (-0.55%) or just over one-half of one percent! And BM never had more than a one month losing streak! Either BM is the world's best stock and options manager that the SEC and the investing public has never heard of or he's a fraud. You would have to figure that at some point BM owned a WorldCom, Enron, GM or HealthSouth in their portfolio when bad or really bad news came out and caused these stocks to drop like a rock.*

8. **Red Flag # 11** *Two press articles, which came to print well after my initial May 1999 presentation to the SEC, do doubt Bernie Madoff's returns and they are:*
   A. The May 7, 2001 edition of Barron's, in an article entitled, ***"Don't Ask, Don't Tell; Bernie Madoff is so secretetive, he even asks his investors to keep mum,"*** written by Erin Arvedlund, published an expose about Bernie Madoff a few years ago with no resulting investigation by any regulators. Ms. Arvedlund has since left Barron's. I have attached a copy of the Barrons' article which lists numerous red flags.
   B. Michael Ocrant, formerly a reporter for MAR Hedge visited Bernie Madoff's offices and wrote a very negative article that doubted the source of BM's returns. He reported to a colleague that he saw some very unusual things while at Madoff's offices. The SEC should contact him. Michael Ocrant is currently serving as the Director of Alternative Investments; Institutional Investor; New York, NY 10001; Telephone # 212-224-3821 or 212-213-6202; Email: mocrant@iiconferences.com

9. Fund of funds with whom I have spoken to that have BM in their stable of funds continually brag about their returns and how they are generated thanks to BM's access to his broker-dealer's access to order flow. They believe that BM has perfect knowledge of the market's direction due to his access to customer order flow into his broker-dealer. **Red Flag # 12:** *Yes, BM has access to his customer's order flow thru his broker-dealer but he is only one broker out of many, so it is impossible for him to know the market's direction to such a degree as to only post monthly losses once every couple of years. All of Wall Street's big wire houses experience trading losses on a more regular frequency that BM. Ask yourself how BM's trading experience could be so much better than all of the other firms on Wall Street. Either he's the best trading firm on the street and rarely ever has large losing months unlike other firms or he's a fraud.*
10. **Red Flag # 13:** *I believe that BM's returns can be real ONLY if they are generated from front-running his customer's order flow. In other words, yes, if he's buying at a penny above his customer's buy orders, he can only lose one penny if the stock drops but can*

make several pennies if the stock goes up. For example, if a customer has an order to buy 100,000 shares of IBM at $100, BM can put in his own order to buy 100,000 share of IBM at $100.01. This is what's known as a right-tail distribution and is very similar to the payoff distribution of a call option. Doing this could easily generate returns of 30% - 60% or more per anum. He could be doing the same thing by front-running customer sell orders. However, if BM's returns are real but he's generating them from front-running there are two problems with this:

A. *Problem # 1: front-running is one form of insider-trading and is illegal*
B. *Problem # 2: generating real returns from front-running but telling hedge fund investors that you are generating the returns via a complex (but unworkable) stock and options strategy is securities fraud.*

Some time ago, during different market conditions, I ran a study using the Black-Scholes Option Pricing Model to analyze the value of front-running with the goal of putting a monetary value on front-running where the insider knew the customer's order and traded ahead of it. When I ran the study the model inputs were valued at: OEX component stocks annualized volatility on a cap-weighted basis was 50% (during a bear market period), the T-bill rate was 5.80%, and the average stock price was $46. I then calculated the value of an at-the-money call options over time intervals of 1 minute, 5 minutes, 10 minutes, and 15 minutes. I used a 253 trading day year. The SEC should be able to duplicate these results:

1 minute option = 3 cents worth of trade information value
5 minute option = 7 cents worth of trade information value
10 minute option = 10 cents worth of trade information value
15 minute option = 12 cents worth of trade information value

Conclusion: Bernie Madoff used to advertise in industry trade publications that he would pay 1 cent per share for other broker's order flow. If he was paying 1 cent per share for order flow and front-running these broker's customers, then he could easily be earning returns in the 30% - 60% or higher annually. In all time intervals ranging from 1 minute to 15 minutes, having access to order flow is the monetary equivalent of owning a valuable call option on that order. The value of these implicit call options ranges between 3 – 12 times the one penny per share paid for access to order flow. If this is what he's doing, then the returns are real but the stated investment strategy is illegal and based solely on insider-trading.

NOTE: I am pretty confident that BM is a Ponzi Scheme, but in the off chance he is front-running customer orders and his returns are real, then this case qualifies as insider-trading under the SEC's bounty program as outlined in Section 21A(e) of the 1934 Act. However, if BM was front-running, a highly profitable activity, then he wouldn't need to borrow funds from investors at 16% implied interest. Therefore it is far more likely that BM is a Ponzi Scheme. Front-running is a very simple fraud to commit and requires only access to inside information. The elaborateness of BM's fund-raising, his need for secrecy, his high 16% average cost of funds, and reliance on a derivatives investment scheme that few investors (or regulators) would be capable of comprehending lead to a weight of the evidence conclusion that this is a Ponzi Scheme.

11. **Red Flag # 14:** *Madoff subsidizes down months! Hard to believe (and I don't believe this) but I've heard two FOF's tell me that they don't believe Madoff can make money in big down months either. They tell me that Madoff "subsidizes" their investors in down months, so that they will be able to show a low volatility of returns. These types of stories are commonly found around Ponzi Schemes. These investors tell me that Madoff only books winning tickets in their accounts and "eats the losses" during months when the market sells off hard. The problem with this is that it's securities fraud to misstate either returns or the volatility of those returns. These FOF professionals who heard BM tell them that he subsidizes losses were professionally negligent in not turning BM into the SEC, FSA and other regulators for securities fraud.*

    Red Flag # 15: *Why would a fund of funds investor believe any broker-dealer that commits fraud in a few important areas – such as misstating returns and misstating volatility of returns – yet believe him in other areas? I'd really like to believe in the tooth fairy, but I don't after catching my mother putting a quarter underneath my pillow one night.*
12. **Red Flag # 16:** *Madoff has perfect market-timing ability. One investor told me, with a straight face, that Madoff went to 100% cash in July 1998 and December 1999, ahead of market declines. He said he knows this because Madoff faxes his trade tickets to his firm and the custodial bank. However, since Madoff owns a broker-dealer, he can generate whatever trade tickets he wants. And, I'll bet very few FOF's ask BM to fax them trade tickets. And if these trade tickets are faxed, have the FOF's then matched them to the time and sales of the exchanges? For example, if BM says he bot 1 million shares of GM, sold $1 million worth of OTC OEX calls and bot $1 million worth of OTC OEX puts, we should see prints somewhere. The GM share prints would show on either the NYSE or some other exchange while the broker-dealers he traded OTC options thru would show prints of the hedges they traded to be able to provide BM with the OTC options at the prices listed on BM's trade tickets.*
13. **Red Flag # 17:** *Madoff does not allow outside performance audits. One London based hedge fund, fund of funds, representing Arab money, asked to send in a team of Big 4 accountants to conduct a performance audit during their planned due diligence. They were told "No, only Madoff's brother-in-law who owns his own accounting firm is allowed to audit performance for reasons of secrecy in order to keep Madoff's proprietary trading strategy secret so that nobody can copy it. Amazingly, this fund of funds then agreed to invest $200 million of their client's money anyway, because the low volatility of returns was so attractive!! Let's see, how many hedge funds have faked an audited performance history?? Wood River is the latest that comes to mind as does the Manhattan Fund but the number of bogus hedge funds that have relied upon fake audits has got to number in the dozens.*
14. **Red Flag # 18:** *Madoff's returns are not consistent with the one publicly traded option income fund with a history as long as Madoff's. In 2000, I analyzed the returns of Madoff and measured them against the returns of the Gateway Option Income Fund (Ticker GATEX). During the 87 month span analyzed, Madoff was down only 3 months versus GATEX being down 26 months. GATEX earned an annualized return of 10.27% during the period studied vs. 15.62% for Bernie Madoff and 19.58% for the S&P 500. GATEX has a more flexible investment strategy than BM, so GATEX's returns should be*

superior to BM's but instead they are inferior. This makes no sense. How could BM be better using an inferior strategy?

15. **Red Flag # 19**: *There have been several option income funds that went IPO since August 2004. None of them have the high returns that Bernie Madoff has. How can this be? They use similar strategies only they should be making more than BM in up months because most of these option income funds don't buy expensive index put options to protect their portfolios. Thus the publicly traded option income funds should make more money in up markets and lose more than Madoff in down markets. Hmm....that Madoff's returns are so high yet he buys expensive put options is just another reason to believe he is running the world's largest Ponzi Scheme. A good study for the SEC would be to compare 2005 performance of the new option income funds to Bernie Madoff while accounting for the cost of Bernie's index put option protection. There's no way Bernie can have positive returns in 2005 given what the market's done and where volatility is.*
16. **Red Flag # 20**: *Madoff is suspected of being a fraud by some of the world's largest and most sophisticated financial services firms. Without naming names, here's an abbreviated tally:*

    A. A managing director at Goldman, Sachs prime brokerage operation told me that his firm doubts Bernie Madoff is legitimate so they don't deal with him.

    B. From an Email I received this past June 2005 I now suspect that the end is near for BM. All Ponzi Schemes eventually topple of their own weight once they become too large and it now appears that BM is having trouble meeting redemptions and is attempting to borrow sizeable funds in Europe.

ABCDEFGH and I had dinner with a savvy European investor that studies the HFOF market. He stated that both RBC and Socgen have removed Madoff some time ago from approved lists of individual managers used by investors to build their own tailored HFOFs.

More importantly, Madoff was turned down, according to this source, for a borrowing line from a Euro bank, I believe he said Paribas. Now why would Madoff need to borrow more funds? This Euro Investor said that Madoff was in fact running "way over" our suggested $12-14 billion (Fairfield Sentry is running $5.3 BB by themselves!) . Madoff's 12 month returns is about 7% net of the feeder fund's fees. Looks like he is stepping down the pay out.

    C. An official from a Top 5 money center bank's FOF told me that his firm wouldn't touch Bernie Madoff with a ten foot pole and that there's no way he's for real.

17. **Red Flag # 21:** *ECN's didn't exist prior to 1998. Madoff makes verbal claims to his third party hedge FOF's that he has private access to ECN's internal order flow, which Madoff pays for, and that this is a substantial part of the return generating process. If this is true, then where did the returns come from in the years 1991 – 1997, prior to the ascendance of the ECN's? Presumably, prior to 1998, Madoff only had access to order flow on the NASDAQ for which he paid 1 cent per share for. He would have no such advantage pre-1998 on the large-cap, NYSE listed stocks the marketing literature says he buys (Exxon, McDonalds, American Express, IBM, Merck, etc...).*
18. **Red Flag # 22:** *The Fairfield Sentry Limited Performance Chart (Attachment 1) depicted for Bernie Madoff's investment strategy are misleading. The S&P 500 return line is accurate because it is moving up and down, reflecting positive and negative returns. Fairfield Sentry's performance chart is misleading, it is almost a straight line rising at a 45 degree angle. This chart cannot be cumulative in the common usage of the term for reporting purposes, which means "geometric returns." The chart must be some sort of arithmetic average sum, since a true*

cumulative return line, given the listed monthly returns would be exponentially rising (i.e. curving upward at an increasing rate). My rule of thumb is that if the manager misstates his performance, you can't trust him. Yet somehow Madoff is now running the world's largest, most clandestine hedge fund so clearly investors aren't doing their due diligence. And why does he provide the S&P 500 as his benchmark when he is actually managing using a S&P 100 strategy? Shouldn't the performance line presented be the S&P 100's (OEX) performance?

19. **Red Flag # 23:** *Why is Bernie Madoff borrowing money at an average rate of 16.00% per anum and allowing these third party hedge fund, fund of funds to pocket their 1% and 20% fees bases upon Bernie Madoff's hard work and brains? Does this make any sense at all? Typically FOF's charge only 1% and 10%, yet BM allows them the extra 10%. Why? And why do these third parties fail to mention Bernie Madoff in their marketing literature? After all he's the manager, don't investors have a right to know who's managing their money?*

20. **Red Flag # 24:** *Only Madoff family members are privy to the investment strategy. Name one other prominent multi-billion dollar hedge fund that doesn't have outside, non-family professionals involved in the investment process. You can't because there aren't any. Michael Ocrant, the former MAR Hedge Reporter listed above saw some highly suspicious red flags during his visit to Madoff's offices and should be interviewed by the SEC as soon as possible.*

21. **Red Flag # 25:** *The Madoff family has held important leadership positions with the NASD, NASDAQ, SIA, DTC, and other prominent industry bodies therefore these organizations would not be inclined to doubt or investigate Madoff Investment Securities, LLC. The NASD and NASDAQ do not exactly have a glorious reputation as vigorous regulators untainted by politics or money.*

22. **Red Flag # 26:** *BM goes to 100% cash for every December 31st year-end according to one FOF invested with BM. This allows for "cleaner financial statements" according to this source. Any unusual transfers or activity near a quarter-end or year-end is a red flag for fraud. Recently, the BD REFCO Securities engaged in "fake borrowing" with Liberty, a hedge fund, that made it appear that Liberty owed REFCO over $400 million in receivables. This allowed REFCO to mask its true debt position and made all of their equity ratios look better than they actually were. And of course, Grant Thorton, REFCO's external auditor missed this $400 million entry. As did the two lead underwriters who were also tasked with due-diligence on the IPO - CSFB and Goldman Sachs. BM uses his brother-in-law as his external auditor, so in this case there isn't even the façade of having an independent and vigilant auditor verifying the accounting entries.*

23. **Red Flag # 27:** *Several equity derivatives professionals will all tell you that the split-strike conversion strategy that BM runs is an outright fraud and cannot possibly achieve 12% average annual returns with only 7 down months during a 14 ½ year time period. Some derivatives experts that the SEC should call to hear their opinions of how and why BM is a fraud and for some insights into the mathematical reasons behind their belief, the SEC should call:*

   a. Leon Gross, Managing Director of Citigroup's world-wide equity derivatives research unit; 3rd Floor, 390 Greenwich Street; New York, NY 10013: Tel# 800.492.9833 or 212.723.7873 or leon.j.gross@citigroup.com [Leon can't believe that the SEC hasn't shut down Bernie Madoff yet. He's also amazed that FOF's actually believe this stupid options strategy is capable of earning a positive return much less a 12% net average annual return. He thinks the strategy would have trouble earning 1% net much less 12% net. Leon is a free spirit, so if you ask him he'll tell you but you'd understand it better if you met him at his workplace in a private conference room and tell him he won't need to have Citigroup lawyers present, you're just there for some friendly opinions. He talks derivatives at a high level, so ask simple "yes or no" type questions to start off the interview then drill down.]

b. Walter "Bud"Haslett, CFA; Write Capital Management, LLC; Suite 455; 900 Briggs Road; Mount Laurel, NJ 08065; Tel#: 856.727.1700 or bud.haslett@writecapital.com www.writecapital.com [Bud's firm runs $ hundreds of millions in options related strategies and he knows all of the math.]

c. Joanne Hill, Ph.D.; Vice-President and global head of equity derivatives research, Goldman Sachs (NY), 46th Floor; One New York Plaza, New York, NY 10004; Tel# 212.902.2908 [Again, make sure she doesn't lawyer up or this conversation will be useless to you. Tell her you want her opinion and no one will hold her to it or ever tell she gave the SEC an opinion without legal counsel present.]

24. **Red Flag # 28:** *BM's Sharpe Ratio of 2.55 (Attachment 1: Fairfield Sentry Ltd. Performance Data) is UNBELIEVABLY HIGH compared to the Sharpe Ratios experienced by the rest of the hedge fund industry. The SEC should obtain industry hedge fund rankings and see exactly how outstanding Fairfield Sentry Ltd.'s Sharpe Ratio is. Look at the hedge fund rankings for Fairfield Sentry Ltd. and see how their performance numbers compare to the rest of the industry. Then ask yourself how this is possible and why hasn't the world come to acknowledge BM as the world's best hedge fund manager?*

25. **Red Flag # 29:** *BM tells the third party FOF's that he has so much money under management that he's going to close his strategy to new investments. However, I have met several FOF's who brag about their "special access" to BM's capacity. This would be humorous except that too many European FOF's have told me this same seductive story about their being so close to BM that he'll waive the fact that he's closed his funds to other investors but let them in because they're special. It seems like every single one of these third party FOF's has a "special relationship" with BM.*

Conclusions:

1. I have presented 174 months (14 ½ years) of Fairfield Sentry's return numbers dating back to December 1990. Only 7 months or 4% of the months saw negative returns. Classify this as "definitely too good to be true!" No major league baseball hitter bats .960, no NFL team has ever gone 96 wins and only 4 losses over a 100 game span, and you can bet everything you own that no money manager is up 96% of the months either. It is inconceivable that BM's largest monthly loss could only be -0.55% and that his longest losing streaks could consist of 1 slightly down month every couple of years. Nobody on earth is that good of a money manager unless they're front-running.

2. There are too many red flags to ignore. REFCO, Wood River, the Manhattan Fund, Princeton Economics, and other hedge fund blow ups all had a lot fewer red flags than Madoff and look what happened at those places.

3. Bernie Madoff is running the world's largest unregistered hedge fund. He's organized this business as "hedge fund of funds private labeling their own hedge funds which Bernie Madoff **secretly** runs for them using a split-strike conversion strategy getting paid only trading commissions which are not disclosed." If this isn't a regulatory dodge, I don't know what is. This is back-door marketing and financing scheme that is opaque and rife with hidden fees (he charges only commissions on the trades). If this product isn't marketed correctly, what is the chance that it is managed correctly? In my financial industry experience, I've found that wherever there's one cockroach in plain sight, many more are lurking behind the corner out of plain view.

4. Mathematically this type of split-strike conversion fund should never be able to beat US Treasury Bills much less provide 12.00% average annual returns to investors net of fees. I and other derivatives professionals on Wall Street will swear up and down that a split-strike conversion strategy cannot earn an average annual return anywhere near the 16% gross returns necessary to be able to deliver 12% net returns to investors.

5. BM would have to be trading more than 100% of the open interest of OEX index put options every month. And if BM is using only OTC OEX index options, it is guaranteed that the Wall Street firms on the other side of those trades would have to be laying off a significant portion of that risk in the exchange listed index options markets. Every large derivatives dealer on Wall Street will tell you that Bernie Madoff is a fraud. Go ask the heads of equity derivatives trading at Morgan Stanley, Goldman Sachs, JP Morgan and Citigroup their opinions about Bernie Madoff. They'll all tell the SEC that they can't believe that BM hasn't been caught yet.

6. The SEC is slated to start overseeing hedge funds in February 2006, yet since Bernie Madoff is not registered as a hedge fund but acting as one but via third party shields, the chances of Madoff escaping SEC scrutiny are very high. If I hadn't written this report, there's no way the SEC would have known to check the facts behind all of these third party hedge funds.

Potential Fall Out if Bernie Madoff turns out to be a Ponzi Scheme:

1. If the average hedge fund is assumed to be levered 4:1, it doesn't take a rocket scientist to realize that there might be anywhere from a few hundred billion on up in selling pressure in the wake of a $20 - $50 billion hedge fund fraud. With the hedge fund market estimated to be $1 trillion, having one hedge fund with 2% - 5% of the industry's assets under management suddenly blow up, it is hard to predict the severity of the resulting shock wave. You just know it'll be unpleasant for anywhere from a few days to a few weeks but the fall out shouldn't be anywhere near as great as that from the Long Term Capital Management Crises. Using the hurricane scale with which we've all become quite familiar with this year, I'd rate BM turning out to be a Ponzi Scheme as a Category 2 or 3 hurricane where the 1998 LTCM Crises was a Category 5.

2. Hedge fund, fund of funds with greater than a 10% exposure to Bernie Madoff will likely be faced with forced redemptions. This will lead to a cascade of panic selling in all of the various hedge fund sectors whether equity related or not. Long –short and market neutral managers will take losses as their shorts rise and their longs fall. Convertible arbitrage managers will lose as the long positions in underlying bonds are sold and the short equity call options are bought to close. Fixed income arbitrage managers will also face losses as credit spreads widen. Basically, most hedge funds categories with two exceptions will have at least one big down month thanks to the unwinding caused by forced redemptions. Dedicated Short Funds and Long Volatility Funds are the two hedge fund categories that will do well.

3. The French and Swiss Private Banks are the largest investors in Bernie Madoff. This will have a huge negative impact on the European capital markets as several large fund of funds implode. I figure one-half to three-quarters of Bernie Madoff's funds come from overseas. The unwinding trade will hurt all markets across the globe but it is the Private European Banks that will fare the worst.

4. European regulators will be seen as not being up to the task of dealing with hedge fund fraud. Hopefully this scandal will serve as a long overdue wake-up call for them and result in increased funding and staffing levels for European Financial Regulators.

5. In the US Fairfield Sentry, Broyhill, Access International Advisors, Tremont and several other hedge fund, fund of funds will all implode. There will be a call for increased hedge fund regulation by scared and battered high net worth investors.

6. The Wall Street wire house FOF's are not invested in Madoff's strategy. As far as I know the wire house's internal FOF's all think he's a fraud and have avoided him like the plague. But these very same wire houses often own highly profitable hedge fund prime brokerage operations and these operations will suffer contained, but painful nonetheless, losses from loans to some hedge funds that go bust during the panic selling. As a result, I predict that some investment banks will pull out of the prime brokerage business deeming it too volatile from an earnings standpoint. Damage to Wall Street will be unpleasant in that hedge funds and FOF's are a big source of trading revenues. If the

hedge fund industry fades, Wall Street will need to find another revenue source to replace them.

7. US Mutual fund investors and other long-term investors in main stream investment products will only feel a month or two's worth of pain from the selling cascade in the hedge fund arena but their markets should recover afterwards.

8. Congress will be up in arms and there will be Senate and House hearings just like there were for Long Term Capital Management.

9. The SEC's critics who say the SEC shouldn't be regulating private partnerships will be forever silenced. Hopefully this leads to expanded powers and increased funding for the SEC. Parties that opposed SEC entry into hedge fund regulation will fall silent. The SEC will gain political strength in Washington from this episode but only if the SEC is proactive and launches an immediate, full scale investigation into all of the Red Flags surrounding Madoff Investment Securities, LLC. Otherwise, it is almost certain that NYAG Elliot Spitzer will launch his investigation first and once again beat the SEC to the punch causing the SEC further public embarrassment.

10. Hedge funds will face increased due diligence from regulators, investors, prime brokers and counter-parties which is a good thing and long overdue.

Potential Fall Out if Bernie Madoff is found out to be front-running customer order flow:

1. This would be just one more black eye among many for the brokerage industry and the NYSE and NASDAQ. At this point the reputations of both the NYSE and NASDAQ are already at rock bottom, so there's likely little downside left for these two troubled organizations.

2. The industry wouldn't miss a beat other than for the liquidation of Madoff Investment Securities, LLC. Figure it will be similar to REFCO's demise only there won't be a buyer of the firm given that they cheated customers who would all be embarrassed to remain customers once the news they've been ripped off is on the front-pages. These former customers are more likely to sue for damages than remain customers. Unsecured lenders would face losses but other than that the industry would be better off.

3. At least the returns are real, in which case determining restitution could keep the courts busy for years. The Class Action Bar would be thrilled. A lot of the FOF's are registered offshore in places where the long arm of the law might not reach. My guess is that the fight for the money off-shore would keep dozens of lawyers happily employed for many years.

4. The FOF's would suffer little in the way of damage. All could be counted on to say "*We didn't know the manager was generating returns illegally. We relied upon the NYSE and NASDAQ to regulate their markets and prevent front-running therefore we see no reason to return any funds.*"

Attachments:

1. 2 page Summary of Fairfield Sentry Ltd with performance data from December 1990 – May 2005

2. Copy of the May 7, 2001 Barrons' article, ***"Don't Ask, Don't Tell; Bernie Madoff is so secretetive, he even asks his investors to keep mum,"*** written by Erin E. Arvedlund.

3. Partial list of French and Swiss money-managers and private banks with investments in Bernie Madoff's hedge fund. Undoubtedly there are dozens more European FOF's and Private Banks that are invested with BM.

4. 2 page offering memorandum, faxed March 29, 2001, for an investment in what I believe is Fairfield Sentry Ltd., one of several investment programs run by Madoff Investment Securities, LLC for third party hedge fund, fund of funds. I do not know who the source was who faxed this document since the fax heading is blank. The document number listed at the bottom of the page appears to read I:\Data\WPDOCS|AG_\94021597

ATTACHMENT 1: Fairfield Sentry Performance Data

Fairfield Sentry Ltd

Fund Category(s):
Long/Short Equity

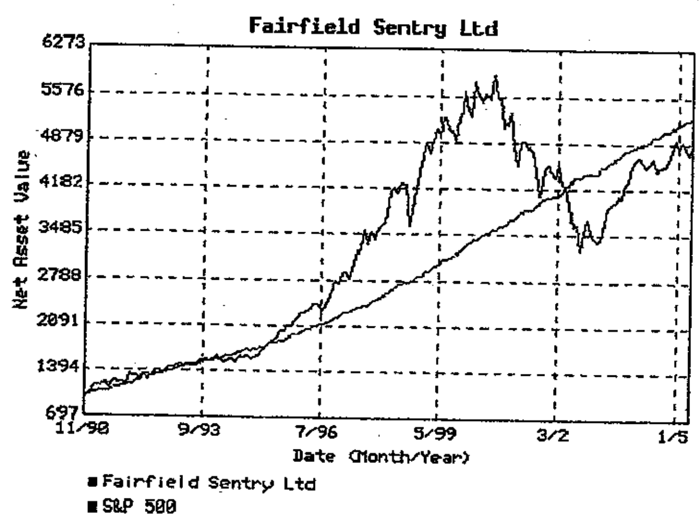
Strategy Description:
The Fund seeks to obtain capital appreciation of its assets principally through the utilization of a nontraditional options trading strategy described as "split strike conversion", to which the Fund allocates the predominant portion of its assets. This strategy has defined risk and profit parameters, which may be ascertained when a particular position is established. Set forth below is a description of the "split strike conversion" strategies ("SSC Investments"). The establishment of a typical position entails (i) the purchase of a group or basket of equity securities that are intended to highly correlate to the S&P 100 Index, (ii) the sale of out-of-the-money S&P 100 Index call options in an equivalent contract value dollar amount to the basket of equity securities, and (iii) the purchase of an equivalent number of out-of-the-money S&P 100 Index put options. An index call option is out-of-the-money when its strike price is greater than the current price of the index; an index put option is out-of-the-money when the strike price is lower than the current price of the index. The basket typically consists of approximately 35 to 45 stocks in the S&P 100. The logic of this strategy is that once a long stock position has been established, selling a call against such long position will increase the standstill rate of return, while allowing upward movement to the short call strike price. The purchase of an out-of-the-money put, funded with part or all of the call premium, protects the equity position from downside risk. A bullish or bearish bias of the positions can be achieved by adjustment of the strike prices in the S&P 100 puts and calls. The further-away the strike prices are from the price of the S&P 100, the more bullish the strategy. However, the dollar value underlying the put options always approximates the value of the basket of stocks.

Contact Info	
Fund:	Fairfield Sentry Ltd
General Partner:	Arden Asset Management
Address:	919 Third Avenue 11th th Floor New York NY 10022 USA
Tel:	212-319-6060
Fax:	
Email:	fairfieldfunds@fggus.com
Contact Person:	Fairfield Funds
Portfolio Manager:	

Fees & Structure	
Fund Assets:	$5100.00million
Strategy Assets:	$5300.00million
Firm Assets:	$8300million
Min. Investment:	$ 0.10million
Management Fee:	1.00%
Incentive Fee:	20.00%
Hurdle Rate:	
High Water Mark:	Yes
Additions:	Monthly
Redemptions:	Monthly
Lockup:	
Inception Date:	Dec-1990
Money Invested In:	United States
Open to New Investments:	Yes

Annual Returns

1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
2.83%	18.58%	14.67%	11.68%	11.49%	12.95%	12.99%	14.00%	13.40%	14.18%	11.55%	10.68%	9.33%	8.21%	7.07%	2.52%



Year To Date:	·2.52%
Highest 12 Month Return:	19.98%
Lowest 12 Month Return:	6.23%
Average Annual Return:	12.00%
Average Monthly Return:	0.96%
Highest Monthly Return:	3.36%
Lowest Monthly Return:	-0.55%
Average Gain:	1.01%
Average Loss:	-0.24%
Profitable Percentage:	95.98%
Compounded Monthly Return:	0.96%
Longest Losing Streak:	1mo
Maximum Drawdown:	-0.55%

Sharpe Ratio (Rolling 12):	2.56
Sharpe Ratio (Annualized):	2.56
Std. Dev. (Monthly):	0.75%
Std. Dev. (Rolling 12):	2.74%
Beta:	0.06
Alpha:	0.91
R:	0.30
R Squared:	0.09

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
1990	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	2.83% E
1991	3.08% E	1.46% E	0.59% E	1.39% E	1.88% E	0.37% E	2.04% E	1.07% E	0.80% E	2.82% E	0.08% E	1.63% E
1992	0.49% E	2.79% E	1.01% E	2.86% E	-0.19%	1.29% E	0.00% E	0.92% E	0.40% E	1.40% E	1.42% E	1.43% E
1993	0.00% E	1.93% E	1.86% E	0.06% E	1.72% E	0.86% E	0.09% E	1.78% E	0.35% E	1.77% E	0.26% E	0.45% E
1994	2.16% E	-0.36%	1.52% E	1.82% E	0.51% E	0.29% E	1.78% E	0.42% E	0.82% E	1.88% E	-0.55%	0.68% E
1995	0.92% E	0.76% E	0.84% E	1.69% E	1.72% E	0.50% E	1.08% E	-0.16%	1.70% E	1.60% E	0.51% E	1.10% E
1996	1.49% E	0.73% E	1.23% E	0.64% E	1.41% E	0.22% E	1.92% E	0.27% E	1.22% E	1.10% E	1.58% E	0.48% E
1997	2.45% E	0.73% E	0.86% E	1.17% E	0.63% E	1.34% E	0.75% E	0.35% E	2.39% E	0.55% E	1.56% E	0.42% E
1998	0.91% E	1.29% E	1.75% E	0.42% E	1.76% E	1.28% E	0.83% E	0.28% E	1.04% E	1.93% E	0.84% E	0.33% E
1999	2.06% E	0.17% E	2.29% E	0.36% E	1.51% E	1.76% E	0.43% E	0.94% E	0.73% E	1.11% E	1.61% E	0.39% E
2000	2.20% E	0.20% E	1.84% E	0.34% E	1.37% E	0.80% E	0.65% E	1.32% E	0.25% E	0.92% E	0.68% E	0.43% E
2001	2.21% E	0.14% E	1.13% E	1.32% E	0.32% E	0.23% E	0.44% E	1.01% E	0.73% E	1.28% E	1.21% E	0.19% E
2002	0.03% E	0.60% E	0.46% E	1.16% E	2.12% E	0.26% E	3.36% E	-0.06%	0.13% E	0.73% E	0.16% E	0.06% E
2003	-0.27%	0.04% E	1.97% E	0.10% E	0.95% E	1.00% E	1.44% E	0.22% E	0.93% E	1.32% E	-0.08%	0.32% E
2004	0.94% E	0.50% E	0.05% C	0.43% C	0.66% C	1.28% C	0.08% C	1.33% E	0.53% E	0.03% E	0.79% E	0.24% E
2005	0.51% E	0.37% E	0.85% C	0.14% C	0.63% C	N/A	N/A	N/A	N/A	N/A	N/A	N/A

END ATTACHMENT # 1 FAIRFIELD SENTRY LTD. PERFORMANCE DATA

Attachment 2: Barron's Article dated May 7, 2001

"Don't Ask, Don't Tell"

Bernie Madoff is so secretive, he even asks investors to keep mum

By ERIN E. ARVEDLUND
Barron's | Monday, May 7, 2001

Two years ago, at a hedge-fund conference in New York, attendees were asked to name some of their favorite and most-respected hedge-fund managers. Neither George Soros nor Julian Robertson merited a single mention. But one manager received lavish praise: Bernard Madoff.

Folks on Wall Street know Bernie Madoff well. His brokerage firm, Madoff Securities, helped kick-start the Nasdaq Stock Market in the early 1970s and is now one of the top three market makers in Nasdaq stocks. Madoff Securities is also the third-largest firm matching buyers and sellers of New York Stock Exchange-listed securities. Charles Schwab, Fidelity Investments and a slew of discount brokerages all send trades through Madoff.

Some folks on Wall Street think there's more to how Madoff (above) generates his enviable stream of investment returns than meets the eye. Madoff calls these claims "ridiculous."

But what few on the Street know is that Bernie Madoff also manages $6 billion-to-$7 billion for wealthy individuals. That's enough to rank Madoff's operation among the world's three largest hedge funds, according to a May 2001 report in MAR Hedge, a trade publication.

What's more, these private accounts, have produced compound average annual returns of 15% for more than a decade. Remarkably, some of the larger, billion-dollar Madoff-run funds have never had a down year.

When Barron's asked Madoff Friday how he accomplishes this, he said, "It's a proprietary strategy. I can't go into it in great detail."

Nor were the firms that market Madoff's funds forthcoming when contacted earlier. "It's a private fund. And so our inclination has been not to discuss its returns," says Jeffrey Tucker, partner and co-founder of Fairfield Greenwich, a New York City-based hedge-fund marketer. "Why Barron's would have any interest in this fund I don't know." One of Fairfield Greenwich's most sought-after funds is Fairfield Sentry Limited. Managed by Bernie Madoff, Fairfield Sentry has assets of $3.3 billion.

A Madoff hedge-fund offering memorandums describes his strategy this way: "Typically, a position will consist of the ownership of 30-35 S&P 100 stocks, most correlated to that index, the

sale of out-of-the-money calls on the index and the purchase of out-of-the-money puts on the index. The sale of the calls is designed to increase the rate of return, while allowing upward movement of the stock portfolio to the strike price of the calls. The puts, funded in large part by the sale of the calls, limit the portfolio's downside."

Among options traders, that's known as the "split-strike conversion" strategy. In layman's terms, it means Madoff invests primarily in the largest stocks in the S&P 100 index -- names like General Electric, Intel and Coca-Cola. At the same time, he buys and sells options against those stocks. For example, Madoff might purchase shares of GE and sell a call option on a comparable number of shares -- that is, an option to buy the shares at a fixed price at a future date. At the same time, he would buy a put option on the stock, which gives him the right to sell shares at a fixed price at a future date.

The strategy, in effect, creates a boundary on a stock, limiting its upside while at the same time protecting against a sharp decline in the share price. When done correctly, this so-called market-neutral strategy produces positive returns no matter which way the market goes.

Using this split-strike conversion strategy, Fairfield Sentry Limited has had only four down months since inception in 1989. In 1990, Fairfield Sentry was up 27%. In the ensuing decade, it returned no less than 11% in any year, and sometimes as high as 18%. Last year, Fairfield Sentry returned 11.55% and so far in 2001, the fund is up 3.52%.

Those returns have been so consistent that some on the Street have begun speculating that Madoff's market-making operation subsidizes and smooths his hedge-fund returns.

How might Madoff Securities do this? Access to such a huge capital base could allow Madoff to make much larger bets -- with very little risk -- than it could otherwise. It would work like this: Madoff Securities stands in the middle of a tremendous river of orders, which means that its traders have advance knowledge, if only by a few seconds, of what big customers are buying and selling. By hopping on the bandwagon, the market maker could effectively lock in profits. In such a case, throwing a little cash back to the hedge funds would be no big deal.

When Barron's ran that scenario by Madoff, he dismissed it as "ridiculous."

Still, some on Wall Street remain skeptical about how Madoff achieves such stunning double-digit returns using options alone. The recent MAR Hedge report, for example, cited more than a dozen hedge fund professionals, including current and former Madoff traders, who questioned why no one had been able to duplicate Madoff's returns using this strategy. Likewise, three option strategists at major investment banks told Barron's they couldn't understand how Madoff churns out such numbers. Adds a former Madoff investor: "Anybody who's a seasoned hedge-fund investor knows the split-strike conversion is not the whole story. To take it at face value is a bit naïve."

Madoff dismisses such skepticism. "Whoever tried to reverse-engineer \, he didn't do a good job. If he did, these numbers would not be unusual." Curiously, he charges no fees for his money-management services. Nor does he take a cut of the 1.5% fees marketers like Fairfield

Greenwich charge investors each year. Why not? "We're perfectly happy to just earn commissions on the trades," he says.

Perhaps so. But consider the sheer scope of the money Madoff would appear to be leaving on the table. A typical hedge fund charges 1% of assets annually, plus 20% of profits. On a $6 billion fund generating 15% annual returns, that adds up to $240 million a year.

The lessons of Long-Term Capital Management's collapse are that investors need, or should want, transparency in their money manager's investment strategy. But Madoff's investors rave about his performance -- even though they don't understand how he does it. "Even knowledgeable people can't really tell you what he's doing," one very satisfied investor told Barron's. "People who have all the trade confirmations and statements still can't define it very well. The only thing I know is that he's often in cash" when volatility levels get extreme. This investor declined to be quoted by name. Why? Because Madoff politely requests that his investors not reveal that he runs their money.

"What Madoff told us was, 'If you invest with me, you must never tell anyone that you're invested with me. It's no one's business what goes on here,'" says an investment manager who took over a pool of assets that included an investment in a Madoff fund. "When he couldn't explain \ how they were up or down in a particular month," he added, "I pulled the money out."

For investors who aren't put off by such secrecy, it should be noted that Fairfield and Kingate Management both market funds managed by Madoff, as does Tremont Advisers, a publicly traded hedge-fund advisory firm.

URL for this article:
http://online.barrons.com/article/SB989019667829349012.html

END ATTACHMENT# 2 BARRON'S ARTICLE

ATTACHMENT 4

Copy of a Fax dated March, 21, 2001 3:57 p.m. from an unknown sender (I forgot who sent it) that explains the Use of Proceeds and Investment Program offered by Fairfield Sentry Ltd but managed by Bernie Madoff. The fax machine header reads NO.880______P.1_______ so it is impossible for me to identify the source at this time. This looks to be pages 6 and 7 of an offering memorandum. [redacted] The document number listed on both pages is a bit blurry [redacted] to read I:\DATA\WPDOCS|AG_\94021597

USE OF PROCEEDS

The entire net proceeds from the sale of the interests will be available to the Partnership. The Partnership incurred approximately $5,000 in connection with the initial offering of Interests for the admission of Limited Partners (such costs consisting primarily of legal fees and blue sky filing fees. The General Partners do no intent to pay any commissions or fees to broker-dealers in connection with the offering. However, in the event any fees or commissions are paid, they will be paid by the General Partners rather than the Partnership. The General Partners have not established any maximum amounts for such fees and commissions, none of which have been paid or earned to date.

The Partnership's funds are allocated to an account at Bernard L. Madoff Investment Securities (see "INVESTMENT PROGRAM"). Funds not so allocated will be maintained in cash. Bernard L. Madoff Securities is employed solely as an agent of the Partnership. It has no ownership interest in the Partnership and no role in the overall management of the Partnership.

The Partnership will not make any loans to affiliated entities nor will it invest in any foreign government securities.

INVESTMENT PROGRAM

The Partnership seeks to obtain capital appreciation of its assets through the utilization of nontraditional options trading strategies. The General Partners have established a discretionary account for the Partnership at Bernard L. Madoff Investment Securities ("BLM"), a registered broker-dealer in New York, New York, which utilizes a strategy described as a "split strike conversion". This strategy has defined risk and profit parameters which may be ascertained when a particular position is established. All investment decisions in the account at BLM are effected by persons associated with BLM. The firm, which employs approximately 150 people, acts primarily as a market maker in stocks and convertible securities. Most of the stocks for which it acts as a market maker are also listed on the New York Stock Exchange. Set forth below is a description of the "split strike conversion strategies.

The establishment of a typical position entails (i) the purchase of equity shares, (ii) the sale of a related out of the money call option representing an amount of underlying shares equal to the number of equity shares purchased, and (iii) the purchase of a related put option which is at or out of the money. A call option is sold out of the money when its strike price is greater than the current price of the stock; a put option is out of the money when the strike price is lower than the current price of the stock.

The logic of this strategy is that once a long stock position has been established, selling a call against such along position will increase the standstill rate of return, while allowing upward movement to the short call strike price. The purchase of an at or out of the money put, funded with part or all of the call premium, protects the equity position from downside risk.

Equity index options are also utilized in this trading methodology. Such a strategy involves buying a group of equity securities that together will highly correlate to the S&P 100 Index ("the OEX"). Equivalent contract value dollar amounts of out of the money OEX call options are sold, and out of the money OEX put options are purchased, against the basket of stocks. The basket typically consists of approximately 35 stocks in the S&P 100 Index.

A bullish or bearish bias of the positions can be achieved by adjustment of the strike prices in the OEX puts and calls. The further away the strike prices are from the price of the S&P 100 Index, the more bullish the strategy. However, the dollar value underlying the put options always approximates the value of the basket of stocks.

The Partnership bears the cost of all brokerage fees and commissions charged in connection with the account at BLM. All interest earned on credit balances is credited to the Partnership.

BLM acts as principal in connection with its sale of securities to the Partnership, and the purchase of securities from the Partnership. BLM acts as a market-maker in the stocks purchased and sold by the Partnership. These market making activities enable BLM to trade with the Partnership as principal. See "CERTAIN RISK FACTORS".

The options transactions executed for the benefit of Sentry are effected, primarily, in the over-the-counter, not on a registered options exchange.

There can be no assurance that the investment objectives of the Partnership will be achieved. THE PARTNERSHIP'S INVESMENT PROGRAM IS SPECULATIVE AND ENTAILS SUBSTANTIAL RISKS. MARKET RISKS ARE INHERENT IN ALL SECURITIES TO VARYING DEGREES. NO ASSURANCE CAN BE GIVEN THAT THE PARTNERSHIP'S INVESTMENT OBJECTIVE WILL BE REALIZED. (SEE "CERTAIN RISK FACTORS".)

Per a conversation with Meaghan Cheong of the NY SEC today:
Categories: **Case 16 Madoff** 12/1/2005 3:01 PM

Per a conversation with Meaghan Cheong of the NY SEC today:

A. She won't comment about the investigation except to say that they are investigating Madoff. She is not allowed to comment on any requests for documents or other requests; or to provide me with updates on the investigation.
B. The SEC has a "No Comment" policy regarding the press.
C. I read her points 1, 2, & 3 above:
1. The SEC needs a trophy for its push to regulate hedge funds and I've just given them one.
2. The SEC needs to show the hedge fund world that they have teeth and are sophisticated enough to regulate hedge funds.
3. The SEC Commissioners can't let Madoff off the hook. If they vote against opening up a formal investigation and Madoff blows up, the SEC's reputation and that of the five commissioners would be destroyed.
D. I failed to ask her if or when the SEC would be opening up a formal investigation.
E. She didn't give me anything concrete to assure me that my fears of the SEC ignoring my case for the 3rd time isn't a legitimate fear on my part. I asked her in various ways to give me that assurance. She just said that they are looking into it.
G. I provided her with additional SEC references that she can ask regarding my abilities and past assistance to the SEC:
1. Peter Bresnans, newly promoted SEC Deputy Chief of Enforcement in Washington.
2. Walter Ricciardi, newply promoted SEC Deputy Chief of Enforcment in Washington.
H. I think I want to give this story to the Wall Street Journal. If Meaghan Cheong (who is a lawyer by training - I asked) had been more definative in her response, I wouldn't have but my safety is in jeapordy. And given the SEC's piss poor political performance [redacted] I can't trust them not to back down to political pressure in DC once [redacted]

----- **Original Message** -----
Categories: **Case 16 Madoff**

12/16/2005 6:20 PM

----- Original Message -----
From: Harry Markopolos
To: Meaghan Cheung
Sent: Friday, December 16, 2005 6:19 PM
Subject: Update on Bernard Madoff

Meaghan,

1. I had a 40 minute telephone conversation with Michael O'Crant, who wrote a story for MAR Hedge published in May 2001 entitled, "Madoff tops charts; skeptics ask how." He lost his hard drive a while back and doesn't have an electronic copy of the story but I am in the process of obtaining a copy and will forward it to you once I do.

2. Michael is willing to meet with you and share his observations on Madoff with you. He said it was the most intriguing story he ever did and that Madoff is either the smartest guy on Wall Street or he's crooked as hell. He also said that even back in 2001, Madoff was only admitting to managing $7 billion but that when Michael was having drinks with 4 or 5 hedge fund fund of fund guys they personally counted $12 - $13 billion in assets under management by Bernie. Lots of things didn't add up and he's happy to share his observations with you. His contact information is included in my 25 page report to the SEC. Mike has a copy of my report and he wanted to send it to Ginny Anderson of the NY Times but I told him not to do that because I gave the Wall Street Journal an exclusive on the story.

3. John Wilke, senior investigative reporter for the Wall Street Journal will soon start working on this story once a major story of his runs next week. He's got a major front page investigative peice coming in next week's Wall Street Journal sometime between Monday - Thursday. You might want to read this story and judge for yourself how competent of a journalist he is. He works out of the Washington office but has strong ties to Boston. He was formerly a reporter for the Boston Globe and then the Wall Street Journal's Boston office. He says he's coming up to Boston to buy me a pint at his favorite pub so already I like him.

4. I've also compiled several pages of contact information that might be useful to the SEC's investigation. I've tried to think of the quickest way for the SEC to determine if Bernie is a fraud or not and believe I've come up with some methods that make sense. I'll try to get that to you next week.

5. There's a good chance I may be in New York on either Wed or Thursday, Dec 21 & 22, on another case involving [redacted] If I'm coming into town, I'll call ahead and see if you'd like to meet with me. I've got a several inch thick file folder on Madoff that I would be happy to let you copy if the SEC has any interest.

Thank you & Good Luck with your inquiries,

Harry Markopolos, CFA
Financial Fraud Investigator
[redacted]

Go to source >>

Received from Meaghan Cheung of the SEC's NY Office: 12/19/2005 1:18 PM
Categories: **Case 16 Madoff**

Received from Meaghan Cheung of the SEC's NY Office:

From: "Cheung, Meaghan S." [redacted]
[Add to Address Book]
To: "Harry Markopolos" [redacted]
Subject: RE: Update on Bernard Madoff
Date: Monday, December 19, 2005 1:07:04 PM Mon, 19 Dec 2005 18:07:04 +0000 [View Source]

Thanks for the update. If you are in New York next week, give us a call.

Meaghan Cheung

Go to source: Comcast Message Center

Harry Markopolos

From: Harry Markopolos [redacted]]
Sent: Wednesday, December 21, 2005 12:46 PM
To: Meaghan Cheung [redacted]
Subject: 05012001 MAR HEDGE MADOFF STORY.doc

Meaghan,

1. Attached is the MAR Hedge article referred to in my report. It's only 5 pages long but covers some of the same material I did in my May 1999 submission to the SEC.
2. Note the references to several feeder funds.
   A. Fairfield Sentry and Tremont you already know about from my report
   B. Kingate (London based) but with offices in New York: FIM(USA), 780 Third Avenue, New York, NY 10017; telephone # 212.223.7321 and fax # 212.223.7592 | in London they are at FIM Advisers LLP, 20 St. James Street, London SW1A 1ES; telephone +44 20 7389 8900 or fax # +44 20 7389 8911; http://www.fim-group.com
   C. Thema (Swiss based) I had not heard mention of prior to reading this article.
3. Note also Madoff's size - $7 billion in 2001 which was huge 5 years ago. O'Crant believes Madoff was actually running at least $12 - $13 billion at the time according to some folks he had spoken with. Now I expect he's in the $30 billion range or thereabouts.
4. Note the reference to superior risk-adjusted returns and Sharpe Ratios of 3.4. To put that 3.4 in perspective, the Financial Analysts Journal, it its November / December 2005 edition (Volume 61, Number 6) contains performance data for various hedge fund categories, 1995-2003. The Sharpe Ratios range from a high of .46 for a Convertible Arbitrage Strategy to the next highest which is .31 for Event-Driven. A 3.4 Sharpe Ratio for a multi-year period would be akin to a baseball player hitting 100 home runs a year while batting .400 (and not cheating by using steroids).
5. Michael O'Crant, the story's author, has agreed to meet with you to discuss what he calls the most intriguing story of his career. Either Madoff is the best trader on Wall Street or he's the largest fraudster in the world. Michael lives and works [redacted] and can be reached at [redacted] or [redacted] He has over 20 years of experience as a financial journalist, so he'll be able to explain his thoughts on Madoff and provide you with areas where you will want to look more closely. I believe he's going on vacation and might not be back in town until after the New Year.
6. I hope you're making out okay during the NYC Transit Strike. I decided not to travel to NYC until the strike is over.

Wishing you much success and good health in 2006,

Harry Markopolos, CFA
[redacted]

Madoff tops charts; skeptics ask how

By Michael Ocrant

May-1-2001 - Mention Bernard L. Madoff Investment Securities to anyone working on Wall Street at any time over the last 40 years and you're likely to get a look of immediate recognition.

After all, Madoff Securities, with its 600 major brokerage clients, is ranked as one of the top three market makers in Nasdaq stocks, cites itself as probably the largest source of order flow for New York Stock Exchange-listed securities, and remains a huge player in the trading of preferred, convertible and other specialized securities instruments.

Beyond that, Madoff operates one of the most successful "third markets" for trading equities after regular exchange hours, and is an active market maker in the European and Asian equity markets. And with a group of partners, it is leading an effort and developing the technology for a new electronic auction market trading system called Primex.

But it's a safe bet that relatively few Wall Street professionals are aware that Madoff Securities could be categorized as perhaps the best risk-adjusted hedge fund portfolio manager for the last dozen years. Its $6—7 billion in assets under management, provided primarily by three feeder funds, currently would put it in the number one or two spot in the Zurich (formerly MAR) database of more than 1,100 hedge funds, and would place it at or near the top of any well-known database in existence defined by assets.

More important, perhaps, most of those who are aware of Madoff's status in the hedge fund world are baffled by the way the firm has obtained such consistent, nonvolatile returns month after month and year after year.

Madoff has reported positive returns for the last 11-plus years in assets managed on behalf of the feeder fund known as Fairfield Sentry, which in providing capital for the program since 1989 has been doing it longer than any of the other feeder funds. Those other funds have demonstrated equally positive track records using the same strategy for much of that period.

Those who question the consistency of the returns, though not necessarily the ability to generate the gross and net returns reported, include current and former traders, other money managers, consultants, quantitative analysts and fund-of-funds executives, many of whom are familiar with the so-called split-strike conversion strategy used to manage the assets.

These individuals, more than a dozen in all, offered their views, speculation and opinions on the condition that they wouldn't be identified. They noted that others who use or have used the strategy — described as buying a basket of stocks closely correlated to an index, while concurrently selling out-of-the-money call options on the index and buying out-of-the-money put options on the index — are known to have had nowhere near the same degree of success.

The strategy is generally described as putting on a "collar" in an attempt to limit gains compared to the benchmark index in an up market and, likewise, limit losses to something less than the benchmark in a down market, essentially creating a floor and a ceiling.

Madoff's strategy is designed around multiple stock baskets made up of 30—35 stocks most correlated to the S&P 100 index. In marketing material issued by Fairfield Sentry, the sale of the calls is described as increasing "the standstill rate of return, while allowing upward movement of the stock portfolio to the strike price of the calls." The puts, according to the same material, are "funded in large part by the sale of the calls, [and] limit the portfolio's downside.

"A bullish or bearish bias can be achieved by adjusting the strike prices of the options, overweighting the puts, or underweighting the calls. However, the underlying value of the S&P 100 puts is always approximately equal to that of the portfolio of stocks," the marketing document concludes.

Throughout the entire period Madoff has managed the assets, the strategy, which claims to use OTC options almost entirely, has appeared to work with remarkable results.

Again, take the Fairfield Sentry fund as the example. It has reported losses of no more than 55 basis points in just four of the past 139 consecutive months, while generating highly consistent gross returns of slightly more than 1.5% a month and net annual returns roughly in the range of 15.0%.

Among all the funds on the database in that same period, the Madoff/Fairfield Sentry fund would place at number 16 if ranked by its absolute cumulative returns.

Among 423 funds reporting returns over the last five years, most with less money and shorter track records, Fairfield Sentry would be ranked at 240 on an absolute return basis and come in number 10 if measured by risk-adjusted return as defined by its Sharpe ratio.

What is striking to most observers is not so much the annual returns — which, though considered somewhat high for the strategy, could be attributed to the firm's market making and trade execution capabilities — but the ability to provide such smooth returns with so little volatility.

The best known entity using a similar strategy, a publicly traded mutual fund dating from 1978 called Gateway, has experienced far greater volatility and lower returns during the same period.

The capital overseen by Madoff through Fairfield Sentry has a cumulative compound net return of 397.5%. Compared with the 41 funds in the Zurich database that reported for the same historical period, from July 1989 to February 2001, it would rank as the best performing fund for the period on a risk-adjusted basis, with a Sharpe ratio of 3.4 and a standard deviation of 3.0%. (Ranked strictly by standard deviation, the Fairfield Sentry funds would come in at number three, behind two other market neutral funds.)

Bernard Madoff, the principal and founder of the firm who is widely known as Bernie, is quick to note that one reason so few might recognize Madoff Securities as a hedge fund manager is because the firm makes no claim to being one.

The acknowledged Madoff feeder funds — New York-based Fairfield Sentry and Tremont Advisors' Broad Market; Kingate, operated by FIM of London; and Swiss-based Thema — derive all the incentive fees generated by the program's returns (there are no management fees), provide all the administration and marketing for them, raise the capital and deal with investors, says Madoff.

Madoff Securities' role, he says, is to provide the investment strategy and execute the trades, for which it generates commission revenue.

[Madoff Securities also manages money in the program allocated by an unknown number of endowments, wealthy individuals and family offices. While Bernie Madoff refuses to reveal total assets under management, he does not dispute that the figure is in the range of $6 billion to $7 billion.]

Madoff compares the firm's role to a private managed account at a broker-dealer, with the broker-dealer providing investment ideas or strategies and executing the trades and making money off the account by charging commission on each trade.

Skeptics who express a mixture of amazement, fascination and curiosity about the program wonder, first, about the relative complete lack of volatility in the reported monthly returns.

But among other things, they also marvel at the seemingly astonishing ability to time the market and move to cash in the underlying securities before market conditions turn negative; and the related ability to buy and sell the underlying stocks without noticeably affecting the market.

In addition, experts ask why no one has been able to duplicate similar returns using the strategy and why other firms on Wall Street haven't become aware of the fund and its strategy and traded against it, as has happened so often in other cases; why Madoff Securities is willing to earn commissions off the trades but not set up a separate asset management division to offer hedge funds directly to investors and keep all the incentive fees for itself, or conversely, why it doesn't borrow the money from creditors, who are generally willing to provide leverage to a fully hedged portfolio of up to seven to one against capital at an interest rate of Libor-plus, and manage the funds on a proprietary basis.

These same skeptics speculate that at least part of the returns must come from other activities related to Madoff's market making. They suggest, for example, that the bid-ask spreads earned through those activities may at times be used to "subsidize" the funds.

According to this view, the benefit to Madoff Securities is that the capital provided by the funds could be used by the firm as "pseudo equity," allowing it either to use a great deal of leverage without taking on debt, or simply to conduct far more market making by purchasing additional order flow than it would otherwise be able to do.

And even among the four or five professionals who express both an understanding of the strategy and have little trouble accepting the reported returns it has generated, a majority still expresses the belief that, if nothing else, Madoff must be using other stocks and options rather than only those in the S&P 100.

Bernie Madoff is willing to answer each of those inquiries, even if he refuses to provide details about the trading strategy he considers proprietary information.

And in a face-to-face interview and several telephone interviews, Madoff sounds and appears genuinely amused by the interest and attention aimed at an asset management strategy designed to generate conservative, low risk returns that he notes are nowhere near the top results of well-known fund managers on an absolute return basis.

The apparent lack of volatility in the performance of the fund, Madoff says, is an illusion based on a review of the monthly and annual returns. On an intraday, intraweek and intramonth basis, he says, "the volatility is all over the place," with the fund down by as much as 1%.

But as whole, the split-strike conversion strategy is designed to work best in bull markets and, Madoff points out, until recently "we've really been in a bull market since '82, so this has been a good period to do this kind of stuff."

Market volatility, moreover, is the strategy's friend, says Madoff, as one of the fundamental ideas is to exercise the calls when the market spikes, which with the right stock picks would add to the performance.

In the current bearish environment, when some market experts think the fund should have been showing negative returns, albeit at levels below the benchmark index, managing the strategy has become more difficult, says Madoff, although performance has remained positive or, as in February, flat.

The worst market to operate in using the strategy, he adds, would be a protracted bear market or "a flat, dull market." In a stock market environment similar to what was experienced in the 1970s, for instance, the strategy would be lucky to return "T-bill like returns."

Market timing and stock picking are both important for the strategy to work, and to those who express astonishment at the firm's ability in those areas, Madoff points to long experience, excellent technology that provides superb and low-cost execution capabilities, good proprietary stock and options pricing models, well-established infrastructure, market making ability and market intelligence derived from the massive amount of order flow it handles each day.

The strategy and trading, he says, are done mostly by signals from a proprietary "black box" system that allows for human intervention to take into account the "gut feel" of the firm's professionals. "I don't want to get on an airplane without a pilot in the seat," says Madoff. "I only trust the autopilot so much."

As for the specifics of how the firm manages risk and limits the market impact of moving so much capital in and out of positions, Madoff responds first by saying, "I'm not interested in educating the world on our strategy, and I won't get into the nuances of how we manage risk." He reiterates the undisputed strengths and advantages the firm's operations provide that make it possible.

Avoiding market impact by trading the underlying securities, he says, is one of the strategy's primary goals. This is done by creating a variety of stock baskets, sometimes as many as a dozen, with different weightings that allow positions to be taken or unwound slowly over a one- or two-week period.

Madoff says the baskets comprise the most highly capitalized liquid securities in the market, making the entry and exit strategies easier to manage.

He also stresses that the assets used for the strategy are often invested in Treasury securities as the firm waits for specific market opportunities. He won't reveal how much capital is required to be deployed at any given time to maintain the strategy's return characteristics, but does say that "the goal is to be 100% invested."

The inability of other firms to duplicate his firm's success with the strategy, says Madoff, is attributable, again, to its highly regarded operational infrastructure. He notes that one could make the same observation about many businesses, including market making firms.

Many major Wall Street broker-dealers, he observes, previously attempted to replicate established market making operations but gave up trying when they realized how difficult it was to do so successfully, opting instead to acquire them for hefty sums.

[Indeed, says Madoff, the firm itself has received numerous buyout offers but has so far refused any entreaties because he and the many members of his immediate and extended family who work there continue to enjoy what they do and the independence it allows and have no desire to work for someone else.]

Similarly, he adds, another firm could duplicate the strategy in an attempt to get similar results, but its returns would likely be unmatched because "you need the physical plant and a large operation" to do it with equal success. However, many Wall Street firms, he says, do use the strategy in their proprietary trading activities, but they don't devote more capital to such operations because their return on capital is better used in other operations.

Setting up a proprietary trading operation strictly for the strategy, or a separate asset management division in order to collect the incentive fees, says Madoff, would conflict with his firm's primary business of market making.

"We're perfectly happy making the commissions" by trading for the funds, he says, which industry observers note also gives the firm the entirely legitimate opportunity to "piggyback" with proprietary trading that is given an advantage by knowing when and where orders are being placed.

Setting up a division to offer funds directly, says Madoff, is not an attractive proposition simply because he and the firm have no desire to get involved in the administration and marketing required for the effort, nor to deal with investors.

Many parts of the firm's operations could be similarly leveraged, he notes, but the firm generally believes in concentrating on its core strengths and not overextending itself. Overseeing the capital provided by the funds and its managed accounts, he says, provides another fairly stable stream of revenue that offers some degree of operational diversification.

Madoff readily dismisses speculation concerning the use of the capital as "pseudo equity" to support the firm's market making activities or provide leverage. He says the firm uses no leverage, and has more than enough capital to support its operations.

He notes that Madoff Securities has virtually no debt and at any given time no more than a few hundred million dollars of inventory.

Since the firm makes markets in only the most highly capitalized, liquid stocks generally represented by the S&P 500 index, a majority of which are listed on the NYSE, as well as the 200 most highly capitalized Nasdaq-listed stocks, says Madoff, it has almost no inventory risk.

Finally, Madoff calls ridiculous the conjecture that the firm at times provides subsidies generated by its market making activities to smooth out the returns of the funds in a symbiotic relationship related to its use of the capital as a debt or equity substitute. He agrees that the firm could easily borrow the money itself at a fairly low interest rate if it were needed, and would therefore have no reason to share its profits. "Why would we do that?"

Still, when the many expert skeptics were asked by MAR/Hedge to respond to the explanations about the funds, the strategy and the consistently low volatility returns, most continued to express bewilderment and indicated they were still grappling to understand how such results have been achieved for so long.

Madoff, who believes that he deserves "some credibility as a trader for 40 years," says: "The strategy is the strategy and the returns are the returns." He suggests that those who believe there is something more to it and are seeking an answer beyond that are wasting their time.

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Tuesday, December 27, 2005 11:56 AM
To: Meaghan Cheung [redacted]
Subject: 12262005 WSJ In FCC Auctions of Airwaves Gabelli was behind the Scenes.doc

Meaghan,

1. Today's Wall Street Journal front-page cover story is an expose on Mario Gabelli of Gabelli Mutual Funds. It is written by senior investigative reporter John Wilke, the same fellow who is doing a similar story on Bernard Madoff. John is based out of Washington but he's from Boston, having served on the Boston Globe's staff and on the WSJ's New England staff before leaving Boston in 1994.

2. I canceled my plans to travel to NYC in the wake of the transit strike but hope to reschedule another trip in mid-January.

3. I've improved my Madoff Report and will send you a revised edition soon. There's some additional mathematical reasons why those types of returns that Madoff claims are not possible. The math is easy for me, but I'm attempting to put it into english so non-derivatives professionals will understand it.

Thank you,

Harry Markopolos, CFA
[redacted]

From: harry[redacted]
To: "Scott Franzblau" [redacted]
Subject: RE: Possible Madoff Plays for your Personal Accounts
Date: Tue, 18 Oct 2005 17:39:23 +0000

Scott,

Darn it! I was afraid of that. And Oppenheimer Funds is owned by the insurance company Mass Mutual, so they'd be able to cover the liability. It'd hurt, but they have the reserves to cover it, so there's not a good individual equity put play with Madoff unless we can think of someone else with large exposure.

Thanks for the information,

Harry

-------------- Original message --------------
Harry,

Oppenheimer Funds Mgt (Mutual Fund CO.) owns Tremont not he BD.

Scott Franzblau
Principal
Benchmark Plus Partners
[redacted]

From: harrymm@comcast.net [mailto[redacted]
Sent: Tuesday, October 18, 2005 11:38 AM
To: Frank Casey; Scott Franzblau; Neil Chelo
Subject: Possible Madoff Plays for your Personal Accounts

Frank,

There's plenty of dry tinder laying next to the powder keg, now all we're waiting for is the spark to set off the expolosion. Banks are merely lemmings in search of the next cliff. And they'll never learn because the FED's always there to bail them out.

Madoff has no need to borrow money, they've got between $20-$30 billion in FOF money. It's got to be a Ponzi, because if they were real they wouldn't be effectively borrowing from their FOF clients at 12-18%, they'd be relying on S-T financing like every other BD and be borrowing at LIBOR + or - some small spread.

As for the fallout from Madoff, here's one possible set of scenarios:
1) Assume that the average FOF has a 20% weighting to Madoff (because he's so "safe" we know that the stupid money European FOFs like Access have a 45% weight which boosts our average. The French & Swiss FOF's have high weights to Madoff whereas the more sane US FOF's would likely limit him to a 5% - 10% weight).

2) Assume the low range of aum is $20 billion, divide by our .20 avg weight and we have $100 billion in FOF exposure on the low end where these FOF's will be met with client redemptions. Assuming avg. leverage of 2, and that's $200 billion in forced selling.
3) If we assume he has aum of $30 billion, then that equates to $300 billion in forced selling.
4) The Swiss and French FOF's with the greatest exposure to Madoff will be crushed.
5) US FOF's with over $4 billion in exposure to Bernie like Tremont will be crushed and their parent, Opennheimer, will be forced to merge into a white knight or it just might implode so quickly that it merely goes under.

Conclusions:
1) Madoff going down will sink a number of Swiss, French and US FOF's. At $20 billion aum he's 2% of the hedge fund market, at $30 billion he's 3%. Not such a huge number that he sinks the markets, but big enough that the unwinding of distressed FOF's leads to a wave of selling turbulence in the convert arb, long-short, merger arb, and other hedge fund sectors. Could the selling cascade into something much bigger ala the 87 crash? It just might - figure 50/50 between it being a replay of 87 or just another Asian Currency Crises type event. We won't know until it happens.
2) FOF's with only a 5% exposure to Madoff are best positioned to survive the immediate aftermath. Those with a 10% exposure are going to face client redemptions because the clients won't trust the rest of the FOF's dud dilligence (when due dilligence fails it should be called dud dilligence). The Euro FOF's and Tremont with > 20% exposures to Madoff are kaput.
3) The secondary effects of Madoff are likely to be of far greater impact to the hedge fund industry. And the fact that the world's largest hedge fund was operating unbeknownst to regulators even realizing they existed will be a huge blow and lead to stricter regulation of hedge funds. Then the fact that FOF's purposely ignored numerous red flags will call the entire FOF industry into question.

How to best play this in your PA:
1) Next month Index put options stuck 5% OTM or thereabouts as your main trading position.
2) If we're within 2 weeks of an expiration, buying $5,000 - $10,000 of near month 8%-10% OTM puts as a spec trade.
3) Puts on Oppenheimer if they have put options listed on it would be a great trade as well. Unlike the indexes which may drop 25% max to perhaps 5% min, the owner of Tremont Capital will see its stock go to 0. (we need tor research this and find out which of the two Oppenheimers' owns Tremont).

-------------- Original message --------------

Banks Putting Kibosh On HF Lending

The recent hedge fund scandals have gotten banks thinking about cutting back on the amount of money they lend HFs, according to *The Independent*. The paper reports that the U.S. **Securities and Exchange Commission** and the U.K.'s **Financial Services Authority** each expressed concern over the amount banks are lending to HFs, which prompted the financial institutions to take a closer look at their lending standards, which one banker called "reckless" and "counterproductive." *The Independent* reports one European bank had a hedge fund exposure of about $88 billion, which was more than 50% greater than the bank's market value. The paper notes that a small number of major banks, notably **JPMorgan Chase, Deutsche Bank, Credit Suisse** and **UBS**, together have more than $500 billion in HF risk.

Frank R. Casey, Director of Marketing
Benchmark-Plus Management LLC

[redacted]

[redacted]

BPM manages $1.5 billion in hedged Fund-Of-Hedge-Funds and since 1998 has produced over 1000 basis points of annualized Alpha with a maximum decline of 210 basis points. Past Performance Is Not Necessarily Indicative of Future Results!

[Back]

Per a conversation with Pat Burns today:
Categories: **Case 16 Madoff**

12/1/2005 2:46 PM

Per a conversation with Pat Burns today:

1. The SEC needs a trophy for its push to regulate hedge funds and I've just given them one.
2. The SEC needs to show the hedge fund world that they have teeth and are sophisticated enough to regulate hedge funds.
3. The SEC Commissioners can't let Madoff off the hook. If they vote against opening up a formal investigation and Madoff blows up, the SEC's reputation and that of the five commissioners would be destroyed.

Per a 30 minute conversation with Pat Burns:
Categories: **Case 16 Madoff** 12/1/2005 3:39 PM

Per a 30 minute conversation with Pat Burns:

1. He is taking the story to the WSJ for assignment to their best investigative reporter.
2. If anything happens to me in the interim, TAF is greenlighted to go to the Press immediately.

SentMail: Email 1 of 8
Categories: **Case 16 Madoff** 12/2/2005 1:03 PM

SentMail: Email 1 of 8 ');} else {document.write('');} previous email '};} else {document.write('');} next email next email

From: harrymm@comcast.net [Add to Address Book] [View Source]
To: "Patrick Burns" [redacted]
Subject: Re: wsj coffee
Date: Fri, 02 Dec 2005 17:53:33 +0000

Pat,

1. I will assemble a file containing contacts for him to telephone. It's a heck of a lot easier for these folks to talk to an investigative reporter than it is to the SEC, so it will be a long list.

2. Story One is calling the senior equity derivatives folks on Wall Street for their opinion on BM's strategy. His best approach is to first ascertain whether BM can achieve anywhere close to 16% annual returns with an unbelievably high (as in this high of a risk to reward ratio is way too high to be believable unless BM is an alien lifeform) 2.55 Sharpe Ratio using the purported strategy. That is big news and will send strong warning tremors across Wall Street and kick Elliott Spitzer into action & unleash a tidal wave of subpoenas from the NYAG's office along with more front page press coverage. An earthquake will soon follow.

3. Story Two is covering the blow up, whenever that is, but these things tend to blow up rather quickly. Enron lasted thru 24 days of WSJ front-page coverage before entering bankruptcy, LTCM was on its knees and mortally wounded within a week, and Refco lasted only a few days after making the front page.

4. Story Three is covering the whistleblower's journey over 6 1/2 years as he turned the case three times and was rebuffed twice by the SEC in May 1999 and October 2001. Knowing that the SEC would gain regulatory authority come Feb 1, 2006, the whistleblower took the case to the SEC in late October 2005 and the SEC opened an investigation the same day. I'd like to plug the fact that the SEC's Section 21A(e) bounty program has only paid bounties to whistleblowers twice in its 71 year history and that the bounty only pays rewards for information related to insider-trading cases. General securities fraud is not rewarded (but should be akin to the FCA and the IRS's 7623 reward programs). The lack of a meaningful bounty program allows and encourages small frauds into becoming large frauds. This fraud should have been stopped in mid-1999 but wasn't due to regulatory gaps and the lack of a working whistleblowers' bounty program.

5. In presenting the package, you can bill it as the largest hedge fund blow up since Long Term Capital Management's in August - October 1998. And, in reality, since it will likely involve hundreds of billions in selling pressure, the losses to investors will be akin to the largest company in the S&P 500, General Electric (with a market capitalization value of $373 billion), suddenly collapsing. Therefore this is a much bigger story than the falls of Enron and WorldCom and truly is the biggest finance story since LTCM's demise that almost led to a systemic collapse of the world's financial system. During LTCM's blow up, the corporate bond markets actually stopped trading and Wall Street's investment banks were in danger of insolvency. While this isn't quite as big as that, it will be almost as much as a watershed event for the $1 trillion hedge fund industry.

6. Please don't mention the [redacted] case [redacted] route on that one.

Thanks! I owe TAF bigtime for this,

Harry

-------------- Original message --------------

I'm having coffee around 2 pm with a WSJ reporter re: the Bernie Mac thing. He is writing the piece on our friend [redacted] and it's a hell of a good story [redacted]. This reporter is a repeat player and he understands that we are elephant hunting. If he can get a clear shot at the target, he will bag this trophy story. He is an investigative reporter, which is good. The WSJ is always cautious, however, and papering the allegations is critical. A good thing to have for him, when you talk, is a list of people he might be able to talk to.

Patrick

Go to source: Comcast Message Center

Per a 9 minute conversation with Neil Chelo:
Categories: **Case 16 Madoff**

12/2/2005 1:05 PM

Per a 9 minute conversation with Neil Chelo:

1. Story is going to the WSJ today at 2 p.m.
2. Be ready for a call from the reporter.
3. I will forward you his name ASAP.
4. Prepare your remarks in advance and determine whether you want your name revealed or if you merely want your title used "source who is a head of risk management at a $1 billion + HFOF with extensive derivatives experience."
5. I asked NRC to send me everything in his database on HFOF's who have deep pockets and who are invested in BM so that I can have my legal team [redacted] investors.

SentMail: Email 1 of 3 From: harrymm@comcast.net [Add to Address Book] [View Source] 12/5/2005 11:53 AM
Categories: **Case 16 Madoff**

SentMail: Email 1 of 3

From: harrymm@comcast.net [Add to Address Book] [View Source]
To: "Patrick Burns" [redacted]
Subject: Re: WSJ coffee
Date: Mon, 05 Dec 2005 16:43:35 +0000

Pat,
1. The New England Regional office of the SEC (Boston) believed me each time I went to them with the case - May 1999, October 2001, and most recently October 25, 2005. Each time they turned it over to the New York office which ignored it the first 2 times it arrived.
2. Boston spent a week looking into it, said to paraphrase "hey, there's something here and it looks big, we'd better send it to New York." Mike Garritty of the Boston Office then called me up and said (to paraphrase), "we looked into Bernie and found some things we are not at liberty to share with you, we've forwarded your information to New York. Per your instructions we have not divulged your identity. They know you as the Boston whistleblower and you would have to identify yourself to them when calling. They are eager to hear from you and you will find them especially attentive and willing to listen. The branch chief's name for the investigation is Meaghan Cheung."
3. I called Meaghan Cheung, New York's Branch Chief covering Madoff. From several calls I can determine:
A. She's an attorney by training but says she's pretty decent at accounting and headed up the Adelphia case for the SEC.
B. She's Korean.
C. She told me that it's her and a SEC Staff Attorney handling my case. This is a key bit of information because rarely does the SEC have a regulator (a Branch Chief) and an enforcer, a Staff Attorney, working side by side unless the case is both high profile and under active investigation. Typically when I go into the SEC's Boston office, since they know me, my attorney and the quality of the cases that I've brougth them in the past, my cases get handled right from the start by regulators teamed with enforcers.
D. She's made a request for documents and sent it to Bernie. Typically, Bernie would then bring in outside counsel to review all docs before sending anything to the SEC. That could take weeks.
E. She's made no mention of this being a formal investigation which means that the SEC Staff in Washington present this to the 5 SEC Commissioners for a vote. Once the Commission votes in favor of opening up a formal investigation, Meaghan Cheung has subpoena power and typically her office would spend a day cranking out a wave of subpoenas. That's usually when the public finds out that a publicly held company is under formal SEC investigation - the target will announce this in a press release. However, Bernie is not a publicly held company, so he wouldn't be forced to disclose this.
4. Meaghen and the SEC regional offices play by gentlemens' rules and never seek publicity or leak about a case under active investigation. They're number one response is "No comment." The only known leaks from the SEC come from their Washington headquarters which won't hesitate to leak when it suits the SEC's interests.
5. After a case is completed, the SEC's Regional personnel - either the Regional Administrator (the top dog even though the title sounds like that of a secretary) or the Region's Chief of Enforcement will issue a press release and usually include some zingers about the defendent, how bad they were, how strict their

punishment is, and how anyone else in the industry caught doing something similar will be found and dealt with too.
6. Since I have to guess, here's what I think:
A. The Boston Office looked in the system and found past audits of Bernie that raised some red flags. They also did an internet search and were able to confirm some details contained in my report. Knowing me and the other good stuff I've brought them they sent it directly to New York.
B. New York read my report and said, "holy shit, this is going to be big, we'd better assign a branch chief and enforcement lawyer to it ASAP."
C. New York made a request for documents and here we sit, waiting for Bernie to produce the requested documents.
7. Some color: whenever a target says it is cooperating fully with an SEC investigation, you can bet they are engaged in a last ditch defense akin to the Battle of Stalingrad. The odds of Bernie producing 100% of the docs requested range between slim and none. The odds of the SEC then elevating the status of the investigation to a formal investigation are close to 100% since if they ignore Bernie and he subsquently blows up, the SEC's reputation would be in tatters. When it comes between the SEC's interests and that of a target, the SEC will investigate and try to be as thorough as they can.
8. Additional color: The SEC has no derivatives experts on its staff. The odds of an SEC branch chief and enforcement attorney understanding the trading strategy involved are less than zero. What to me and the other derivatives professionals in the industry is obviously bogus, won't be intuitive to the SEC's staff.
9. Ponzi Scheme? Most likely but I can't be certain. Even at the low end of the range for his assets under management of $20 billion, that'd be too much for him to return 16% gross. He'd have to earn $3.2 billion per year gross from front-running. That seems high.
10. What I and the other derivatives professionals on Wall Street do know is that he's a fraudster and can't be earning 16% per year from the split-strike conversion options strategy that he says he is using to earn those returns. That alone puts him behind bars.

Harry
-------------- Original message --------------
The reporter at the WSJ is John Wilke. He is interested and I papered him with what you gave me plus a little more that I uncovered myself.
I think the quickest way to a story is if the SEC will confirm there is an investigation. Right now it's a story about something that is "too good to be true," which is a good story but it appears to have been written twice before without the SEC taking action. I am not up to speed on various SEC administrations, and so it may be that this current board will swing a little harder than their predecessors and investigate a little more too.
I know you think this is a Ponzi scheme, not front running, but how long could such a Ponzi scheme last? And how could it last with most of the money coming from a single player? Front running would seem to make more sense, absent a legal explanation (he's a time traveler with a copy of "Barron's History of Stock Indexes, 1980-2050" in his back pocket). These are my questions, not Wilke's (he was going to read your stuff this weekend), but he may raise them himself.
This is a good story -- we just need to flesh out as much as we can for the inevitable questions.
P.

I

From: harry[redacted]
To: [redacted]m (Neil Chelo),[redacted]h (Frank Casey)
Subject: Update on Bernie for the Wall Street Journal
Date: Tue, 06 Dec 2005 01:15:24 +0000

Frank, Neil,

1. The Wall Street Journal senior investigative reporter's name is John Wilke. He's got my report along with an 8 page contact list containing which questions he should ask and who he should ask them of. I gave him contact information for 46 people including you two.
2. Right now he's jammed with a front page story exposing fraud by a major mutual fund family which involves an aerobics instructor (sounds like it'll combine sex with financial fraud so it'll be juicy). Once that story hits and you'll know it when you read it given what I've told you already and what by-line to look for, Bernie is next. We'll see how well this reporter does with the mutual fund case. Also, the guy knows his puts from his calls, so that's a plus.
3. The current thinking is that this story can't just be a rehash of the O'Crant article in MAR Hedge and the Barron's article which Madoff somehow survived. They're going to want to dig deep, real deep and it looks like they're going to investigate BM's entire 40 year career looking for dirt. This could take several weeks before they're ready to go. Apparently he's been working on the mutual fund scandal story for a while now, so at least he's thorough.
4. I recommended that John contacts the following five individuals in this order:
A. Mike O'Crant
B. Erin Arvedlund
C. Frank Casey
D. Neil Chelo
E. Matt Moran while paying a visit to the OEX pit and interviewing the pit traders on BM's split-strike conversion strategy and asking the pit traders whether anyone out there is trading $20 billion plus in OTC OEX puts and calls each month that they don't know about.
5. Figure the Journal's on it just as soon as the mutual fund sex / fraud story hits. In the meantime, get your talking points committed to a sheet of paper and come up with some really witty quotes that combine humor or a story with what your opinion of BM's return stream, volatility, investors etc.... And, if you don't want your name appearing, by all means give him permission to use your title of the Director of Risk Management or SVP of Marketing for a $1 billion plus HFOF. [redacted]

Thank you,

Harry

[Back]

A List of Questions the Wall Street Journal may want to ask RE Bernie Madoff:

"Are you aware of the options buy-write strategy run by Bernie Madoff of Madoff Securities?"

If the answer is "NO, I never heard of Bernie Madoff" then ask:

1. What types of returns would you expect the following split-strike conversion options strategy to achieve?

   A. Purchase 30 – 35 large cap stocks to replicate the OEX Standard & Poor's 100 stock index.

   B. Sell out-of-the-money, over-the-counter, OEX index call options to generate income, and

   C. Buy at-the-money, over-the-counter, OEX index put options to protect against market risk to the downside.

2. Could this split-strike option conversion strategy be capable of earning average annual gross returns of 16% with only 7 monthly losses during the past 14 ½ years?

3. If I told you the largest of those 7 monthly losses was minus (0.55%) what would you say to that?

4. Could this strategy be capable of having a Sharpe Ratio of 2.55?

5. How extraordinary do you consider a 2.55 Sharpe Ratio? What is the typical Sharpe Ratio for the hedge fund industry?

6. Are you aware of any hedge fund that manages in excess of $20 billion of OEX index options?

7. Could $20 billion plus be run by a single hedge fund manager using the strategy I just described without you having heard about it?

8. Would a $20 billion plus, unlevered (meaning without borrowing on margin to increase the size of the fund) hedge fund be considered large?

If the answer is "YES, I've heard of Bernie Madoff," then ask:

1. What do you understand his strategy to be?
2. Do you believe he actually runs the split-strike conversion options strategy he says he's running?
3. How much do you believe his assets under management to be?
4. Can you tell me who the fund of funds are that are invested with him?
5. Can I have their contact information?
6. Madoff has shown investors 16% average annual gross returns, pre-fee, for the past 14 ½ years with only 7 monthly losses, with the larges monthly loss being minus (0.55%) along with a Sharpe Ratio of 2.55. How realistic do you consider those performance numbers to be?
7. Assuming those performance numbers I just stated, how good is a Sharpe Ratio of 2.55 compared to the rest of the hedge fund industry?
8. Name hedge fund managers with better returns than Bernie Madoff? (Steve A. Cohen, or "SAC" might be mentioned but I can't think of too many others in that class of super high performers).
9. Name hedge fund managers with a better Sharpe Ratio than Bernie Madoff?
10. I've heard that Bernie Madoff might be running somewhere between $20 - $50 billion running his options strategy using over-the-counter OEX Standard & Poor's index options. In your opinion, does the OEX index market have the depth and liquidity to handle that much trading size?
11. If Bernie Madoff were running $20 billion plus on an unlevered basis, how do you think his size would rank in the $1 trillion hedge fund industry?
12. Do you know who Bernie Madoff trades his over-the-counter OEX index options through?
13. Have you ever seen the footprints of Bernie Madoff's trades in the markets that you trade?
14. In your opinion, are over-the-counter OEX index options more expensive or less expensive to trade than listed OEX index options traded on the Chicago Board Options Exchange (CBOE)?

15. Do you know which accounting firm Bernie Madoff uses for his outside auditors?

16. Have you heard any stories about Bernie Madoff subsidizing his investors during down months or down markets such as 1997's Asian Currency Crises or 1998's Long Term Capital Management Crises?

17. Have you heard any stories about Bernie Madoff going to cash ahead of major market sell-offs? How do you think he manages to sell ahead of the market?

If I was a Wall Street Journal Reporter the first things I would do is familiarize myself with prior press articles that cast serious suspicion on Bernie Madoff and his purported split-strike options strategy. There are five (5) individuals I would call and or meet with first in order to launch my research effort:

1. I would read the article written by Michael O'Crant, formerly a reporter for MAR Hedge. Mike visited Madoff's offices and saw some unusual things while there for his interview. Mike is currently Director of Alternative Investments; Institutional Investor; New York, NY 10001; Telephone # (212) 224-3821 or (212) 213-6202; mocrant@iiconferences.com I would call him up for coffee, ask him to bring you a copy of his MAR Hedge article, and de-brief him.

2. The 2nd person I would visit with is Ms. Erin Arvedlund, a former Barron's reporter, who wrote her expose on Madoff in the May 7, 2001 edition of Barron's. Attachment 2 in my report contains a reprint of this article and you should read it before meeting with Erin.

3. The 3rd person I would contact is Mr. Frank Casey, Senior VP for Hedge Fund Marketing; Parkway Capital Corporation; 4th Floor; 303 West Main Street; Freehold, NJ 07728; (732) 303-8038; fcasey@bpfunds.com Frank can name you $15 billion or more of Madoff's hedge fund investors. He markets for a $1.5 billion hedge fund, fund of funds, and he used to run a commodity trading advisor. He is intimately familiar with options and believes that Madoff is a fraud. He is willing to speak with you extensively about why he doubts Madoff is for real. Parkway Capital markets for Benchmark Plus, a hedge fund, fund of funds located in Tacoma, WA. Frank and I worked together at Rampart Investment Management Company, Inc. in Boston for several years and he helped Michael O'Crant when Michael was writing his article for MAR Hedge. Frank also has assisted me in reviewing this report. Frank comes into NYC quite often and you definitely want to sit down with him for a full de-briefing.

4. The 4th person I would contact is Mr. Neil Chelo, CFA Director of Risk Management; Benchmark Plus; Tacoma, WA; (253) 573-0657 extension 115; cell # (425) 466-5277; nchelo@bpfunds.com Neil was an equity derivatives portfolio manager who worked for me for many years at Rampart Investment Management Company in Boston, MA. He has years of experience running options strategy similar to the strategy that BM purports to run. He can tell you more reasons than I can on why BM is a fraud. He can also illustrate why a 2.55 Sharpe Ratio that BM says he has is impossible to achieve. Neil also assisted me in reviewing this

report and saw me take this case to the SEC in May 1999 and October 2001. He travels to NYC on a regular basis and would be happy to meet with you.

5. Matt Moran, Esquire; Vice-President of Marketing; Chicago Board Options Exchange (CBOE); 5th Floor; 400 South LaSalle Street; Chicago, IL 60605; (312) 786-7249; moran@cboe.com www.cboe.com I would ask Matt what he knows about Bernie Madoff, if he believes that BM trades $20 billion + in over-the-counter OEX Standard & Poor's index options every month, or if trading that kind of size is even possible. Then I would ask him what his opinion is of BM – is Bernie for real? Who does he recommend that you contact to further your investigation? Ask him for the monthly or annual statistics for the OEX Standard & Poor's 100 index option that the CBOE lists and trades on its exchange. <u>And, by all means, do travel to Chicago and have Matt escort you to the floor of the OEX trading pit. You should ask Matt to hook you up for breakfast, lunch and dinner with the OEX pit traders where you can ask all sorts of questions about Bernie Madoff. Your time spent in Chicago should focus on determining what the OEX index trading professionals think of Bernie Madoff's return numbers and his options trading strategy. Show them the performance tables from Fairfield Sentry Ltd. and ask them for their opinion on whether those numbers are real or not.</u>

After contacting the five (5) parties above and meeting with several OEX pit traders in Chicago, you will know whether the Wall Street Journal has a scoop on the biggest story since the fall of Long Term Capital Management.

Attached below is a list of Financial Services Industry professionals who have derivatives expertise. ***Not all will have heard of Bernie Madoff which is itself a glaring red flag, since someone this large in the options markets should be known by every single person on this list. That perhaps half will have heard of him and the other half will not know who he is seems implausible given Madoff's huge size.*** I left the industry over a year ago and apologize in instances where this contact list is out of date and the people listed have either moved or their telephone numbers have changed.

1. George Anagnos, Executive Vice-President, US Business Development; Euronext Liffe (Europe's largest derivatives exchange); Suite 2602; One Exchange Plaza; 55 Broadway; NY, NY 10006-3008; (212) 482-3000; george.anagnos@liffe.com George is the US head of the largest European derivatives exchange. He's taught derivatives at the post-graduate level for many years.

2. Ed Astrachan, CFA, FSAA; head of asset-liability management at Sunlife Insurance Company in Wellesley, MA; Ed used to run an option buy-write fund for Liberty Mutual Insurance Company and knows options math; (617) 928-0981; or eastrachan@aol.com

3. Ian Baker, CFA; Derivatives Analyst; Wellington Management Company, 21st floor; 75 State Street; Boston, MA 02109; (617) 951-5877 or cell # (617) 645-1394;

idbaker@wellington.com Ian teaches post-graduate courses in derivatives and has extensive derivatives management experience at Wellington Mutual Funds in Boston.

4. Chris Baker; President; C.P. Baker & Company; Suite 301; 303 Congress Street; Boston, MA 02210; (617) 439-0770; Chris is an options expert and he is quite familiar with options strategies. He owns a brokerage firm that trades derivatives.

5. Larry Bernstein; Managing Partner; Amber Mountain Capital Management (a hedge fund); Suite 4002; 100 East Huron Street; Chicago, IL 60611; in New York he can be reached at (212) 224-7396; or his Chicago Cell # (312) 560-1692; larry@ambermountain.com Larry used to head up Salomon Brothers fixed income derivatives trading desk and knows derivatives math inside and out.

6. Professor Zvi Bodie; Finance Professor; Boston University School of Management; Room 534; 595 Commonwealth Avenue; Boston, MA 02215; (617) 353-4160; zbodie@bu.edu; co-author of several textbooks including one with Nobel Prize Winner Robert Merton, co-inventor of the Black-Scholes-Merton options pricing model. Zvi has written extensively on options strategies.

7. Benjamin Bowler; Director of Equity Derivatives Strategy; Merill Lynch; 19th Floor; 4 World Financial Center; New York, NY 10080; (212) 449-3199; 'Benjamin_bowler@ml.com

8. Tony M. Briney; Managing Director; Goldman Sachs (Boston); 19th Floor; 125 High Street; Boston, MA 02110; (617) 204-2246; tony.briney@gs.com Tony heads up the Boston equity derivatives trading desk for Goldman Sachs.

9. Roger Brodie; Derivatives Sales Trader; UBS; 9th Floor; 1285 Avenue of the Americas; NY, NY 10019; (800) 848-8955; (212) 713-3953

10. Frank Casey; Senior VP for Hedge Fund Marketing; Parkway Capital Corporation; 4th Floor; 303 West Main Street; Freehold, NJ 07728; (732) 303-8038; fcasey@bpfunds.com Frank can name you $15 billion or more of Madoff's hedge fund investors. He markets for a $1.5 billion hedge fund, fund of funds, and he used to run a commodity trading advisor. He is intimately familiar with options and believes that Madoff is a fraud. He is willing to speak with you extensively about why he doubts Madoff is for real. Parkway Capital markets for Benchmark Plus, a hedge fund, fund of funds located in Tacoma, WA.

11. Neil Chelo; Director of Risk Management; Benchmark Plus; Tacoma, WA; (253) 573-0657 extension 115; cell # (425) 466-5277; nchelo@bpfunds.com Neil was an equity derivatives portfolio manager who worked for me for many years at Rampart Investment Management Company in Boston, MA. He has years of experience running options strategy similar to the strategy that BM purports to run. He can tell you more reasons than I can on why BM is a fraud. He can also illustrate why a 2.55 Sharpe Ratio that BM says he has is impossible to achieve.

12. Meaghan Cheung, Branch Chief, US Securities & Exchange Commission's New York Regional Office; (212) 336-0050; cheungm@sec.gov Meaghan is a lawyer by training and recently handled the Adelphia Case for the SEC. She is leading the SEC's Madoff investigation. From talking with her I surmise that she's already made a document request to Madoff and that this is not yet a formal investigation where the SEC has subpoena power (which requires a vote of the 5 SEC commissioners).

13. Avi Cohen; President; Avian Securities; Suite 300; 15 Court Square; Boston, MA 02108; (617) 531-3851 or (888) 283-7324; cohena@aviansecurities.com www.avianresearch.com Avi used to be an equity derivatives trader for Kidder, Peabody in NY. He now owns and operates a small broker-dealer and he trades a good bit of equity options for large institutional firms.

14. Dean Curnutt; Principle; Bank of America Securities; 9 West 57th Street; NY, NY 10019; (212) 583-8373; dcurnutt@bofasecurities.com Dean heads up equity derivatives trading strategy for B of A Securities. He's very facile with derivatives mathematics.

15. Dan DiBartolomeo; President; Northfield Information Services; 5th Floor; 184 High Street; Boston, MA 02110; (617) 451-2222; dan@northinfo.com Dan is familiar with the Madoff fraud and says BM's .06 correlation to the S&P 500 using an equity strategy is fishy. Dan's company develops and sells risk management software for portfolio managers and has offices in Boston, London, Moscow, and Tokyo. Ask him what he thinks about the strategy being able to achieve a 2.55 Sharpe Ratio with only 7 down months over 14.5 years with the largest drawdown being minus (0.55%).

16. Ronald M. Egalka, President & CEO; Rampart Investment Management Company, Inc.; 14th Floor; One International Place, Boston, MA 02110; (617) 342-6919; cell # (617) 645-0005; Ron is CEO of a $6 billion + equity derivatives money management firm located in Boston. He has extensive experience with option buy-write strategies. I used to work at Rampart and was their Chief Investment Officer before leaving at the end of August 2004 to start my own firm (after providing several months notice).

17. Robert Fagan; Managing Director; Morgan Stanley; 5th Floor / Equity Derivatives; (212) 761-5030; bfa@ms.com Robert has traded equity derivatives for Morgan Stanley since 1984 (if he's still there). I haven't spoken to him for 3 years, so he may have left during last year's purge by Robert Purcell, Morgan Stanley's now disgraced former Chairman.

18. Justin Ferri, VP of Structured Products; Merrill Lynch; 4 World Financial Center; NY, NY 10080; (212) 449-6577; 'justin_ferri@ml.com Justin used to work on Merrill's equity option trading desk and he might know something about Madoff or he can put you in touch with the head of Merrill's equity derivatives trading desk.

19. Mary R. Foster; Associate Director of Equity Derivatives Trading; Bear Stearns, Three First National Plaza; Chicago, IL 60602; (800) 621-1046 or (312) 580-4095; mrfoster@bear.com

20. Jeff Fritz; Senior Equity Derivatives Sales Trader; Oxford Trading Associates; (800) 333-9089. Jeff has over two decades of equity derivatives trading experience. I consider him to be the world's top equity derivatives trader. Whenever I had an extremely difficult position to trade, Jeff was my first and only call. He's as bright as they come.

21. Andrew Fulton; VP and head of equity derivatives trading; Glen Mede Trust; Suite 1200; 1650 Market Street; Philadelphia, PA 19103-7391; (215) 419-6711; 'andrew_fulton@glenmede.com

22. Hazlitt Gill; VP and Manager Analyst; Citigroup Alternative Investments; 7th Floor; 399 Park Avenue; NY, NY 10043; (212) 559-0198; hazlitt.gill@citigroup.com Citigroup believes that Madoff is a fraud and they don't invest money with him.

23. Amy Goodfriend; Retired Partner; Goldman Sachs (New York); home # (203) 869-6766 Amy used to head up Goldman's equity derivatives trading desk in New York. After the Goldman IPO, she banked her $100 million + in proceeds from the sale and retired shortly after 9-11 to raise her 3 children in Greenwich, CT. Her husband Seth is a managing director of investment banking for Merrill Lynch. She knows options as well as anyone. Goldman Sachs is one of the world's largest derivatives traders, so if she hasn't ever seen Madoff's order flow or seen his footprints in the market, something is very wrong.

24. Andrew Goodman; Equity Derivatives Trader; Lehman Brothers (Boston); 14th floor; 260 Franklin Street; Boston, MA 02110; (617) 330-5972; agoodman@lehman.com

25. Leon Gross; Global Head of Equity Derivatives Research; Citigroup (New York); 3rd floor; 390 Greenwich Street; NY, NY 10013; (800) 492-9833 or (212) 723-7873 leon.j.gross@citigroup.com *I met with Leon in September 2005 and he came right out and said to me, "I can't believe that Madoff hasn't been shutdown by the SEC yet. How can anybody invest in that stupid strategy? It shouldn't even be able to earn a positive return." Leon is head of a large equity derivatives research staff located in offices around the globe. He has an IQ north of 200 and is the brightest equity derivatives researcher currently practicing.*

26. Bob Henry; former marketer for various equity derivatives products; currently in between jobs; (212) 683-2123. Bob knows a lot about who does what and how well on Wall Street regarding equity derivatives.

27. Daniel E. Holland III; Managing Director; Goldman Sachs (Boston) Prime Brokerage; 19th Floor; 125 High Street; Boston, MA 02110; (617) 204-2273 dan.holland@gs.com Goldman Sachs is one of the largest traders of equity derivatives and if they don't handle Madoff's flow or see it in the markets, then something's rotten.

28. Gregory M. Hryb; President; Darien Capital Management; (203) 655-4315; ghryb@aol.com Greg has run hundreds of millions in options related strategies over the years. I worked for him for the 3 years, 1988-1991.

29. Jay Huber; Derivatives Sales Trader; Access Securities; 30 Buxton Farm Road; Stamford, CT 06905; (203) 321-1529; jhuber@accesssecurities.com

30. Tom Huber; Senior VP for Structured Products; Glenmede Trust; Suite 1200; 1650 Market Street; Philadelphia, PA 19103; (215) 419-6988 'tom_huber@glenmede.com Tom has over 20 years of equity derivatives trading experience on both the sellside and the buyside.

31. Professor Robert A. Jarrow; Full Professor; Cornell University; raj15@cornell.edu Bob invented several options formulas that carry his name.

32. Ira G. Kawaller; President; Kawaller & Company, LLC; 162 State Street; Brooklyn, NY 11201-5610; (718) 694-6270; kawaller@kawaller.com

33. Charles Leveroni, Senior VP for equity trading; Lehman Brothers (Boston); 14th Floor; 260 Franklin Street; Boston, MA 02110; (617) 330-5972 or cell # (781) 458-4961; clever@lehman.com

34. Lisa Kay; Director of Institutional Equity Derivatives Trading; Merrill Lynch (New York); 5th Floor; 4 World Financial Center; NY, NY 10080; (212) 449-9882 or (800) 937-0530; lkay@exchange.ml.com

35. Joel Kugler; Equity Derivatives Sales Trader; Catfin; 11th Floor; 450 Park Avenue; NY, NY 10022; (212) 610-1199 or (212) 775-2087; jkugler@catfin.com Joel has over two decades of equity derivatives trading experience.

36. Walter A. Lamerton; Derivatives Sales Trader; SOGEN (a large French Bank); NY, NY; (212) 278-5303 or (212) 278-5310; walter.lamerton@sgcib.com

37. Sanjay Lillaney; CEO; RMG Partners (a hedge fund); Suite 1780; 350 California Street; San Francisco, CA 94104; (415) 544-4214; sl@rmgsf.com Sanjay has run equity derivatives strategies for hedge funds.

38. John P. McAuliffe (nicknamed Johnny Mac); Equity Derivatives Sales Trader; Susquehanna; 3rd Floor; 40 Wall Street; NY, NY 10005-1302; (877) 681-0604 or (212) 709-5335; mcauliff@sig.com Susquehanna is a major market maker on all of the derivatives exchanges so if they don't see Madoff's orders printing that's a big problem.

39. Charlie Miles; Former head of Citigroup's equity derivatives trading desk and now running an internal options volatility arbitrage hedge fund for Deutsche Bank; (212) 454-6284 or cell # (917) 692-2497 He knows everyone on Wall Street and has extensive

equity derivatives trading experience. If he doesn't know of Madoff that's a huge red flag.

40. Michael Millan; Equity Derivatives Sales Trader; Catfin; 450 Park Avenue; NY, NY; (212) 610-1199; mmillan@catfin.com Mike used to head up the options trading desk for Kidder, Peabody. He has 25 + years of Wall Street derivatives experience.

41. Matt Moran, Esquire; Vice-President of Marketing; Chicago Board Options Exchange (CBOE); 5th Floor; 400 South LaSalle Street; Chicago, IL 60605; (312) 786-7249; moran@cboe.com www.cboe.com

42. John O'Connell; Morgan Stanley Equity Derivatives Training Staff; 32nd Floor; 750 7th Avenue; NY, NY 10019; (212) 762-1658 or john.o'connell@msdw.com

43. Michael O'Crant; Director of Alternative Investments; Institutional Investor; New York, NY 10001; Telephone # (212) 224-3821 or (212) 213-6202; mocrant@iiconferences.com

44. Holly Robinson; Deputy Head of Equity Derivatives Trading Desk; Citigroup (New York); 3rd Floor; 390 Greenwich Street; NY, NY 10013; (800) 492-9833 or (212) 723-7873; holly.robinson@citigroup.com

45. Alan Rubenfeld; Managing Director & Head of Program Trading; Deutsche Bank; 60 Wall Street; NY, NY; (856) 351-5793 alan.rubenfeld@db.com Alan wrote the book, "Super Traders," and is quite well known in financial circles. Ask to speak to Matt, Deutsche Bank's head of equity derivatives RE Bernie Madoff. Matt (whose last name I forget but it's Italian) has over 25 years of Wall Street derivatives experience as does his boss Rick Goldshmidt.

46. David Shimko, Ph.D.; Principal; Risk Capital Management; 15th Floor; 1790 Broadway (58th Street); NY, NY 10019; (212) 918-1888 www.e-rcm.com David is well published in the field of derivatives and risk management. He wrote "Continuous Time Finance," which is the standard derivatives textbook used in Ph.D. programs around the world. He knows more about derivatives risk management than anyone else that I know and can critique Madoff's purported strategy as well as anyone.

47. Nikki Tippins; Equity Derivatives Sales Trader; JP Morgan Securities, Inc.; 11th floor; 277 Park Avenue; NY, NY 10172-3401; (212) 622-5722; nikki.tippins@jpmorgan.com

Finally, last and least, my contact information is:

Harry Markopolos, CFA
Work #: [redacted]
E-mail: [redacted]

From: 12/16/2005 4:16 PM
Categories: **Case 16 Madoff**

From: "Wilke, John" <[redacted]
[Add to Address Book]

To: [redacted]>

Subject: inquiry from WSJ

Date: Friday, December 16, 2005 3:30:34 PM Fri, 16 Dec 2005 20:30:34 +0000 [View Source]

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Many thanks for your counsel.

John Wilke
Wall Street Journal
[redacted]-direct
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Go to source: Comcast Message Center

Had an 11 minute telecon with John Wilke of the Wall Street Journal. He has a major 12/16/2005 4:17 PM
Categories: **Case 16 Madoff**

Had an 11 minute telecon with John Wilke of the Wall Street Journal. He has a major story coming out next week between Mon - Thurs night, but wants to fit in a long call with me on Madoff. He used to work for the Boston Globe and the WSJ while in Boston and left here in 1994. Boston is his favorite city and he'd like to be able to come back here to live. Said he'd love to buy me a pint in Boston.

Had a 40 minute call with Michael O'Crant of II Conferences in NYC re his May 2001
Categories: **Case 16 Madoff**

12/16/2005 5:45 PM

Had a 40 minute call with Michael O'Crant of II Conferences in NYC re his May 2001 article for MAR Hedge entitled, "Madoff Tops Charts; Skeptics ask how." He said the following:

1. Madoff was the most interesting story he ever covered.
2. He attributed $7 billion in aum to Madoff at the time of the story but over drinks with 4 or 5 HFOF guys they personally came up with $12 or $13 billion in aum. Bernie was in Michael's words, "The largest hedge fund you never heard of."
3. 2 HFOF's, Fairfield Sentry and one other had large sums invested.
4. He was surprised when I told him that Tremont was an investor.
5. He said he met with several HNW investors with large sums who invested with Bernie and asked them if they knew or even cared about how he was making his returns. They all responded in like fashion saying, "we don't know or care as long as we're earning our steady 1% a month."
6. He said Erin Arvedlund of Barron's called him up and asked for a copy of his MAR Hedge article saying that she wanted to do a follow-up. She then proceeded to plagarize his article. What Barron's wrote had several errors in it as well. Bernie called Mike from a golf course in Europe after the Barron's article hit and said to Mike, "What can you do that's the press." Bernie was non-plussed and showed no anger at Barron's which impressed Mike.
7. He said that Bernie is very charming. When he called Bernie up and said he'd spent months writing a feature article about his fund, Bernie said he was surprised he never heard from anyone that the press was interested in doing such a story. He then asked Mike to come on down to his office - an hour or so later Mike was sitting down in Bernie's office. Bernie became very vague when asked how he generated returns saying that it was proprietary. Investors who need to know what Bernie's doing are told "sorry, you need to invest with someone else." He had 2 interviews with Bernie and came away thinking either this guy is the brightest guy on Wall Street or he's crooked as hell.
8. He did not know that Bernie's accountant is his brother-in-law.
9. He sent Bernie's return numbers to a quant fund to analyze and reverse engineer without letting the quants know where the return numbers came from. They came back and said they could only be from a market-maker.
10. Mike was incredulous that Bernie could have a 60 month long winning streak with no down months. Some US based HFOF's said that those returns were too good to be true and that's why they refused to invest with Bernie.
11. We discussed how BM could afford to pay 16% for funding when other B/D's were funding at much lower short-term rates. That was inexplicable according to Mike.
12. I said that as a derivatives expert myself, I knew this strategy was not capable of beating T-bill returns. Mike laughed and said that other derivatives guys said the same thing including the head trader at Tiger who said, "no way he can trade billions in OTC options without moving the market and the street seeing the trades. Heck, Tiger moved the market with only $100 million trades and this movement made the trading very expensive."
13. He's had bad experiences with [redacted] plagerizing his stories in particular one story he broke while writing for Standard & Poors right before the Gulf War broke out in 1991 about how all of the US exchanges had a conference call on how to handle trading when combat operations began. It was Mike's scoop but the very next day the WSJ put the same story on the [redacted] and only changed the wording of Mike's story a little bit. He then called the managing editor of the [redacted] complain but the guy was totally unresponsive. He also said that the [redacted] has blown the identities of some sources who wished to remain anonymous. Therefore he doesn't trust them and with his over 20 years of reporting experience, he has plenty of reasons not to trust the [redacted]
14. However he does trust Ginny or Jenny Anderson of the NY Times and asked me if he could

send my report to her. I said no that it was for his personal use only.
15. I asked him if he would be willing to cooperate with Ms. Meagan Cheung, Branch Chief of the SEC in New York. I gave him Meaghan's number and e-mail address. He said if she called him he would be glad to cooperate but that he wasn't going to call her.
16. He referred me to the MAR Hedge archives and I found his article but couldn't find a means to purchase it. Mike lost his computer's hard drive a while back and all of his electronic versions of his MAR Hedge stories disappeared. He says he probably has a hard copy in the basement storage unit of his coop though he'd have to search several boxes to locate it if it's still there. He asked me to send him a copy of the article once I got it in electonic format. I agreed to do so.
17.

Spoke to Mike O'Crant: 12/19/2005 11:45 AM
Categories: **Case 16 Madoff**

Spoke to Mike O'Crant:

1. [redacted]

2. He said when he asked HNW investors if they were suspicious about how Madoff earned his returns, everyone told him, "No, as long as I get my 1% a month, I'm happy." One fellow in particular ran RBC's structured hedge funds products desk that offered long-dated options on hedge funds where the P&L could be rolled forward 10 years. He said these seemed to be quite legal, had white shoe legal opinions, and had real risk associated with them. You could roll forward 10 years but that didn't mean you'd have a profit.

3. I let Mike know of [redacted] IRS and sent him IRS [redacted] and IRS [redacted]

4. Mike hadn't yet read my 25 page report on Madoff. He plans on taking it with him on holiday. He's going to his co-op storage unit to get some suitcases, so he may run across the hard copy of his 2001 Madoff article.

20 minute call with Zoe Van Schydel, CFA in Miami, FL. 12/19/2005 12:15 PM
Categories: **Case 16 Madoff**

20 minute call with Zoe Van Schydel, CFA in Miami, FL.

1. She's a freelance reporter writing for Barron's, CFA Magazine, and II and would love to write the story on my big hedge fund case (not identified to her).

2. Spent 10 years at the SEC, left there as a Branch Chief. Says the SEC is bureaucratic and political and turns down slam dunk cases all too often. She had one case where a RIA was paying 90 cents per share commission to a B/D in return for clients. The lawyers for the perp wanted to settle and said they'd sign anything the SEC gave them and pay whatever fine the SEC asks. The SEC enforcement lawyers didn't see how this was illegal even though no disclosure to the clients was ever made about the abnormally high trading commissions.

3. Zoe's contact information is: [redacted] or email at [redacted] She'd like to write my story.

4. Her advice to me RE the SEC is to inform the commissioners who are in favor of hedge fund regulation that there is a big case in NYC and to monitor it.

Kingate operated by FIM Contact Data per Frank Casey 12/21/2005 12:22 PM
Categories: **Case 16 Madoff**

Kingate operated by FIM Contact Data per Frank Casey

William Gilmore
Analyst -Arb Strategies
FIM Advisors LLP
20 St. James Street
London SW1A 1ES
httw://www.fim-group.com/
Tel +44 20 7389 8900

FIM(USA)
780 Third Avenue
New York, NY 10017
(212) 223-7321

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Wednesday, December 21, 2005 12:40 PM
To: [redacted]@wsj[redacted]
Subject: 05012001 MAR HEDGE MADOFF STORY.doc

John,

1. Attached is the article written by Michael O'Crant in the May 1, 2001 edition of MAR Hedge.
2. In speaking with Mike at length, he said it was the most intriguing story of his career. Either Madoff is the most brilliant trader on Wall Street or he's the biggest crook was his opinion.
3. Mike has a real [redacted]. Apparently he [redacted] his stories the next day and it [redacted]ce. He also feels that [redacted] have violated sources confidentiality in the past and didn't want it to happen to him.
4. The most surprising items in the story were that there are two other large feeder funds which I did not account for in my 25 page report to the SEC:
   A. Kingate (run by FIM which has offices in London and New York).
   B. Thema (a swiss based fund of funds)

Regards,

Harry Markopolos, CFA
Financial Fraud Investigator
[redacted]

-----Original Message----- 12/21/2005 2:24 PM
Categories: **Case 16 Madoff**

-----Original Message-----
From: Wilke, John [mailto[redacted]]
Sent: Wednesday, December 21, 2005 2:10 PM
To: Harry Markopolos
Subject: RE: 05012001 MAR HEDGE MADOFF STORY.doc

Thanks for sending, I'll look it over. I'm sorry to hear about [redacted] and hope it involved no one I know. In this business, you have to be honest with people—sources and competitors—or you aren't going to last very long. Did some other paper pick up this story back in 2001?

Whenever possible, I'd prefer to stay under the radar until I've had a chance to dig into this. The fewer folks who know we're studying this, the better. I'll reciprocate and keep your interest confidential for now as well.

I'll be out of town a few days next week, but will have email access. Would welcome anything further you come across that might help me understand this. Looking forward to meeting with you come January.

-----Original Message-----
From: Harry Markopolos [mailto:[redacted]]
Sent: Wednesday, December 21, 2005 12:40 PM
To: Wilke, John
Subject: 05012001 MAR HEDGE MADOFF STORY.doc

John,

1. Attached is the article written by Michael O'Crant in the May 1, 2001 edition of MAR Hedge.

2. In speaking with Mike at length, he said it was the most intriguing story of his career. Either Madoff is the most brilliant trader on Wall Street or he's the biggest crook was his opinion.

3. Mike has a real [redacted] Apparently he [redacted] and it happened more than once. He also feels that [redacted] in the past and didn't want it to happen to him.

4. The most surprising items in the story were that there are two other large feeder funds which I did not account for in my 25 page report to the SEC:

   A. Kingate (run by FIM which has offices in London and New York).

   B. Thema (a swiss based fund of funds)

Regards,

Harry Markopolos, CFA
Financial Fraud Investigator

Madoff tops charts; skeptics ask how

By Michael Ocrant

May-1-2001 - Mention Bernard L. Madoff Investment Securities to anyone working on Wall Street at any time over the last 40 years and you're likely to get a look of immediate recognition.

After all, Madoff Securities, with its 600 major brokerage clients, is ranked as one of the top three market makers in Nasdaq stocks, cites itself as probably the largest source of order flow for New York Stock Exchange-listed securities, and remains a huge player in the trading of preferred, convertible and other specialized securities instruments.

Beyond that, Madoff operates one of the most successful "third markets" for trading equities after regular exchange hours, and is an active market maker in the European and Asian equity markets. And with a group of partners, it is leading an effort and developing the technology for a new electronic auction market trading system called Primex.

But it's a safe bet that relatively few Wall Street professionals are aware that Madoff Securities could be categorized as perhaps the best risk-adjusted hedge fund portfolio manager for the last dozen years. Its $6—7 billion in assets under management, provided primarily by three feeder funds, currently would put it in the number one or two spot in the Zurich (formerly MAR) database of more than 1,100 hedge funds, and would place it at or near the top of any well-known database in existence defined by assets.

More important, perhaps, most of those who are aware of Madoff's status in the hedge fund world are baffled by the way the firm has obtained such consistent, nonvolatile returns month after month and year after year.

Madoff has reported positive returns for the last 11-plus years in assets managed on behalf of the feeder fund known as Fairfield Sentry, which in providing capital for the program since 1989 has been doing it longer than any of the other feeder funds. Those other funds have demonstrated equally positive track records using the same strategy for much of that period.

Those who question the consistency of the returns, though not necessarily the ability to generate the gross and net returns reported, include current and former traders, other money managers, consultants, quantitative analysts and fund-of-funds executives, many of whom are familiar with the so-called split-strike conversion strategy used to manage the assets.

These individuals, more than a dozen in all, offered their views, speculation and opinions on the condition that they wouldn't be identified. They noted that others who use or have used the strategy — described as buying a basket of stocks closely correlated to an index, while concurrently selling out-of-the-money call options on the index and buying out-of-the-money put options on the index — are known to have had nowhere near the same degree of success.

The strategy is generally described as putting on a "collar" in an attempt to limit gains compared to the benchmark index in an up market and, likewise, limit losses to something less than the benchmark in a down market, essentially creating a floor and a ceiling.

Madoff's strategy is designed around multiple stock baskets made up of 30—35 stocks most correlated to the S&P 100 index. In marketing material issued by Fairfield Sentry, the sale of the calls is described as increasing "the standstill rate of return, while allowing upward movement of the stock portfolio to the strike price of the calls." The puts, according to the same material, are "funded in large part by the sale of the calls, [and] limit the portfolio's downside.

"A bullish or bearish bias can be achieved by adjusting the strike prices of the options, overweighting the puts, or underweighting the calls. However, the underlying value of the S&P 100 puts is always approximately equal to that of the portfolio of stocks," the marketing document concludes.

Throughout the entire period Madoff has managed the assets, the strategy, which claims to use OTC options almost entirely, has appeared to work with remarkable results.

Again, take the Fairfield Sentry fund as the example. It has reported losses of no more than 55 basis points in just four of the past 139 consecutive months, while generating highly consistent gross returns of slightly more than 1.5% a month and net annual returns roughly in the range of 15.0%.

Among all the funds on the database in that same period, the Madoff/Fairfield Sentry fund would place at number 16 if ranked by its absolute cumulative returns.

Among 423 funds reporting returns over the last five years, most with less money and shorter track records, Fairfield Sentry would be ranked at 240 on an absolute return basis and come in number 10 if measured by risk-adjusted return as defined by its Sharpe ratio.

What is striking to most observers is not so much the annual returns — which, though considered somewhat high for the strategy, could be attributed to the firm's market making and trade execution capabilities — but the ability to provide such smooth returns with so little volatility.

The best known entity using a similar strategy, a publicly traded mutual fund dating from 1978 called Gateway, has experienced far greater volatility and lower returns during the same period.

The capital overseen by Madoff through Fairfield Sentry has a cumulative compound net return of 397.5%. Compared with the 41 funds in the Zurich database that reported for the same historical period, from July 1989 to February 2001, it would rank as the best performing fund for the period on a risk-adjusted basis, with a Sharpe ratio of 3.4 and a standard deviation of 3.0%. (Ranked strictly by standard deviation, the Fairfield Sentry funds would come in at number three, behind two other market neutral funds.)

Bernard Madoff, the principal and founder of the firm who is widely known as Bernie, is quick to note that one reason so few might recognize Madoff Securities as a hedge fund manager is because the firm makes no claim to being one.

The acknowledged Madoff feeder funds — New York-based Fairfield Sentry and Tremont Advisors' Broad Market; Kingate, operated by FIM of London; and Swiss-based Thema — derive all the incentive fees generated by the program's returns (there are no management fees), provide all the administration and marketing for them, raise the capital and deal with investors, says Madoff.

Madoff Securities' role, he says, is to provide the investment strategy and execute the trades, for which it generates commission revenue.

[Madoff Securities also manages money in the program allocated by an unknown number of endowments, wealthy individuals and family offices. While Bernie Madoff refuses to reveal total assets under management, he does not dispute that the figure is in the range of $6 billion to $7 billion.]

Madoff compares the firm's role to a private managed account at a broker-dealer, with the broker-dealer providing investment ideas or strategies and executing the trades and making money off the account by charging commission on each trade.

Skeptics who express a mixture of amazement, fascination and curiosity about the program wonder, first, about the relative complete lack of volatility in the reported monthly returns.

But among other things, they also marvel at the seemingly astonishing ability to time the market and move to cash in the underlying securities before market conditions turn negative; and the related ability to buy and sell the underlying stocks without noticeably affecting the market.

In addition, experts ask why no one has been able to duplicate similar returns using the strategy and why other firms on Wall Street haven't become aware of the fund and its strategy and traded against it, as has happened so often in other cases; why Madoff Securities is willing to earn commissions off the trades but not set up a separate asset management division to offer hedge funds directly to investors and keep all the incentive fees for itself, or conversely, why it doesn't borrow the money from creditors, who are generally willing to provide leverage to a fully hedged portfolio of up to seven to one against capital at an interest rate of Libor-plus, and manage the funds on a proprietary basis.

These same skeptics speculate that at least part of the returns must come from other activities related to Madoff's market making. They suggest, for example, that the bid-ask spreads earned through those activities may at times be used to "subsidize" the funds.

According to this view, the benefit to Madoff Securities is that the capital provided by the funds could be used by the firm as "pseudo equity," allowing it either to use a great deal of leverage without taking on debt, or simply to conduct far more market making by purchasing additional order flow than it would otherwise be able to do.

And even among the four or five professionals who express both an understanding of the strategy and have little trouble accepting the reported returns it has generated, a majority still expresses the belief that, if nothing else, Madoff must be using other stocks and options rather than only those in the S&P 100.

Bernie Madoff is willing to answer each of those inquiries, even if he refuses to provide details about the trading strategy he considers proprietary information.

And in a face-to-face interview and several telephone interviews, Madoff sounds and appears genuinely amused by the interest and attention aimed at an asset management strategy designed to generate conservative, low risk returns that he notes are nowhere near the top results of well-known fund managers on an absolute return basis.

The apparent lack of volatility in the performance of the fund, Madoff says, is an illusion based on a review of the monthly and annual returns. On an intraday, intraweek and intramonth basis, he says, "the volatility is all over the place," with the fund down by as much as 1%.

But as whole, the split-strike conversion strategy is designed to work best in bull markets and, Madoff points out, until recently "we've really been in a bull market since '82, so this has been a good period to do this kind of stuff."

Market volatility, moreover, is the strategy's friend, says Madoff, as one of the fundamental ideas is to exercise the calls when the market spikes, which with the right stock picks would add to the performance.

In the current bearish environment, when some market experts think the fund should have been showing negative returns, albeit at levels below the benchmark index, managing the strategy has become more difficult, says Madoff, although performance has remained positive or, as in February, flat.

The worst market to operate in using the strategy, he adds, would be a protracted bear market or "a flat, dull market." In a stock market environment similar to what was experienced in the 1970s, for instance, the strategy would be lucky to return "T-bill like returns."

Market timing and stock picking are both important for the strategy to work, and to those who express astonishment at the firm's ability in those areas, Madoff points to long experience, excellent technology that provides superb and low-cost execution capabilities, good proprietary stock and options pricing models, well-established infrastructure, market making ability and market intelligence derived from the massive amount of order flow it handles each day.

The strategy and trading, he says, are done mostly by signals from a proprietary "black box" system that allows for human intervention to take into account the "gut feel" of the firm's professionals. "I don't want to get on an airplane without a pilot in the seat," says Madoff. "I only trust the autopilot so much."

As for the specifics of how the firm manages risk and limits the market impact of moving so much capital in and out of positions, Madoff responds first by saying, "I'm not interested in educating the world on our strategy, and I won't get into the nuances of how we manage risk." He reiterates the undisputed strengths and advantages the firm's operations provide that make it possible.

Avoiding market impact by trading the underlying securities, he says, is one of the strategy's primary goals. This is done by creating a variety of stock baskets, sometimes as many as a dozen, with different weightings that allow positions to be taken or unwound slowly over a one- or two-week period.

Madoff says the baskets comprise the most highly capitalized liquid securities in the market, making the entry and exit strategies easier to manage.

He also stresses that the assets used for the strategy are often invested in Treasury securities as the firm waits for specific market opportunities. He won't reveal how much capital is required to be deployed at any given time to maintain the strategy's return characteristics, but does say that "the goal is to be 100% invested."

The inability of other firms to duplicate his firm's success with the strategy, says Madoff, is attributable, again, to its highly regarded operational infrastructure. He notes that one could make the same observation about many businesses, including market making firms.

Many major Wall Street broker-dealers, he observes, previously attempted to replicate established market making operations but gave up trying when they realized how difficult it was to do so successfully, opting instead to acquire them for hefty sums.

[Indeed, says Madoff, the firm itself has received numerous buyout offers but has so far refused any entreaties because he and the many members of his immediate and extended family who work there continue to enjoy what they do and the independence it allows and have no desire to work for someone else.]

Similarly, he adds, another firm could duplicate the strategy in an attempt to get similar results, but its returns would likely be unmatched because "you need the physical plant and a large operation" to do it with equal success. However, many Wall Street firms, he says, do use the strategy in their proprietary trading activities, but they don't devote more capital to such operations because their return on capital is better used in other operations.

Setting up a proprietary trading operation strictly for the strategy, or a separate asset management division in order to collect the incentive fees, says Madoff, would conflict with his firm's primary business of market making.

"We're perfectly happy making the commissions" by trading for the funds, he says, which industry observers note also gives the firm the entirely legitimate opportunity to "piggyback" with proprietary trading that is given an advantage by knowing when and where orders are being placed.

Setting up a division to offer funds directly, says Madoff, is not an attractive proposition simply because he and the firm have no desire to get involved in the administration and marketing required for the effort, nor to deal with investors.

Many parts of the firm's operations could be similarly leveraged, he notes, but the firm generally believes in concentrating on its core strengths and not overextending itself. Overseeing the capital provided by the funds and its managed accounts, he says, provides another fairly stable stream of revenue that offers some degree of operational diversification.

Madoff readily dismisses speculation concerning the use of the capital as "pseudo equity" to support the firm's market making activities or provide leverage. He says the firm uses no leverage, and has more than enough capital to support its operations.

He notes that Madoff Securities has virtually no debt and at any given time no more than a few hundred million dollars of inventory.

Since the firm makes markets in only the most highly capitalized, liquid stocks generally represented by the S&P 500 index, a majority of which are listed on the NYSE, as well as the 200 most highly capitalized Nasdaq-listed stocks, says Madoff, it has almost no inventory risk.

Finally, Madoff calls ridiculous the conjecture that the firm at times provides subsidies generated by its market making activities to smooth out the returns of the funds in a symbiotic relationship related to its use of the capital as a debt or equity substitute. He agrees that the firm could easily borrow the money itself at a fairly low interest rate if it were needed, and would therefore have no reason to share its profits. "Why would we do that?"

Still, when the many expert skeptics were asked by MAR/Hedge to respond to the explanations about the funds, the strategy and the consistently low volatility returns, most continued to express bewilderment and indicated they were still grappling to understand how such results have been achieved for so long.

Madoff, who believes that he deserves "some credibility as a trader for 40 years," says: "The strategy is the strategy and the returns are the returns." He suggests that those who believe there is something more to it and are seeking an answer beyond that are wasting their time.

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Wednesday, December 21, 2005 5:24 PM
To: 'Frank Casey'
Subject: RE: re Ocrant['s story

Frank,

No debt at $6 or $7 billion gets my hopes up that it's a front-running scheme and qualifies for the SEC bounty. But, at $30 billion, I'm thinking Ponzi. Still, anything's possible. We know with 100% certainty that he's not using an OEX OTC split-strike conversion options strategy and that alone puts Bernie into prison. [redacted] If so, then you can enjoy several [redacted] the pitcher, you have to compete with all of the other pitchers.

Harry

-----Original Message-----
From: Frank Casey [mailto:[redacted]]
Sent: Wednesday, December 21, 2005 4:22 PM
To: Harry Markopolos
Subject: re Ocrant['s story

Re-reading that story shows just how much can be called into question. He claims no debt so it must be commissions and perhaps even piggy-backing. Neither explain how he can produce granular returns on essentially a bull market strategy.

Frank R. Casey, Director of Marketing
Benchmark-Plus Management LLC

[redacted]

[redacted]

BPM manages $1.5 billion in hedged Fund-Of-Hedge-Funds and since 1998 has produced over 1000 basis points of annualized Alpha with a maximum decline of 230 basis points. Past Performance Is Not Necessarily Indicative of Future Results!

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Tuesday, December 27, 2005 11:23 AM
To: Frank Casey ([redacted] Neil Chelo [redacted]n)
Subject: 12262005 WSJ In FCC Auctions of Airwaves Gabelli was behind the Scenes.doc

Frank, Neil

1. Attached is today's Wall Street Journal front-page cover story written by senior investigative reporter John Wilke. He's going to be writing the Madoff story starting in January but I don't know how long it will take. The Gabellis Story took time and I'm sure this one will too.

2. [redacted]

Harry

2006 Madoff Case Activity Cover Page

Date of Analysis: 12/28/2008

I have organized 2006 into two parts:

Part One consists of my 03/03/2006 conversation memo from a five-minute telephone call with New York SEC Branch Chief Meaghan Cheung.

Part Two consists of a chronological listing of e-mails and evidence gathering by Frank Casey, Neil Chelo, Mike Ocrant and myself during the year.

1. I am currently planning on only submitting Part One, my March 3, 2006 conversation memo of the call with the New York SEC Branch Chief to Congress.

2. I would like a legal review of the case documents [redacted] to determine if they should be released to Congress, to the SEC's Inspector General, to US law enforcement, to foreign law enforcement, to victim's, to the plaintiff's bar, to the defendant's bar, and to the public.

Thank you,

Harry Markopolos, CPA, CFE
Chartered Financial Analyst
Certified Fraud Examiner

-----Original Message----- From: Harry Markopolos [mailto:harrymm@comcast.net] Sent: 1/16/2006 1:56 PM
Categories: **Case 16 Madoff**

-----Original Message-----
From: Harry Markopolos [mailto[redacted]
Sent: Monday, January 16, 2006 1:56 PM
To: 'Neil Chelo'
Subject: RE: Madoff
Neil,
1. Am I that lucky? Gee, I sure hope that's how Bernie is earning his returns. Front-running customer order flow would qualify for the SEC's insider-trading reward whereas a simple Ponzi Scheme would not.
2. I believe he has to be running $30 billion right now, plus or minus $10 billion, which seems to large a base to earn those kind of returns on.
3. There are 4 possible combinations:
A. 100% Ponzi
B. 100% Front-running
C. Mix of Ponzi and Front-running
D. Bernie is an alien life form from outer space with inhuman forecasting skills
4. A thru C above are illegal.
5. D, if true, would cause a panic in the marketplace according to Mike Garrity, SEC Branch Chief in Boston. He said it would scare investors because they would lose confidence that they had a fair shot at beating the market if there were aliens cherry picking our markets.
Good luck with your studies,
Harry

-----Original Message-----
From: Neil Chelo [mailto:[redacted]
Sent: Friday, January 13, 2006 2:43 PM
To: [redacted]
Subject: Madoff
Spoke to Steven W. Winters today of Gemini Investments in NYC. He worked for Madoff from 2/94 to 7/97. He was involved in prop. trading and overseeing market makers.
While he did not work in HF Option unit, he said it is the real deal. Having knowledge of limit order book was a big money maker.
Neil

Spoke to Neil Chelo RE Steven W. Winters observations: 1/17/2006 11:06 AM
Categories: **Case 16 Madoff**

Spoke to Neil Chelo RE Steven W. Winters observations:

1. Steve said if BM had 10% of the order flow on IBM shares, it extrapolated that to being what the NYSE order book looked like.
2. If IBM was at 100 and BM had lots of limit orders to sell IBM at 104, they were safe selling 105 strike calls.
3. This argument falls apart since BM purports to only sell OEX OTC Index calls and purchase OEX OTC Index puts.
4. Steve never saw any of the options transactions. He ran the risk book on the stock trading side.
5. Steve thinks BM and his two sons are brilliant and hard-working. He believes in Bernie.

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Monday, January 23, 2006 10:23 AM
To: 'Frank Casey'
Subject: RE: have you heard boo from WSJ reporter yet?

Frank,

The chances of BM being for real are somewhere between slim and none. I can only get paid if he was front-running his B/D's order flow. Lots of luck with that being the case. There's no way that you can earn returns for $30 billion in aum via front-running order flow. $1 or even $2 B maybe, but $30 B is out of the question.

Harry

-----Original Message-----
From: Frank Casey [mailto[redacted]
Sent: Monday, January 23, 2006 10:09 AM
To: Harry Markopolos
Subject: RE: have you heard boo from WSJ reporter yet?

Good Luck and I hope that you make money somehow on this!

Frank R. Casey, Director of Marketing, Benchmark-Plus Management LLC

[redacted]

[redacted]

BPM manages $1.5 billion in hedged Fund-Of-Hedge-Funds. Past Performance Is Not Necessarily Indicative of Future Results!

From: Harry Markopolos [mailto:harrymm@comcast.net]
Sent: Monday, January 23, 2006 7:07 AM
To: Frank Casey
Subject: RE: have you heard boo from WSJ reporter yet?

Frank,

Yes I have, we're speaking this week by telephone to arrange a time for him to travel to Boston and interview me / review the file.

Harry

-----Original Message-----
From: Frank Casey [mailto[redacted]
Sent: Monday, January 23, 2006 9:55 AM

To: [redacted]
Subject: have you heard boo from WSJ reporter yet?

Frank R. Casey, Director of Marketing
Benchmark-Plus Management LLC

[redacted]

[redacted]

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Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Monday, January 30, 2006 4:13 PM
To: Frank Casey [redacted]
Cc: Neil Chelo ([redacted]
Subject: Integral Partners Derivatives Hedge Fund Fraud Just Now going to Trial

Frank, Neil,

1. The Integral Partners hedge fund fraud case is finally going to trial 5 years and 5 months after this Ponzi Scheme collapsed in the wake of 9-11.

2. That's why I called the Wall Street Journal RE Madoff. If the SEC took this long to address a simple derivatives fraud like Integral, what chance do they have with Madoff?

3. Darren Unruh, formerly of Kennedy Capital Advisors, and now running his own hedge fund and fund of funds called me for advice. The SEC asked him to testify and offered to pay his travel expenses. I told him to take them up on their offer.

4. In looking back, Integral came up on Frank's radar screen because they purported to use a derivatives strategy and had an excellent Sharpe Ratio. Frank called in a favor and obtained their power point slides. Frank asked me to take a look and tell him what they were doing. I couldn't make heads or tails of the slides but came up with 7 derivatives questions to ask Integral. Frank and I put them on speaker phone, I asked all 7 questions and received 7 totally wrong answers which made it clear that these guys were a fraud. Integral didn't know the first thing about options. Little did we know that Kennedy Capital, the Chicago Art Institute, and Integral Partners were all linked. But, even if we had, it was too late for the Kennedy's and the Chicago Art Institute. By that time most of the money was already spent on fast cars, fast women, and other things.

5. The SEC is in way over their heads with respect to hedge fund frauds that much is clear.

Thought you'd be as amazed as I was to find out that the SEC's civil case still hasn't gone to trial,

Harry

-----Original Message----- From: Harry Markopolos [mailto:harrymm@comcast.net] Sent: 1/30/2006 4:48 PM
Categories: **Case 16 Madoff**

-----Original Message-----
From: Harry Markopolos [mailto:[redacted]
Sent: Monday, January 30, 2006 4:48 PM
To: 'Frank Casey'
Subject: RE: Integral Partners Derivatives Hedge Fund Fraud Just Now going to Trial
Frank,
Bernie is actually borrowing at 16% because he's delivering 12% net to investors after the HFOF's take their 1% and 20%. 16% minus the HFOF 1% management fee = 15%. .20 times 15% = 3%. So the HFOF's are receiving 4% (1% + 20% of 15% or 3%) while the investors receive 12%. Bernie "earns" only commissions or so he says. However, we all know he isn't trading $20 - $50 billion worth of OTC OEX options each month. The SEC left to their own devices is incapable of catching Bernie Madoff. The SEC's legal staff is dumber than dirt and there's not one of them I've met that can count to 21 without pulling down his pants to find that "last digit." The Wall Street Journal however has brought down frauds and it doesn't take them long either. Enron lasted just 24 days before filing for bankruptcy after making the front page. Ditto for WorldCom. Refco only lasted a weekend, but it was a B/D and totally reliant on the overnight repo market. Bernie won't last long after his next front page appearance either.

Harry
-----Original Message-----
From: Frank Casey [mailto:[redacted]
Sent: Monday, January 30, 2006 4:21 PM
To: Harry Markopolos
Subject: RE: Integral Partners Derivatives Hedge Fund Fraud Just Now going to Trial
Hey, their job is to not lose face, or take career risks; whaddau expect? Bernie will be retired before they get their act together I expect. Not saying that he is a fraud or anything but still No One can answer one simple question: Why borrow at 12% when a BD can borrow at 40 bp over LIBOR? But then Berbie says he won't leverage and why should he, he has dumb money!
Frank R. Casey, Director of Marketing, Benchmark-Plus Management LLC
[redacted]
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Frank R. Casey, Director of Marketing, Benchmark-Plus Management LLC

[redacted]

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To: Frank Casey
Cc: Neil Chelo

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5. The SEC is in way over their heads with respect to hedge fund frauds that much is clear.

Thought you'd be as amazed as I was to find out that the SEC's civil case still hasn't gone to trial,

Harry

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Tuesday, February 07, 2006 3:40 PM
To: John Wilke [redacted]e@wsj.[redacted]
Subject: Update from Harry Markopolos

John,

I know you're flying over the pond later in the week. Just touching base to see if you have a date in mind for a trip to Beantown? I have a few inches of background material I'm going to have copied for your work files / research effort.

Safe travels,

Harry Markopolos, CFA
Financial Fraud Investigator
[redacted]

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Thursday, February 16, 2006 4:30 PM
To: 'Frank Casey'
Subject: RE: reporter making progress?

Frank,

He's supposed to be coming to Boston next week. I just went out and had a very thick file copied for him.

Harry

-----Original Message-----
From: Frank Casey [mailto[redacted]]
Sent: Thursday, February 16, 2006 3:46 PM
To: [redacted]
Subject: reporter making progress?

Frank R. Casey, Director of Marketing
Benchmark-Plus Management LLC

[redacted]

[redacted]

BPM manages $1.4 billion in hedged Fund-Of-Hedge-Funds. Benchmark Plus Partners LLC Market Neutral Fund, our flagship vehicle since 1998, has produced over 950 basis points of annualized Alpha with a maximum decline of 150 basis points. Past Performance Is Not Necessarily Indicative of Future Results!

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Friday, February 17, 2006 4:56 PM
To: John Wilke [redacted]@wsj.[redacted]
Subject: Boston Visit for Madoff Story?

John

Will you be coming to Boston next week? My calendar for the week of Feb 20th is relatively light. I have a Dr.'s appointment on Tuesday, the 21st at 1:40 p.m. in downtown Boston but am otherwise free. I made copies of my files for you to take back with you.

Harry
[redacted]

Harry Markopolos

From: Harry Markopolos [harrymm@comcast.net]
Sent: Tuesday, March 21, 2006 11:59 AM
To: 'Frank Casey'
Subject: RE: Reporter drop ball or did he visit & get your file?

Frank

The REFCO Story appeared in the Wall Street Journal on Friday and they never opened for business on Monday because they filed for bankruptcy on Sunday. That's the WSJ advantage. Enron, number 7 on the Fortune 500 list, appeared on the cover of the WSJ. They lasted 24 days before their bankruptcy filing. Madoff will be no different and I suspect he'll resemble REFCO more than Enron. Figure 2 – 24 days is the range of how these firms last once the WSJ goes to print.

Harry

-----Original Message-----
From: Frank Casey [mailto[redacted]]
Sent: Tuesday, March 21, 2006 11:35 AM
To: Harry Markopolos
Subject: RE: Reporter drop ball or did he visit & get your file?

If you get frustrated, why go to a traditional news reporter? Why not do it yourself and publish a piece in 1-2 industry rags like Albourne or Opalesque.
http://village.albourne.com/

Or

http://www.opalesque.com/main.php? Matthias F. Knab, Founder-Editor
Opalesque Alternative Market Briefing
Sonnenstr. 2
Munich 80331
Germany
[49] 89-512668-0 knab@opalesque.com

Or maybe try reporter:
Niki Natarajan
Editor **InvestHedge**
HedgeFund Intelligence
Douglas House
16-18 Douglas Street
London
SW1P 4PB
Dir: +44 (0) 20 7901 1936
Tel: +44 (0) 20 7233 8585
Fax:+44 (0) 20 7630 7948
www.hedgefundintelligence.com
Niki Natarajan [nnatarajan@hedgefundintelligence.com]

All three have very large alternatives readership. You will ignite a firestorm so be prepared for the outcome. Double check your facts.

Frank R. Casey, Director of Marketing, Benchmark-Plus Management LLC

[redacted]

[redacted]

Benchmark Plus is a <u>hedged</u>, fund-of-hedge-funds producing market-neutral, zero-beta absolute returns. **<u>Past Performance Is Not Necessarily Indicative of Future Results!</u>**

From: Harry Markopolos [mailto:[redacted]
Sent: Tuesday, March 21, 2006 7:56 AM
To: Frank Casey
Subject: RE: Reporter drop ball or did he visit & get your file?

I tried calling him yesterday to find out what's happening. If he doesn't want the story then I will go to Jenny Anderson of the NY Times.

Harry

> -----Original Message-----
> **From:** Frank Casey [mailto:[redacted]
> **Sent:** Tuesday, March 21, 2006 10:42 AM
> **To:** Harry Markopolos
> **Subject:** Reporter drop ball or did he visit & get your file?
>
> Frank R. Casey, Director of Marketing
> Benchmark-Plus Management LLC
>
> [redacted]
>
> [redacted]
>
> Benchmark Plus is a <u>hedged</u>, fund-of-hedge-funds producing market-neutral, zero-beta absolute returns. We isolate each sub-manager's alpha by removing the portion of return that is due to market influences (beta). **<u>Past Performance Is Not Necessarily Indicative of Future Results!</u>**

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Wednesday, May 31, 2006 9:20 AM
To: 'Frank Casey'
Subject: RE: Madoff Cover Story may be the next one that John Wilkie publishes for the Wall Street Journal

Frank,

The only thing I stand to gain (probably) is lots of free publicity and perhaps invitations to speak at hedge fund conferences. I doubt there's any money in the Madoff case. If it is a Ponzi, the SEC will be more worried about giving the suckers pennies on the dollar back and will likely screw me out of the reward money. [redacted] But it's a good start. [redacted]

Thanks for your support thru the process,

Harry

-----Original Message-----
From: Frank Casey [mailto[redacted]
Sent: Wednesday, May 31, 2006 8:52 AM
To: Harry Markopolos
Subject: RE: Madoff Cover Story may be the next one that John Wilkie publishes for the Wall Street Journal

Good luck; this should validate your new career path.

Frank R. Casey, Director of Marketing, Benchmark-Plus Management LLC

[redacted]

[redacted]

Benchmark Plus is a hedged, fund-of-hedge-funds producing market-neutral, zero-beta absolute returns.
Past Performance Is Not Necessarily Indicative of Future Results!

From: Harry Markopolos [mailto:harrymm@comcast.net]
Sent: Wednesday, May 31, 2006 6:51 AM
To: Frank Casey
Subject: RE: Madoff Cover Story may be the next one that John Wilkie publishes for the Wall Street Journal

Frank,

I am in active discussions with the Wall Street Journal but cannot say more at this point. They realize that if they print Madoff on the front page they have to be right as rain, because of the fallout.

Harry

-----Original Message-----
From: Frank Casey [mailto:[redacted]]
Sent: Wednesday, May 31, 2006 8:42 AM
To: Harry Markopolos
Subject: RE: Madoff Cover Story may be the next one that John Wilkie publishes for the Wall Street Journal

Harry,
Maybe you should go to a HF news rag to get published as the traditional outlets and SEC seemed stalled.

Frank R. Casey, Director of Marketing, Benchmark-Plus Management LLC

[redacted]

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From: Harry Markopolos [mailto[redacted]]
Sent: Sunday, April 09, 2006 7:56 AM
To: Neil Chelo
Cc: Frank Casey
Subject: Madoff Cover Story may be the next one that John Wilkie publishes for the Wall Street Journal

Neil, Frank,

John Wilkie, the senior investigative reporter for the Wall Street Journal, published this cover story on Friday which is why he is so late in getting to Boston. He said he's coming up either late this week or late next week and that his next big cover story will be Madoff.

John's working on a drug scandal that likely gets into the WSJ next week but then he's going to work on Madoff. John's been covering the Lipitor scandal pretty heavily lately but he's just doing maintenance followups as that investigation continues.

Harry

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Friday, June 23, 2006 12:19 PM
To: 'Frank Casey'
Subject: RE: Ho Hum, Market always takes fraud in stride:

Frank,

If the SEC is this incompetent (which they are, believe me) and can't handle Pequot then they certainly can't handle Madoff. I'm sure the SEC will be in hot water with the US Senate, 2 committees were contacted by the SEC's lawyer - whistleblower, and are investigating. This will put immense pressure on the SEC to vigorously pursue Pequot, in order not to embarrass themselves further. Obviously the SEC under Chairman Cox is backsliding to the bad old days pre-William Donaldson.

Harry

-----Original Message-----
From: Frank Casey [mailto[redacted]
Sent: Friday, June 23, 2006 11:48 AM
To: Harry Markopolos
Subject: RE: Ho Hum, Market always takes fraud in stride:

Is your effort still on track or was it usurped by Pequot?

Frank R. Casey, Director of Marketing, Benchmark-Plus Management LLC

[redacted]

[redacted]

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Past Performance Is Not Necessarily Indicative of Future Results!

From: Harry Markopolos [mailto:harrymm@comcast.net]
Sent: Friday, June 23, 2006 9:11 AM
To: Frank Casey
Subject: RE: Ho Hum, Market always takes fraud in stride:

Frank,

You can't make this stuff up. It's an amazing story. I wonder who the hedge fund investors in Mr. Flottl's hedge fund were - they lost big-time. I hope Bennett looks good in a dress, because things would go a lot better for him behind bars if he does.

Great headline in today's NY Times about Pequot Capital front-running. I know of other funds that make their money by doing that but never suspected Pequot. The SEC may not wish to investigate due to political reasons, but that won't stop Elliott Spitzer. I'm sure Spitzer's office is cranking out a tidal wave of subpoenas as you read this, subpoenas that will likely be served before the close of business today. Leave it up to the SEC to screw up a large multi-billion hedge fund investigation, they're really good at screwing up.

Harry

-----Original Message-----
From: Frank Casey [mailt[redacted]
Sent: Thursday, June 22, 2006 10:37 AM
To:[redacted]
Subject: Ho Hum, Market always takes fraud in stride:

Refco Bank Hid $1 Billion Loss From Hedge Funds, Arafat Casino

June 22 (Bloomberg) -- At the Israeli army checkpoint on the edge of Jericho, gamblers from Jerusalem and Tel Aviv streamed into the West Bank town to wager on blackjack, play poker and face off with slot machines at the Palestinian-run Oasis Hotel Casino Resort. The casino was open 24 hours a day, seven days a week.

The party that started in September 1998 ended when a Palestinian uprising scared away customers in October 2000, forcing the casino to close within a month.

The Israeli shells that punched holes in the Oasis's stucco- and-black-glass facade also struck a financial blow to one of the casino's investors, Vienna-based Bawag PSK Bank -- the same bank that backed Refco Inc., the New York-based brokerage that collapsed last October after belatedly reporting $430 million in hidden losses.

The tale of Refco's bank -- and its role in the biggest meltdown on Wall Street since junk bond scandals felled Drexel Burnham Lambert Inc. in 1990 -- shows how executives gambled with customers' money and may have deceived the elite of the global financial community, including Goldman Sachs Group Inc., whose chief executive officer, Henry Paulson, is poised to become the next U.S. Treasury Secretary.

Charlotte, North Carolina-based Bank of America Corp., Zurich-based Credit Suisse Group and New York-based Goldman were managers of Refco's 2005 initial public offering. They're now defendants in a shareholder lawsuit against Refco.

Investors allege the banks didn't ensure all important facts about Refco were disclosed in offering papers. The firms haven't yet responded in court.

$14.9 Trillion in Trades

The Refco and Bawag coverups stretched from the Palestinian territories to the Caribbean. Bawag's dealings with Refco led to the demise of a brokerage that processed at least $14.9 trillion in trades for hedge funds and pension funds; Refco handled more derivatives contracts last year than the biggest U.S. options exchange.

For Refco's shareholders, bondholders and creditors, the cost of the deception may exceed several billion dollars. Bawag also jeopardized the deposits of 1.3 million school teachers, mechanics and other workers across Austria by funneling undisclosed loans to Refco and becoming entangled in Yasser Arafat's casino.

Since Refco's collapse, the disclosure of Bawag's dealings with the brokerage has triggered a wave of withdrawals from the bank. Austrian Chancellor Wolfgang Schuessel opened a savings account at Bawag in May in a show of support aimed at preventing a run on the bank.

Offshore Accounts

Refco's flameout can be traced to Bawag's use of offshore accounts to disguise its own failed investments while helping Refco conceal as much as $1 billion in trading losses, according to documents compiled by Austrian and U.S. investigators.

Bawag dumped uncollectible loans into the Refco brokerage account of a British Virgin Islands fund called Liquid Opportunities and then into companies based on the Caribbean island of Anguilla.

``Their risk appetite was very high, and their transparency was very low,'' Nicola Venedey, a senior analyst at Moody's Investors Service Inc. in London, says of Bawag.

Venedey says Bawag management's inability to provide checks and balances led Moody's to downgrade the bank's financial strength rating on May 31 to E+ -- meaning ``very modest'' strength, two notches above the lowest grade -- from C+, defined as ``adequate.''

`Bank Within the Bank'

The former top executives at Bawag, Austria's fourth-largest bank, ignored internal procedures when investing in and lending to both the casino and Refco, says Harald Raffay, who has been the head of Bawag's international department since 1996. He says his fellow bankers never informed him of those transactions.

``We're working like dogs, and then it turns out there's a bank within the bank,'' Raffay, 58, says.

In 1999, Bawag paid about $95 million for 10 percent of Refco, the biggest U.S. independent futures brokerage at the time, and then loaned it more than $1.6 billion over six years in so-called round-trip loans that Refco used to pad its accounts, according to a June 2 settlement agreement with U.S. prosecutors in New York.

After Refco booked its earnings for the year, it repaid Bawag.

``Decisions regarding Refco never crossed my desk, even though it was the most international business,'' Raffay says.

Bawag for Sale

Bawag's owner -- the Austrian Trade Union Federation, which consists of 13 groups, including metalworkers, agricultural workers, artists and sports teams -- has decided to get rid of the bank, founded by Socialist Chancellor Karl Renner in 1922 to provide financial services to workers. It has hired Morgan Stanley to find a buyer.

Bawag's hidden dealings also included an investment company founded by the late Palestinian leader Yasser Arafat, more than $1.3 billion in secret hedge fund losses and a tangle of Caribbean holdings, including phantom bonds Bawag used to disguise bad loans as an investment the bank valued at 350 million euros ($443 million).

These findings come from interviews and documents gathered in Anguilla, Austria, the Bahamas, France, Israel, Libya, Liechtenstein, Malta, the Palestinian territories and the U.S.

Even as Bawag tries to clean up its accounts for a planned sale of the bank, it's staking out new ventures on the fringes of the financial world.

Last year, it opened an office in Libya, the African nation led by Muammar Qaddafi that was considered a sponsor of terror by the U.S. State Department for 27 years, until May.

`I Knew Nothing'

Bawag's dealings with Arafat and Qaddafi are consistent with its history as a labor union bank allied with the Social Democrat Party, previously the Socialist party, whose one-time leader, former Austrian Chancellor Bruno Kreisky, forged relationships with both Arab officials.

In Vienna in 1979, Kreisky received Arafat, then the Palestine Liberation Organization chief, as a fellow head of state.

Raffay says Bawag's Libyan office is a proper and transparent business move by a bank that was lucky enough to get a license to operate in the country that holds Africa's largest crude oil reserves.

He contrasts the office in Libya with the bank's dealings with Refco and the casino transactions. ``I realized I was being cut out of

these deals, and now I'm happy," he says. ``I can go before a judge and say I knew nothing."
Bawag's Oasis investment became a 120 million-euro liability for the bank, according to Bawag CEO Ewald Nowotny, who was hired in January to clean up the mess.

Riding Shotgun

The casino, which accepted only U.S. dollars, had 124 gaming tables and 278 one-armed bandits. It raked in so much cash, according to casino financial reports, that guards, with Palestinian Authority security personnel riding shotgun, made daily trips in compact cars to Arab Bank Plc's downtown Jericho branch to deposit as much as $1 million at a time.
Because the casino was forced to close, Bawag's loss in that investment is about equal to its profit in 2004. The bank earned 113.3 million euros that year. Losses related to Refco and the casino chopped 2005 profit to just 6.3 million euros, the bank said in a statement on June 6.
The public unraveling of Bawag's casino investment, its trading losses and its secret dealings with Refco started on a single day last year, marking the beginning of a crisis that threatened the Austrian bank's existence and forced Refco into bankruptcy.

Loan to Bennett

The day was Oct. 10, when Refco went public with the news it had a hidden deficit. Bawag sold its stake that day in offshore Liquid Opportunities and the related Anguilla companies Bawag used to hide losses, according to evidence gathered by Austrian investigators. The buyer was Thomas Hackl, Bawag's former head of treasury and investment banking, three people close to the investigation say. Hackl, 41, left Bawag to work at Refco as head of global asset management from 2002 to 2004.
Just hours before Refco revealed its losses, Bawag loaned Refco CEO Phillip Bennett 350 million euros, according to Bawag, which sued Refco in November to get the money back. Bennett used the Bawag loan to pay debts to Refco that he'd been hiding for years, according to court filings in the U.S.
A U.S. grand jury indicted Bennett for fraud in November. He pleaded not guilty and is awaiting trial.
Bawag's relationship with Refco is now being picked apart in a series of civil and criminal probes in New York, Vienna and Washington. Bennett, ousted by Refco's board in October, is the only person criminally charged.

$683 Million Settlement

U.S. Attorney Michael Garcia in Manhattan accused Bennett, 57, of fraud after Refco disclosed he'd failed to inform investors of loans the company wasn't able to collect.
Others investigating Refco's collapse and Bawag's role in it include the U.S. Securities and Exchange Commission, Austria's Financial Market Authority and prosecutors in Vienna.
Bawag said on June 5 it would pay shareholders, creditors and regulators at least $683 million as part of a settlement with the Justice Department and the SEC. The agreement allows the bank to escape criminal charges in the U.S. Federal investigations of the individuals involved are continuing.
Bawag's role in helping Refco hide its debts was egregious in the eyes of U.S. law enforcement agencies because the bank was planning to profit by unloading its own stake in Refco, says Scott Friestad, the SEC official overseeing the agency's probe.

South of France Villa

``The bank's former executives understood that the deceptive year-end transactions would help Phillip Bennett and Bawag cash out their ownership interests at the expense of innocent investors," Friestad says.
Most of the suspect dealings happened under the management of Helmut Elsner, Bawag's CEO from 1995 to 2003, who got his start in Bawag's branch in Graz, Austria, and whose wife owns a penthouse constructed on the roof of the bank's headquarters in Vienna, investigators say.
Elsner, 72, today spends his time on France's Cote d'Azur, where he drives a red Ferrari and lives in a villa in the hills outside Cannes. He entertains guests at the nearby restaurant Le Moulin de Mougins, which has been awarded two stars by the Michelin Guide. His lunches typically include mature Bordeaux at about 500 euros a bottle, according to a restaurant staff member who asked not to be named because Elsner is a regular customer.
Reached by telephone inside his gated hillside enclave in May, Elsner declined to be interviewed. ``Contact my lawyer in Vienna," he said.

`Shot at Dawn'

His attorney, Wolfgang Schubert, says that Bawag's transactions were legal and approved by the bank's auditors and the board.
Under Elsner's leadership, Bawag devised a coverup with Bennett, a Briton who studied geography at the University of Cambridge, for their mutual losses, according to the June 2 settlement.
The plaintiffs include Newport Beach, California-based Pacific Investment Management Co., the manager of the world's biggest bond fund, which bought Refco securities with a face value of $82.7 million from August 2004 to October 2005.
Raffay blames the arrogance of Elsner for the bad investments and coverups. ``You speak against him and you were shot at dawn," he says.
Otto Karasek, the managing director of Bawag Malta Bank, a subsidiary based in the Mediterranean island nation, also points the finger at his former boss. ``A lot had to do with the culture of the time and the CEO, Elsner," Karasek says. ``You didn't dare speak against him."

Coverup

In April 2003, Elsner retired as CEO after 48 years at the bank. Johann Zwettler, 64, a member of the bank's board, replaced him.
After Bawag lost about 350 million euros on hedge fund trades in 2000, it enlisted Refco's help to cover them up, according to the June 2 settlement agreement. Unlike traditional institutional investors, many hedge funds have the freedom to bet on virtually anything regardless of risk in pursuit of exceptional returns.
Bawag moved its failed investments off the bank's balance sheet and into offshore companies run through accounts at Refco, Nowotny says.
Bawag also helped Refco hide losses by lending the brokerage hundreds of millions of dollars at the end of fiscal years 2000 to 2005, according to an SEC news release issued on June 5.

`Sham Transactions'

Bennett concealed as much as $970 million in debt and reported healthy finances, according to the shareholder lawsuit.
``The informal structure of these sham transactions clearly reflected their real purpose: to conceal Refco's true financial condition and Bawag's losses from the past trading failures," the lawsuit says. ``Indeed, Bawag had to participate in these transactions because, if the Refco Holdings receivable came to light, Bawag's own trading losses would likely also be revealed."
Bennett owned Refco Group Holdings Inc., known as Refco Holdings. Bawag settled that suit as part of the June 2 agreement with U.S. regulators, without admitting or denying the allegations.
The cycle of hedge fund investments, trading losses and coverups that would lead to Refco's collapse and Bawag's putting itself up for sale began in the early 1990s under Bawag's then CEO, Walter Flottl. He'd run the bank since 1972.

$2 Billion to Son

Flottl, 82, used bank funds to support his son Wolfgang's fledgling Bermuda-based hedge fund, people close to Bawag say.
The younger Flottl, 55, a graduate of Harvard Business School who was then in his early 30s, used the funds to bet, through Refco, on U.S. bonds, takeovers and the movement of currencies.
Austria's banking regulator at the time, the Austrian National Bank, announced an investigation in 1994 following press reports of money transfers to Wolfgang Flottl. It found that Walter Flottl had never informed Bawag's supervisory board about the $2 billion in investments with his son's firm, people close to the investigation say.
The probe, whose results were never publicly disclosed, didn't find anything illegal, Bawag said in a statement the following year. Wolfgang Flottl said in an October interview he returned all of Bawag's money plus a profit. He's married to Anne Eisenhower, the granddaughter of former U.S. President Dwight Eisenhower.

Risky Ventures

Following the probe, Walter Flottl retired in 1995, handing the bank's leadership to Elsner. The new CEO expanded Bawag's

relationship with Refco and started other risky ventures.
Elsner found such an investment in the Palestinian territories. Arafat, as president of the Palestinian Authority, was on the hunt for ways to develop the local economy after the 1993 Oslo Accord created the framework for Palestinian autonomy in the West Bank and Gaza, former Finance Minister Salam Fayyad says.
Austrian investor Martin Schlaff helped bring Bawag together with Arafat's advisers to build a casino in Jericho, according to Palestinian Authority records that list Schlaff as a board member and officer of the casino.
Schlaff was one of Bawag's biggest customers. Schlaff declined to answer written questions submitted to Michael Fink, his spokesman in Vienna.
On Dec. 17, 1996, Palestine Commercial Services Co., an investment company controlled by Arafat, signed an agreement with a group of Austrian investors, including Bawag, according to a report on the investment's history and financial value commissioned by the Palestinian Authority.
Oasis
The casino would be owned by CAP Holding AG, a Liechtenstein- based company whose shareholders were Bawag, with 11 percent; Vienna-based Casinos Austria International, with 16.5 percent; Palestine Commercial Services, with 23.1 percent; and a company called MS Privatstiftung -- controlled by Schlaff -- with 49.5 percent, according to Palestinian Authority and Casinos Austria documents.
Casinos Austria ran the Oasis, along with 62 other casinos in 17 countries and nine gambling ships.
On Sept. 13, 1998, the Oasis opened; its staff grew to about 2,000 by June 2000, when the InterContinental Hotel opened adjacent to the casino. The resort has 181 rooms, 14 suites and three swimming pools on lush grounds surrounded by desert with views of the hills across the border in Jordan.
In its first full year, 1999, the Oasis took in $152.9 million in gaming revenue and turned a profit of $60 million, according to an assessment of the investment by Standard & Poor's for the Palestinian Authority.
Bennett and Elsner
Richard Lehrner, the casino's head of finance and administration at the time, declined to comment.
At the same time Bawag was working with Arafat, the Austrian bank established its first formal links with Refco. Eighteen days after the casino opened, Refco promoted Bennett, then its chief financial officer, to CEO.
The next week, Bennett and Elsner announced they were setting up a joint venture to provide clearing services for futures and options traded on European exchanges. Bawag was able to handle trades for some of Refco's customers, including 20,000 financial institutions, and Refco aimed to profit from widening its client base in Europe.
Wolfgang Flottl was also back in the bank's good graces, and in 1995, Elsner began lending him hundreds of millions of the bank's money to invest, Nowotny says.
Flottl's losses trading Bawag's money would total at least 1 billion euros, Nowotny says.
Asian Crisis
By the late 1990s, Refco also faced hundreds of millions of dollars in losses from customers crippled by the Asian currency crisis that exploded in 1997, according to U.S. prosecutors. It turned to Bawag for fresh financial support. That's when Bawag paid about $95 million for its stake in Refco.
``This significant infusion of capital complements a number of important recent management changes at Refco and positions us well to achieve our strategic goals," Bennett said in an announcement six days later.
What he and Elsner never announced was that, behind the scenes, Refco and Bawag had started working together to make Refco's bad debts disappear before the end of the fiscal year, the June nonprosecution agreement says.
Bennett, faced with unpaid debts from clients, had taken the customers' obligations and moved them to a company he owned called Refco Group Holdings, the SEC's settlement with Bawag shows.
Round-Trip Loans
A firm owned by the CEO owing money to Refco would raise suspicion and possibly trigger a requirement under U.S. securities law to disclose debts to so-called related parties. Bennett needed to give the appearance that an outside company owed the money to Refco, the SEC says.
On Feb. 24, 2000, Bawag and Refco made the first of six annual round-trip loans, according to e-mails contained in the shareholder lawsuit. Bawag wired $300 million to Bennett's holding company, which Bennett then used to temporarily pay a portion of his holding company's debts to Refco.
At the same time, Refco wired $300 million to Bawag, according to Bawag's June 2 nonprosecution agreement with the U.S. attorney. The effect was to make it appear that Refco had money on deposit at Bawag, rather than the truth -- that the firm's CEO owed money to Refco, SEC court filings show. On March 2, after the fiscal year had passed, they reversed the transfers.
Seven months later, on Sept. 28, violence erupted in Jerusalem as Ariel Sharon, then head of Israel's opposition Likud Party, visited the plaza that contains al-Aqsa Mosque, the third- holiest site in Islam, and the Western Wall, the most sacred location in Judaism.
Casino Closed
An uprising spread throughout the West Bank and Gaza, and in the following month, the casino closed. The hotel stayed open, with managers herding guests, including women and children, into the basement for hours at a time during gun battles.
Israeli shells punched holes the size of basketballs in the hotel's side, which has since been repaired with plaster and paint.
With no customers at the gaming tables, the value of the casino plummeted. Still, Bawag engineered a transaction that -- for accounting purposes anyway -- transformed a stricken investment into one worth 120 million euros, Bawag's nonprosecution agreement says.
This accounting alchemy was accommodated by the Liquid Opportunities fund. First, Bawag shifted its casino holding to a Refco account administered by Liquid Opportunities, the nonprosecution agreement says.
Liquid Opportunities
Then, following the transfer, Liquid Opportunities updated its records to reflect an increase of 120 million euros in the value of Bawag's Refco account, the agreement says.
At the time, 120 million euros was the equivalent of $108 million -- eight times what the stake was actually worth, according to S&P's assessment.
Oasis Hotel Casino Resort had a fair market price of $120 million, S&P found. That would value Bawag's stake at about $13.2 million. Nowotny says the 120 million-euro figure includes the casino investment and unrelated liabilities.
By the end of 2000, Bawag also used Liquid Opportunities and offshore accounts at Refco to cover up the bank's hedge fund losses. That year, Bawag made its final loan to Wolfgang Flottl: this time, 350 million euros, according to the nonprosecution agreement. Flottl wagered that the yen would rise, Nowotny says. In the last quarter of 2000, the yen fell 9.1 percent versus a basket of currencies in eight straight weeks of declines, its longest continuous drop in half a decade. Flottl told the bank that he had lost almost all of the money.
Secret Deal
With Bawag's hedge fund failures totaling more than 1 billion euros by December 2000, Elsner made a secret deal with the trade unions, Nowotny says. The unions agreed to guarantee Bawag's debts, allowing it to repay the money.
Elsner and Bennett might have succeeded in hiding their losses if Refco hadn't begun preparing in 2004 for an eventual public offering of its stock.
Bennett started the process by arranging the sale of Bawag's 10 percent stake in Refco to investor Thomas Lee in a leveraged buyout. As part of the deal, Bennett also paid back loans to Bawag, bringing the total payout to Bawag to at least $952 million.
Refco raised the money by selling bonds -- debt that would later be passed on to buyers of $583 million in Refco shares when Lee and Bennett took the company public in August 2005.
Endgame
The endgame for Refco began on Oct. 6, 2005, when Bennett asked Bawag to lend 350 million euros to his company, Refco Group

Holdings, according to Bawag's lawsuit against Refco.
Hackl, the Bawag banker who'd moved to Refco, helped a Refco employee contact Bawag to arrange the loan, Hackl said in an Oct. 26 interview.
On Oct. 10, Bawag agreed to lend Bennett the money. That same day, Hackl bought Bawag's stake in Liquid Opportunities and the Anguilla companies the bank had used to hide its hedge fund losses, three people with knowledge of the Austrian investigation say. Hackl then sold the holdings back to Liechtenstein-based foundations controlled by Bawag, the people say.
The loan was wired into an account at Refco Capital Markets Ltd., a Bermuda subsidiary, at 6 a.m. New York time on Monday, Oct. 10. Less than two hours later, Refco announced that Bennett had hidden losses.
Customers fled, and the brokerage filed for bankruptcy protection in November. Bawag sued Refco for fraud on Nov. 16, and, the next day, CEO Zwettler resigned.
Forgiveness of Debt
The new management under Nowotny negotiated settlements with Refco's shareholders and regulators in the U.S. in order to reassure customers in Austria and stem the tide of withdrawals.
It disclosed the secret shift of Bawag's hedge fund losses and, on June 6, said it had written down the casino investment as a loss against its 2005 earnings.
On June 16, the bank said the trade unions had covered the full 120 million euros.
With the casino closed in Jericho, one of the remaining tourist attractions is a testament to such forgiveness of debt: a sycamore tree on the road that links the casino and the downtown Arab Bank branch.
By local tradition, the town's chief tax collector, Zacchaeus, climbed this tree some 2,000 years ago for a better view of Jesus, who was coming through Jericho. Jesus ordered the tax collector down from the tree, winning a spontaneous pledge, according to the Bible's Book of Luke.
``If I have cheated anybody out of anything, I will pay back four times the amount,'' Jericho's tax man said.
At Bawag and Refco, exacting that kind of justice may also take divine intervention.

To contact the reporters on this story:
Vernon Silver in Rome at vtsilver@bloomberg.net
Otis Bilodeau in Washington at obilodeau@bloomberg.net
Last Updated: June 21, 2006 20:33 EDT

Frank R. Casey, Director of Marketing
Benchmark-Plus Management LLC

[redacted]

[redacted]

Benchmark Plus is a <u>hedged</u>, fund-of-hedge-funds producing market-neutral, zero-beta absolute returns. We isolate each sub-manager's alpha by removing the portion of return that is due to market influences (beta). **<u>Past Performance Is Not Necessarily Indicative of Future Results!</u>**

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Thursday, June 29, 2006 7:36 PM
To: Frank Casey [redacted]
Cc: Neil Chelo [redacted]
Subject: 06292006 WSJ US Charges BP with Price Fixing.doc

Frank, Neil

John Wilkie is the reporter I'm working with on the Madoff Story. He also did front page exposes on Mario Gabelli, a crooked Congressman from W.VA., and the American Red Cross this year.

Harry

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Monday, August 28, 2006 3:04 PM
To: 'Frank Casey'
Subject: RE: Bernie dodged transparency again?

Frank,

1. I am meeting with the WSJ in 2 weeks. After I asked, "what's happening, If you guys don't want it, Ben Stein over at Barron's said he'd take it." At that, I got an immediate response that the journal wants it and a meeting date was quickly set up.

2. The SEC is useless when it comes to derivatives frauds and hedge funds. An SEC staff attorney can barely count to 21, and then only if they're male and smart enough to pull down their pants to find the extra digit.

Harry

> -----Original Message-----
> **From:** Frank Casey [mailto[redacted]
> **Sent:** Monday, August 28, 2006 11:22 AM
> **To**[redacted]
> **Subject:** Bernie dodged transparency again?
>
> At least the SEC is consistent!....ignoring your 3rd cry (of wolf?)
>
> WSJ article dead also?
>
> Frank R. Casey, Director of Marketing
> Benchmark-Plus Management LLC
>
> [redacted]
>
> [redacted]
>
> Benchmark Plus is a <u>hedged</u>, fund-of-hedge-funds producing market-neutral, zero-beta absolute returns. We isolate each sub-manager's alpha by removing the portion of return that is due to market influences (beta). **<u>Past Performance Is Not Necessarily Indicative of Future Results!</u>**

Harry Markopolos

From: Harry Markopolos [harrymm@comcast.net]
Sent: Friday, September 22, 2006 2:39 PM
To: 'Frank Casey'
Cc: 'Neil Chelo'; 'Scott Franzblau'; 'Robert Ferguson'
Subject: RE: What about a HFOF owning BD Equity ala Berinie?

I know [redacted] each headed up the SEC's Boston Office. They talked tough but fail to follow thru [redacted]. They stopped at Putnam, MFS, Columbia /BankAmerica, and Evergreen, leaving all of the others alone despite seeing first-hand evidence of market-timing [redacted] So, I wouldn't put much stock in the SEC regulating hedge funds via the backdoor B/D end.

Madoff - if the SEC hasn't caught him by now, they never will until he blows up. The SEC's problem is that they have too many lawyers and not enough auditors with industry experience who know finance and can easily spot when the numbers don't add up or are too good to be true. For example, on page [redacted] is a full page color add by [redacted] with 3 sets of performance numbers for 3 funds that seem way too good to be true. My bet is that [redacted], which means [redacted] is running a Ponzi Scheme. I called a buddy at the Boston SEC and told him that if he knows anyone in the [redacted] Office, that they should get an audit team over to [redacted] straight away.

P.S. [redacted] had a HFOF with an 8% allocation to Amaranth which apparently is now a 3% allocation. Amaranth told the HFOF that they were multi-strategy and that they had world class risk controls when in fact they had neither.

Harry

-----Original Message-----
From: Frank Casey [mailto [redacted]
Sent: Friday, September 22, 2006 10:05 AM
To: Harry Markopolos
Cc: Neil Chelo; Scott Franzblau; Robert Ferguson
Subject: What about a HFOF owning BD Equity ala Berinie?
Importance: High

22.09.2006 SEC examines hedge funds running trades through own brokerage

From the FT/MSN.com: The Securities and Exchange Commission is tightening scrutiny of hedge funds by stepping up examination of the links between hedge funds and broker-dealers, particularly where they are owned by a hedge fund, a senior SEC official said. The move is a sign that the SEC continues to find ways to regulate hedge funds after a US court federal court in June overturned an SEC rule forcing hedge fund advisers to register with the agency.

Walter Ricciardi, deputy director of enforcement, said: "I think some of the problems we've seen with hedge funds, one of the risk factors, red flags, is where they have their own broker-dealer. "That creates quite a conflict in the sense that investors' money is sitting there and a hedge fund decides to trade through their own broker-dealer and [the hedge fund] get a fee for such trading. "It gives them an incentive to run up trading fees....Full article:

Article source: http://msnbc.msn.com/id/14944454/ - Opalesque is not responsible for the content of external internet sites

Frank R. Casey, Director of Marketing
Benchmark-Plus Management LLC

[redacted]

[redacted]

Benchmark Plus is a hedged, fund-of-hedge-funds producing market-neutral, zero-beta absolute returns. We isolate each sub-manager's alpha by removing the portion of return that is due to market influences (beta). **Past Performance Is Not Necessarily Indicative of Future Results!**

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Tuesday, September 26, 2006 9:46 AM
To: 'Frank Casey'
Subject: RE: Amaranth - the news is only going to get worse

He's got until the end of the week to call me and let me know,

Harry

-----Original Message-----
From: Frank Casey [mailto:fcasey@bpfunds.com]
Sent: Tuesday, September 26, 2006 9:38 AM
To: Harry Markopolos
Subject: RE: Amaranth - the news is only going to get worse

Agreed, thanks.

Did WSJ make a decision re Bernie?

Frank R. Casey, Director of Marketing, Benchmark-Plus Management LLC

[redacted]

Benchmark Plus is a hedged, fund-of-hedge-funds producing market-neutral, zero-beta absolute returns. **Past Performance Is Not Necessarily Indicative of Future Results!**

From: Harry Markopolos [mailto:[redacted]
Sent: Tuesday, September 26, 2006 10:31 AM
To: Frank Casey
Subject: Amaranth - the news is only going to get worse

Frank,

I've heard that a Mass pension plan had heavy exposure to Amaranth but the person wasn't telling which one. My guess is that it's either Mass Prim or Middlesex Country. If so, that'll put this story on the front page of the Globe and Herald.

The news on Amaranth keeps getting worse. Fortunately, it should help the FOFs market against the multi-strategy funds and be good for benchmark. Talk about all your eggs in one basket with a multi-strategy fund with no risk controls despite what the manager was saying and few insitutional investors will risk their careers by investing in a multi-strategy fund. That and your well thought analysis that it is doubtful a multi-strategy manager has alpha in more than 1, perhaps 2 strategies, therefore why not go the FOF route where they pick the best of breed.

Amaranth is merely a warning tremor telling smart folks that the "Big One" is coming.

Harry

Per a call with Matt Moran, Marketing VP, for the Chicago Board Options Exchange. 9/29/2006 3:58 PM
Categories: **Case 16 Madoff**

Per a call with Matt Moran, Marketing VP, for the Chicago Board Options Exchange. Several OEX pit traders are upset and think Bernie Madoff is a fraud but no way can he cooperate with a Wall Street Journal reporter. The request for cooperation would have to go thru CBOE's marketing channels, specifically Lynn Howard who can be reached at [redacted]. Matt would appreciate it if the WSJ would point out that Bernie uses OTC options and that OTC is where the derivatives frauds occur - Exchange Traded Derivatives are closely regulated and safe unlike OTC Derivatives which are unregulated and unsafe.

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Friday, September 29, 2006 4:20 PM
To: John Wilke[redacted]@wsj[redacted]
Subject: 2 initial points of contact for the Bernie Madoff Story

John,

Here are two points of contact to get the Bernie Madoff Story off and running:

1. Leon Gross, head of global equity derivatives research, Citigroup at [redacted]

A. Leon told me point-blank last summer when I visited his office that Bernie is a fraud and there's no way his purported stock & options strategy can possibly beat Treasury Bill returns. He also couldn't believe the guy hasn't been exposed yet and wonders what kind of idiots would invest in such an obvious scam.
B. Your approach should be, "I'm John Wilkie, I want to know about Bernie Madoff but realize your identity would have to remain secret for you to be able to comment. I'd like to hear what you think of his stock and options strategy and know if you or your traders have ever seen Madoff's derivatives volume hit the tape."

2. Lynn Howard, Public Relations Head, Chicago Board Options Exchange (CBOE), [redacted]

A. Matt Moran, VP of Marketing, who is also a lawyer by training, told me that the traders in the index option pits "know of" Bernie Madoff by reputation and think he's an obvious fraud. However, Matt doesn't want to comment to the WSJ but says that if you went to Chicago and visited the pit traders you'd get an earful about Bernie. Matt said Bernie is the biggest options trader the CBOE never met and never saw any trades from.
B. Matt said he'd have to follow official channels and if the WSJ wants to do a story, call Lynn Howard and get an appoitnment to vist the index option pits from her.
C. The CBOE would be more inclined to assist the WSJ if you would assure them that exchange listed derivatives which are SEC regulated are not the derivatives used by the fraudsters. Fraudsters always use Over-the-Counter derivatives (LTCM, Amaranth, Nick Leeson of Barings Bank, Orange County, etc...) which are unregulated and akin to the Wild West. None of the blowups or scandals have occured using exchange listed, regulated derivatives because the margining and oversight are so tight. Say that to them and they'll likely cooperate. The CBOE is sick and tired of the world thinking that derivatives are bad - they'd like the world to know that unregulated OTC derivatives need to be regulated and that they are the cause of financial meltdowns and scandals.
D. Your goal should be to get onto the trading floor and hear what the index option traders in the OEX (S&P 100) and SPX (S&P 500) options pits have to say about Bernie's purported strategy and trading volumes.

3. I'm trying to get a Managing Director at Merrill Lynch Alternatives Investments Group (hedge funds) to talk to you but that better wait until I speak to him first.

Good luck,

Harry

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Friday, September 29, 2006 4:21 PM
To: Frank Casey [redacted]
Cc: Neil Chelo [redacted]
Subject: FW: 2 initial points of contact for the Bernie Madoff Story

Frank, Neil

This is what I sent to the WSJ today.

Harry
-----Original Message-----
From: Harry Markopolos [mailto[redacted]
Sent: Friday, September 29, 2006 4:20 PM
To: John Wilk[redacted]
Subject: 2 initial points of contact for the Bernie Madoff Story

John,

Here are two points of contact to get the Bernie Madoff Story off and running:

1. Leon Gross, head of global equity derivatives research, Citigroup at [redacted]

A. Leon told me point-blank last summer when I visited his office that Bernie is a fraud and there's no way his purported stock & options strategy can possibly beat Treasury Bill returns. He also couldn't believe the guy hasn't been exposed yet and wonders what kind of idiots would invest in such an obvious scam.
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2. Lynn Howard, Public Relations Head, Chicago Board Options Exchange (CBOE), [redacted]

A. Matt Moran, VP of Marketing, who is also a lawyer by training, told me that the traders in the index option pits "know of" Bernie Madoff by reputation and think he's an obvious fraud. However, Matt doesn't want to comment to the WSJ but says that if you went to Chicago and visited the pit traders you'd get an earful about Bernie. Matt said Bernie is the biggest options trader the CBOE never met and never saw any trades from.
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D. Your goal should be to get onto the trading floor and hear what the index option traders in the OEX (S&P 100) and SPX (S&P 500) options pits have to say about Bernie's purported strategy and trading volumes.

3. I'm trying to get a Managing Director at Merrill Lynch Alternatives Investments Group (hedge funds) to talk to you but that better wait until I speak to him first.

Good luck,

Harry

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Monday, November 20, 2006 4:23 PM
To: 'Frank Casey'
Cc: Neil Chelo [redacted]
Subject: UUpdate on Bernie Madoff

Frank, Neil

Because the reporter, John Wilke, did all of those front-page WSJ articles on Congressional corruption, he wasn't able to get to Madoff. The 3 Congressmen (2 Repubicans & 1 Democrat) he exposed are all being investigated by the FBI. He and I just talked on a different front-page story he's doing in December that I gave him. John told me that his editor has read my Madoff analysis and is very, very excited to start their investigation in January. John also knocked off former FBI director William Webster, on the front page of the WSJ, after President Bush nominated him to become head of the Public Accounting Oversight Board so he's a real force in expose journalism. Mr. Webster withdrew from consideration right after the WSJ story ran.

He said that his editor thinks that hedge fund scrutiny will increase now that the Democrats are in power and greenlighted John's investigation starting in January.

I guess we wait and see what transpires, I'll keep you posted, this guy does top shelf corruption stories, but everything he investigates is on a schedule.

Wishing you the best of Thanksgiving Holidays, stop by and visit if you're in town,

Harry

-----Original Message-----
From: Frank Casey [mailto:[redacted]
Sent: Monday, November 20, 2006 12:21 PM
To: [redacted]
Subject: Bernie article a dead issue?

Frank R. Casey, Director of Marketing, Benchmark Plus Management LLC

[redacted]

Benchmark Plus is a hedged, fund-of-hedge-funds targeting market-neutral, zero-beta absolute returns.
Past Performance Is Not Necessarily Indicative of Future Results!

2007 Madoff Case Activity Cover Letter

Date of Analysis: 12/28/2008

I've organized this particularly busy year into two parts:

<u>Part One</u> consists of my June 29, 2007 Submission to the SEC's New York Office.

<u>Part Two</u> is a chronological listing of e-mails, performance numbers, financial statements, an analysis of an actual Madoff portfolio, and other evidence gathering by Frank Case, Neil Chelo, Michael Ocrant and myself.

1. I am currently planning on only submitting Part One, my June 29, 2007 SEC Submission to Congress.

2. I would like a legal review of the case documents [redacted] to determine if they should be released to Congress, to the SEC's Inspector General, to US law enforcement, to foreign law enforcement, to victim's, to the plaintiff's bar, to the defendant's bar, and to the public.

Thank you,

Harry Markopolos

Harry Markopolos, CFA, CFE
Chartered Financial Analyst
Certified Fraud Examiner

June 2007 SEC Submission to the SEC

Date: 12/15/2008

Documents included in this PDF File:

1. June 29, 2007 e-mail cover letter to Meaghan Cheung, SEC Branch Chief, New York Office alerting her to the fact that there exist hedge fund of funds that lever themselves up at a 3:1 and 3.25:1 ratio. I copied Ed Manion, CFA of the Boston SEC Office on this as Ed helped me every step of the way from May 2000 onwards in trying to get the SEC to act. If it had not been for Ed's continued support and encouragement I definitely would have quit after my first meeting with the SEC back in May 2000. Ed's the one who kept me coming back. I fear the SEC will seek to punish Ed and cover up for the many SEC staffers who were negligent since that's seems to be the way this captive agency operates.
2. Fairfield Greenwhich Group, April 2007, updated performance figures.
3. A one-page, Wickford Fund LP historic Pro-Forma prior to April 1, 2007 Fund Launch showing a back-tested set of "theoretically achievable" returns if they had gone backwards in time using 3.1:1 leverage and invested in Bernie Madoff. This Pro-Forma purports to account for the cost of financing costs and, of course, Wickford Fund's asset management fees.
4. An eight-page marketing pitch-book for Wickford Fund LP offering leverage exposure to Madoff at 3:1 and 3.25 leverage ratios.

My comments:

1. Mathematically, if impossible returns are impossible by definition, then using 3 to 1 leverage is the same as multiplying impossible by 3. Unfortunately we now know that Madoff's net return to investors is likely to be zero, so Wickford Fund's investors returns are three times zero, in other words still zero.
2. That the SEC still sat on its hands and didn't at least call the SEC's San Francisco office and have them visit Prospect Capital 's (the offerer of this levered security) offices in San Francisco is beyond belief. Fairfield Greenwich Group was located within a 45-minute drive of the SEC's New York office and they should have paid them a visit as well.
3. It would be interesting to see if any of the off-shore fund's investors were American citizens with hidden investment accounts that they are not paying taxes for. It might be difficult for these folks to claim tax losses domestically.

Harry Markopolos

Harry Markopolos, CFA
Chartered Financial Analyst
Certified Fraud Examiner

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Friday, June 29, 2007 3:58 PM
To: Meaghan Cheung [redacted]
Cc: CFA Ed Manion ([redacted]
Subject: Fraud Update on Bernie Madoff

Hello Meaghan,

1. Attached are some very troubling documents that show the Madoff fraud scheme is gettng even more brazen.

2. Wickford is showing a monthly estimated pro forma set of returns of an investment in Madoff that is leveraged by a factor of 3.0 to 3.25 times and earns annual returns ranging between a low of 11.75% (2005) to a hihg of 33.42% (1997).

3. Madoff couldn't possibly be managing the billions in this strategy unlevered, much less levered. I thought you would want to see these Wickford documents.

4. When Madoff finally does blow up, it's going to be spectacular, and lead to massive selling by hedge fund, fund of funds as they face investor redemptions.

Regards,

Harry Markopolos, CFA
Financial Fraud Investigator
[redacted]

CC: Ed Manion, CFA
Boston SEC Office

Fairfield Greenwich Group

Fairfield Sentry Ltd.

April 2007

STRATEGY DESCRIPTION

The Fund seeks to obtain capital appreciation of its assets principally through the utilization of a nontraditional options trading strategy described as "split strike conversion", to which the Fund allocates the predominant portion of its assets. The investment strategy has defined risk and reward parameters. The establishment of a typical position entails (i) the purchase of a group or basket of equity securities that are intended to highly correlate to the S&P 100 Index, (ii) the purchase of out-of-the-money S&P 100 Index put options with a notional value that approximately equals the market value of the basket of equity securities and (iii) the sale of out-of-the-money S&P 100 Index call options with a notional value that approximately equals the market value of the basket of equity securities. The basket typically consists of between 40 to 50 stocks in the S&P 100 Index. The primary purpose of the long put options is to limit the market risk of the stock basket at the strike price of the long puts. The primary purpose of the short call options is to largely finance the cost of the put hedge and to increase the stand-still rate of return. The "split strike conversion" strategy is implemented by Bernard L. Madoff Investment Securities LLC ("BLM"), a broker-dealer registered with the Securities and Exchange Commission, through accounts maintained by the Fund at that firm. The services of BLM and its personnel are essential to the continued operation of the Fund, and its profitability, if any. The Investment Manager, in its sole and exclusive discretion, may allocate a portion of the Fund's assets (never to exceed, in the aggregate, 5% of the Fund's Net Asset Value, measured at the time of investment) to alternative investment opportunities other than its "split strike conversion" investments.

HIGHLIGHTS

- Sixteen year track record
- Only 14 down months since inception
- Provides long term capital appreciation by delivering short-term gains
- Excellent risk adjusted return
- Market timing strategy
- Highly hedged portfolio

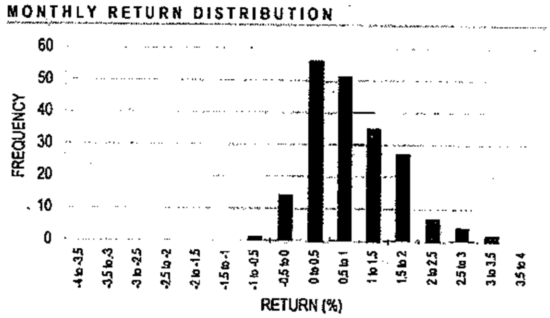
FUND PERFORMANCE

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2007	0.29%	-0.11%	1.64%	0.98%									2.81%
2006	0.70%	0.20%	1.31%	0.94%	0.70%	0.51%	1.06%	0.77%	0.68%	0.42%	0.86%	0.86%	9.38%
2005	0.51%	0.37%	0.85%	0.14%	0.63%	0.46%	0.13%	0.16%	0.89%	1.61%	0.75%	0.54%	7.26%
2004	0.88%	0.44%	-0.01%	0.37%	0.59%	1.21%	0.02%	1.26%	0.46%	0.03%	0.79%	0.24%	6.44%
2003	-0.35%	-0.05%	1.85%	0.03%	0.90%	0.93%	1.37%	0.16%	0.86%	1.26%	-0.14%	0.25%	7.27%
2002	-0.04%	0.53%	0.39%	1.09%	2.05%	0.19%	3.29%	-0.14%	0.06%	0.66%	0.10%	0.00%	8.43%
2001	2.14%	0.08%	1.07%	1.26%	0.26%	0.17%	0.38%	0.94%	0.66%	1.22%	1.14%	0.12%	9.82%
2000	2.14%	0.13%	1.77%	0.27%	1.30%	0.73%	0.58%	1.26%	0.18%	0.86%	0.62%	0.36%	10.67%
1999	1.99%	0.11%	2.22%	0.29%	1.45%	1.70%	0.36%	0.87%	0.66%	1.05%	1.54%	0.32%	13.29%
1998	0.85%	1.23%	1.68%	0.36%	1.69%	1.22%	0.76%	0.21%	0.98%	1.86%	0.78%	0.26%	12.52%
1997	2.38%	0.67%	0.80%	1.10%	0.57%	1.28%	0.68%	0.28%	2.32%	0.49%	1.49%	0.36%	13.10%
1996	1.42%	0.66%	1.16%	0.57%	1.34%	0.15%	1.86%	0.20%	1.16%	1.03%	1.51%	0.41%	12.08%
1995	0.85%	0.69%	0.78%	1.62%	1.65%	0.43%	1.02%	-0.24%	1.63%	1.53%	0.44%	1.03%	12.04%
1994	2.11%	-0.44%	1.45%	1.75%	0.44%	0.23%	1.71%	0.35%	0.75%	1.81%	-0.64%	0.60%	10.57%
1993	-0.09%	1.86%	1.79%	-0.01%	1.65%	0.79%	0.02%	1.71%	0.28%	1.71%	0.19%	0.39%	10.75%
1992	0.42%	2.72%	0.94%	2.79%	-0.27%	1.22%	-0.09%	0.86%	0.33%	1.33%	1.36%	1.36%	13.72%
1991	3.01%	1.40%	0.52%	1.32%	1.82%	0.30%	1.98%	1.00%	0.73%	2.75%	0.01%	1.56%	17.64%
1990												2.77%	2.77%

ANALYTICS

	Fund	S&P 100	Lehman Agg.
Compound Annual Returns	10.98%	11.33%	7.12%
YTD Compound Returns	2.81%	3.74%	2.05%
Annual Standard Deviation	2.51%	14.20%	3.74%
Correlation	N/A	0.32	0.07
Sharpe Ratio	2.78	0.52	0.84
Worst Drawdown	-0.64%	-49.37%	-5.15%
Months To Recover	2	N/A	8
Percentage Up Months	92.39%	63.45%	71.07%
NAV	$ 1,237.11		
Fund Assets	$ 6.6 Billion		

MONTHLY RETURN DISTRIBUTION



Fairfield Greenwich Group

Fairfield Sentry, Ltd.

TERMS AND CONDITIONS

Investment Manager:	Fairfield Greenwich (Bermuda) Ltd.	**Published:**	Irish Stock Exchange/International Herald Tribune
Fees:	Management: 1 % Performance: 20 %	**ISIN:**	VGG3299L1004
Minimum Investment:	$ 100,000	**Administrator:**	Citco Fund Services (Europe) B.V.
Subscriptions:	Monthly	**Custodian:**	Citco Global Custody NV
Redemptions:	Monthly, with 15 calendar days notice		

FAIRFIELD GREENWICH GROUP

Founded in 1983, Fairfield Greenwich Group's ("FGG"), mission is to offer its clients superior alternative asset management funds and related products. Throughout its history, FGG has internally managed its own hedge funds and selectively identified external managers for strategic affiliations. For risk monitoring purposes, FGG obtains portfolio transparency from all managers which are included in its multi-strategy funds. We seek to align our interests more fully with those of our clients by investing a significant portion of our own shareholders' capital with our managers. FGG has approximately USD $13.5 billion in client and firm assets under management. It is an employee owned firm with over 100 employees, 16 of whom are shareholders, and has offices in New York, London, and Bermuda, and representative offices in the U.S., Europe, and Latin America. FGG-related funds have over 900 registered shareholders, including private banks, financial advisors, family offices, pension funds, government authorities, and institutional investors. FGG entities are registered with the U.S. SEC as an investment advisor and broker dealer, and with the U.K. Financial Services Authority as an Investment Manager.

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The Lehman Brothers Aggregate Bond Index is a benchmark index made up of the Lehman Brothers Government/Corporate Bond Index, Mortgage-Backed Securities Index, and Asset-Backed Securities Index, including securities that are of investment-grade quality or better, have at least one year to maturity, and have an outstanding par value of at least $100 million. This document does not constitute an offering of any security, product, service or fund, including interests in the Fund, for which an offer can only be made to qualified investors by the Fund's confidential Private Placement Memorandum (the "PPM"). It is for informational purposes only and may not be relied upon by you in evaluating the merits of investing in the Fund. It is qualified in its entirety by the PPM and no offering of interests in the Fund may be made by any literature, advertising, or document in whatever form other than the PPM, which may qualify, and differ from, the information and opinions contained herein. The PPM contains important information regarding the Fund's investment objectives, risks, fees, and other matters of interest and should be carefully read prior to any investment in the Fund. There are no assurances that the stated investment objectives of the Fund will be met. The purchase of interests of the Fund is suitable only for sophisticated investors for whom an investment in the Fund does not constitute a complete investment program and who fully understand and are willing to assume the risks involved in the Fund's investment program. The interests described herein will not be registered under the laws of any jurisdiction including the United States Securities Act of 1933 or the United States Investment Company Act of 1940, the laws of any state of the United States or the laws of any foreign jurisdiction and may not be offered or sold without compliance to applicable securities laws. 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This information is directed only at persons to whom such investment funds may lawfully be promoted by a person authorised under the Act (an "authorised person") by virtue of Section 238(5) of the Act and Annex 5 to Chapter 3 of the FSA Conduct of Business Sourcebook. Shares in the Fund are only available to such persons. This information must not be relied or acted upon by any other persons. Investors in the Fund will not benefit from the rules and regulations made under the Act for the protection of investors, nor from the Financial Services Compensation Scheme. Shares in the Fund are not dealt in or on a recognised or designated investment exchange for the purposes of the Act, nor is there a market maker in such shares, and it may therefore be difficult for an investor to dispose of his shares otherwise than by way of redemption. 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	Tel: (212) 319-6060	Tel: +44 207 534 9244	Tel: (441) 292-5401	Lugano, Switzerland
	Fax: (212) 319-0450	Fax: +44 207 534 9245	Fax: (441) 292-5413	Joint Venture: Singapore
www.fggus.com	E-mail: main@fggus.com	E-mail: main@fgguk.com	E-mail: main@fggbm.com	

PROSPECT CAPITAL

Wickford Fund LP

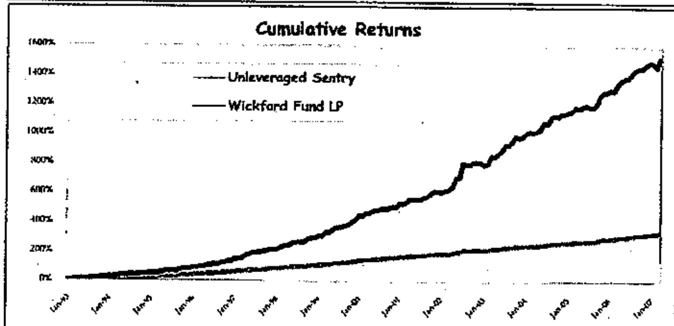
Historic Pro-Forma prior to April 1, 2007 Fund Launch

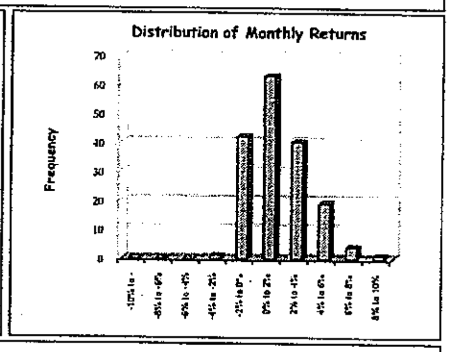
Calculations Using a Leverage Factor of 3.1x

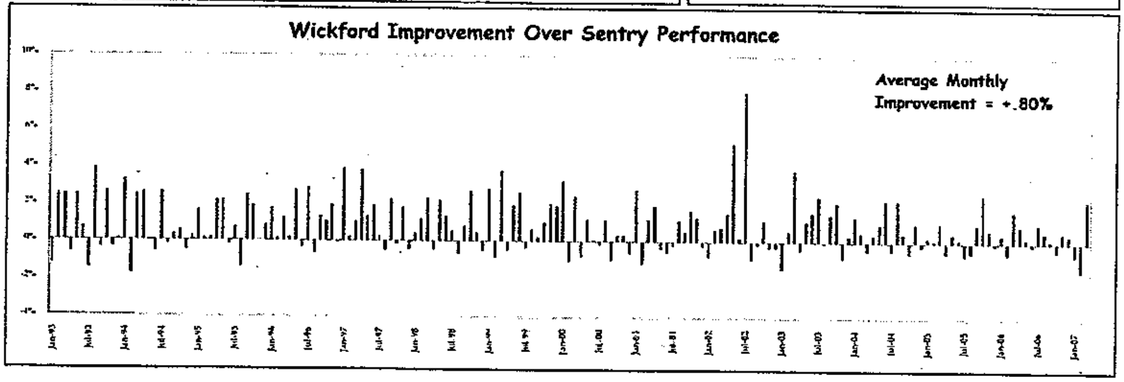
***ESTIMATED* Monthly Pro-Forma of Wickford Fund LP**

Data is Based on Actual Greenwich Sentry Net Performance and ESTIMATED Cost of Financing and Fund Expenses

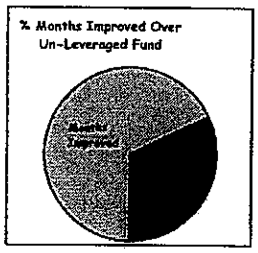
	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	YTD
2007	-0.42%	-1.85%	3.98%	*Fund Launched April 2007 - See Actual Performance Record*									1.84%
2006	1.10%	-0.41%	3.03%	1.88%	0.88%	0.29%	2.14%	1.44%	0.79%	-0.08%	1.42%	1.22%	14.53%
2005	0.74%	0.54%	1.86%	-0.48%	1.10%	0.62%	-0.83%	-0.41%	1.90%	4.29%	1.45%	0.26%	11.75%
2004	2.27%	0.97%	-0.52%	0.84%	1.65%	3.56%	-0.48%	3.61%	0.98%	-0.59%	1.83%	-0.03%	14.91%
2003	-1.93%	1.10%	5.89%	-0.45%	1.85%	2.55%	3.82%	0.05%	2.36%	3.36%	-1.06%	0.68%	19.50%
2002	-0.90%	1.27%	1.44%	2.52%	8.04%	0.57%	12.18%	-1.18%	0.06%	1.97%	-0.22%	-0.25%	27.67%
2001	4.68%	-1.24%	2.35%	3.36%	-0.10%	-0.45%	0.15%	2.09%	1.17%	2.81%	2.21%	-0.11%	18.10%
2000	5.39%	-1.01%	4.24%	-0.59%	2.48%	0.82%	0.39%	2.37%	-0.86%	1.18%	1.18%	-0.29%	16.16%
1999	4.66%	-0.79%	8.10%	-0.22%	3.41%	4.42%	0.00%	1.53%	0.89%	2.06%	3.55%	3.43%	32.92%
1998	1.22%	2.37%	3.99%	-0.15%	3.84%	2.58%	1.42%	-0.48%	1.80%	4.51%	1.25%	-0.29%	24.25%
1997	6.30%	0.85%	2.08%	6.19%	2.54%	3.40%	0.96%	-0.21%	3.90%	0.32%	3.27%	-0.15%	33.42%
1996	3.16%	0.77%	2.43%	0.84%	4.60%	0.04%	4.81%	-0.47%	2.51%	2.14%	3.46%	0.40%	27.51%
1995	3.07%	0.82%	0.88%	3.83%	3.82%	0.27%	1.69%	-1.51%	4.27%	3.40%	0.61%	1.83%	25.35%
1994	5.20%	-2.27%	4.07%	4.27%	0.50%	-0.43%	4.37%	0.17%	1.03%	1.38%	-0.17%	0.95%	20.47%
1993	-1.53%	4.10%	4.01%	-0.57%	4.05%	1.44%	-1.86%	6.11%	-0.22%	4.29%	-0.14%	0.52%	21.70%

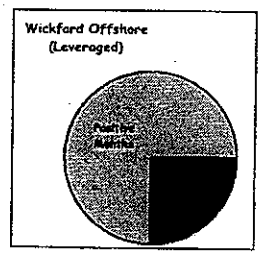






Outperformance	Greenwich Sentry (Un-Leveraged)	Wickford LP (Leveraged)
Average Monthly Return	0.86%	1.66%
% Improvement	-	92%
Months Improved	-	68%
Months Worsened	-	32%
Worst Draw-Down Period	-0.45%	-2.38%
Positive Months	94%	75%
Negative Months	6%	25%

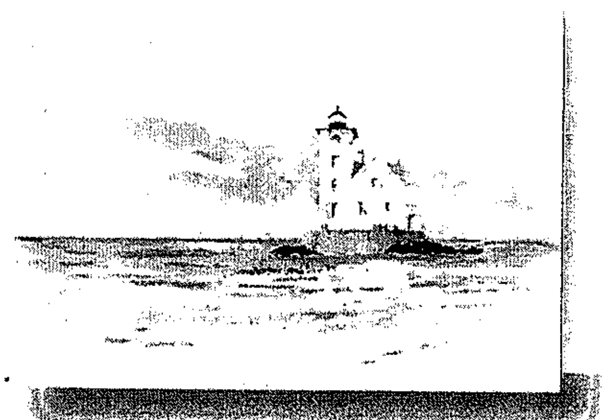




PROSPECT
CAPITAL

WICKFORD FUND, L.P.
WICKFORD OFFSHORE FUND, LTD.

May 2007



Fund Details

The Wickford Funds offer investors access to the performance of Fairfield Greenwich Group's "split strike conversion strategy" via a dynamically leveraged total return swap structure.

DOMESTIC

Wickford Fund, LP is a domestic limited partnership open to qualified purchaser investors and was launched April 1, 2007. The fund invests in Greenwich Sentry, L.P., a domestic limited partnership managed by the Fairfield Greenwich Group.

OFFSHORE

Wickford Offshore Fund, Ltd. is a Cayman investment fund that is scheduled to launch July 1, 2007 and will invest in Fairfield Sentry Ltd., a BVI fund also managed by the Fairfield Greenwich Group.

LEVERAGE

The Funds each invest in the corresponding Fairfield Greenwich Group's "Sentry" strategy via a total return swap structure using 3.0-3.25x leverage: $300-325 of exposure for every $100 invested.

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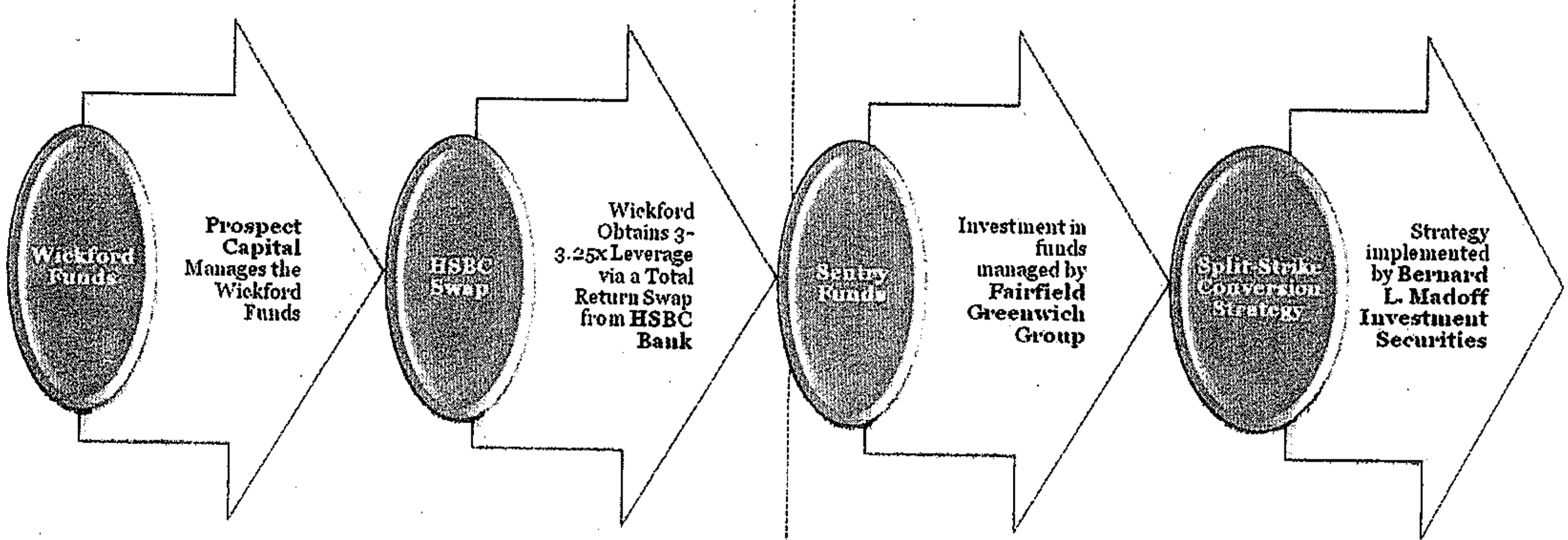
	DOMESTIC | OFFSHORE
DOMICILE	• *Delaware* | *Cayman*
MINIMUM	• $250,000 | $100,000
LIQUIDITY	• Monthly with 20-day Notice
LOCK-UP	• None
MGMT FEE	• 1.00% per year
ADMINISTRATOR	• Fortis Prime Fund Solutions
AUDITOR	• RMS McGladrey
LEGAL COUNSEL	• Appleby Hunter Bailhache (Cayman) • Shutts and Bowen LLP (USA)

Investment Management Structure



PROSPECT CAPITAL

Prospect Capital LLC

One Front St., Suite 3300
San Francisco, CA 94111
Tel 415-986-8040
Fax 415-986-8041

www.prospectcap.com

William Belhumeur
bill@prospectcap.com

Stuart Hamlyn
stuart@prospectcap.com

PROSPECT CAPITAL

- Prospect Capital LLC was founded by Stuart Hamlyn and William Belhumeur for the purpose of assisting institutional investors, fund of funds, and family offices with their alternative investment portfolios.
- Prospect concentrates on locating and researching the highest quality established and emerging fund managers that are most suitable for our sophisticated and experienced hedge fund investors.
- Traditionally, Prospect has sought to identify outstanding hedge funds that have available but limited capacity, and assisted clients in gaining capacity, often through a feeder-fund vehicle with or without additional leverage.
- Prospect Capital is the General Partner of Wickford Fund LP and the Investment Manager of Wickford Offshore Fund Ltd. The directors of Wickford Offshore are William Belhumeur and Ronan Guilfoyle (DMS Management, Cayman Islands).

Investment Strategy

The Split-Strike Conversion Strategy

- The Wickford Funds (through investment in Fairfield Sentry Ltd. and Greenwich Sentry LP) utilize a "split strike conversion" strategy which entails:
  - The purchase of a basket of equities that are highly correlated to the S&P 100 - typically consisting of 35 to 50 stocks in the S&P 100 Index;
  - The purchase of out-of-the-money S&P 100 Index Put Options with a notional value that approximately equals the market value of the basket of equity securities;
  - The sale of out-of-the-money S&P 100 Index Call Options with a notional value that approximately equals the market value of the basket of equity securities.
- The primary purpose of the long put options is to limit the market risk of the stock basket at the strike price of the long puts. The primary purpose of the short call options is to largely finance the cost of the put hedge and to increase the stand-still rate of return.
- This position in its entirety could be characterized as a bull spread which, presuming the stock basket highly correlates to the S&P 100 Index, is intended to work as follows:
  - It sets a floor value below which further declines in the value of the stock basket is offset by gains in the put options;
  - It sets a ceiling value beyond which further gains in the stock basket are offset by increasing liability of the short calls; and
  - It defines a range of potential market gain or loss, depending on how tightly the options collar is struck.
- When the spilt-strike conversion strategy is not active ("out of a trade"), the account is to be invested in treasury bills.

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Fairfield Greenwich Group

- Founded in 1983
- Over $10 billion in Assets Under Management
- Offices in New York, London, Bermuda, Latin America, Singapore
- Approximately 80 employees
- SEC & FSA Registered
- Risk management/oversight office in Bermuda: independent price verification and account value for the Sentry Funds.
- *www.fggus.com*

Fairfield Sentry Ltd. & Greenwich Sentry LP Funds

- Fairfield Sentry launched in Dec. 1990 (16 yr record)
- Greenwich Sentry launched in Jan. 1993
- Over$6 billion invested in the Split-Strike Conversion Strategy
- 10.88% Annualized Returns (domestic)
- 2.41% Annualized Standard Deviation (domestic)
- 92% Positive Months; Worst Draw-Down -0.64%
- *Complete performance records of the Sentry Funds may be provided separately.*

Performance

Wickford Fund LP

Month	Net Return	Cumulative
April 2007	1.33%	1.33%
May 2007		
June 2007		
July 2007		
August 2007		
September 2007		
October 2007		
November 2007		
December 2007		

Fund Inception: April 2007

Wickford Offshore Fund Ltd.

Expected Fund Launch:
July or August 2007

* *Pro-Forma Performance of the Funds may be available separately.*

Disclaimer

- The interests in these Funds are not offered by this brochure. Such an offer may only be made after you have received the Confidential Offering Memorandum concerning that specific Fund. This Summary does not provide all information that is material to an investor's decision to invest in any Fund, including, but not limited to, significant risk factors. Past performance is not a guarantee of future returns. For more information, please refer to the Fund's Confidential Offering Memorandum and read it carefully before you invest.
- These materials are designed for qualified investors and are for informational purposes only and are not for general distribution. This presentation does not constitute an offer to sell or a solicitation of an offer to buy any securities. Interests in the Wickford Fund, L.P. and Wickford Offshore Fund, Ltd. investment vehicles are being offered solely pursuant to Memoranda furnished to prospective subscribers on behalf of Prospect Capital, LLC, and no investment decision should be made until after the prospective subscriber has received and has had the opportunity to review a copy thereof.
- Interests in the Wickford Fund, L.P. and Wickford Offshore Fund, Ltd. investment vehicles will not be registered for offer or for sale under the laws of any jurisdiction, and may not be offered or sold except in compliance with applicable securities laws. Neither Prospect Capital, LLC, Wickford Fund, L.P. nor Wickford Offshore Fund, Ltd. or any of their affiliated entities shall be liable for any errors or omissions in this content, or for any actions taken in reliance thereon.
- The information contained herein has neither been reviewed nor approved by Fairfield Greenwich Group, Fairfield Greenwich (Bermuda) Ltd., Bernard L. Madoff Investment Securities, nor any of their affiliated investment vehicles or affiliated companies. All investment terms, statistical data, and performance information contained herein are estimated or preliminary, may be inaccurate or incomplete, and are subject to revision.
- By accepting this information, you acknowledge that you are a self directed, sophisticated investor, with experience in investing in hedge funds, and that you are a "qualified purchaser," as defined under the Investment Company Act of 1940, as amended, and an "accredited investor," as defined under Regulation D of the Securities Act of 1933, as amended. Any person who may subscribe for an interest in the investment vehicles described herein must be able to bear the risk involved and must meet the suitability requirements related to such an investment.
- The information contained in this presentation is confidential and proprietary to Prospect Capital, LLC, Wickford Fund, L.P. and Wickford Offshore Fund, Ltd. By accepting this presentation, the recipient agrees that it will keep its contents confidential, will not reproduce it in whole or in part and will not disclose the same to any third party (other than its financial, tax and legal advisors) without the express written permission of Prospect Capital.

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Friday, January 19, 2007 4:41 PM
To: 'Frank Casey'
Subject: RE: another OK year for Bernie

Frank,

Bernie would have had to have earned 11.56% gross in order to deliver 8.45% to investors. 11.56% is higher than the VIX was in 2006, so again, it's just so darn obvious the guy is a fraud.

Harry

-----Original Message-----
From: Frank Casey [mailto:[redacted]
Sent: Thursday, January 18, 2007 12:19 PM
To: Harry Markopolos
Subject: another OK year for Bernie

Fund type (key words):	**Market Neutral Equity**
Investment strategy detail	
Style:	**Market Neutral (equity)**
Market:	**EQ Energy (all cap)**
Geography:	**AMER US**
Currency Class:	**US Dollars (USD)**
Lehman/HFN Index Fund:	**Yes**

Fairfield Sentry Ltd

The Fund seeks to obtain capital appreciation of its assets principally through the utilization of a nontraditional options trading strategy described as "split strike conversion", to which the Fund allocates the predominant portion of its assets. This strategy has defined risk and profit parameters, which may be ascertained when a particular position is established. Set forth below is a description of the "split strike conversion" strategies ("SSC Investments"). The establishment of a typical position entails (i) the purchase of a group or basket of equity securities that are intended to highly correlate to the S&P 100 Index , (ii) the sale of out-of-the-money S&P 100 Index call options in an equivalent contract value dollar amount to the basket of equity securities, and (iii) the purchase of an equivalent number of out-of-the-money S&P 100 Index put options. An index call option is out-of-the-money when its strike price is greater than the current price of the index; an index put option is out-of-the-money when the strike price is lower than the current price of the index. The basket typically consists of approximately 35 to 45 stocks in the S&P 100. The logic of this strategy is that once a long stock position has been established, selling a call against such long position will increase the standstill rate of return, while allowing upward movement to the short call strike price. The purchase of an out-of-the-money put, funded with part or all of the call premium, protects the equity position from downside risk. A bullish or bearish bias of the positions can be achieved by adjustment of the strike prices in the S&P 100 puts and calls. The further away the strike prices are from the price of the S&P 100, the more bullish the strategy. However, the dollar value underlying the put options always approximates the value of the basket of stocks.

Fund Snapshot

YTD*:	**8.45%**
2006 Return:	**8.45%**
Total Return:	**496.58‹**
Fund Assets:	**5500mr**
Strategy Assets:	**5500mr**
Firm Assets:	**10600rr**
Max Drawdown:	**-0.55%**
Losing Streak:	**1 Montł**
Sharpe Ratio:	**2.51**
Typ. Net Exposure:	**N/A**
Typical Leverage:	**N/A**
***YTD Through:**	**Nov - 2(**

Frank R. Casey, Director of Marketing, Benchmark Plus Management LLC

[redacted]

Benchmark Plus is a hedged, fund-of-hedge-funds targeting market-neutral, zero-beta absolute returns. **Past Performance Is Not Necessarily Indicative of Future Results!**

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Friday, January 19, 2007 4:46 PM
To: John Wilke[redacted]@wsj.[redacted]
Subject: Bernie Madoff Returns for 2006

John,

Bernie Madoff purported to deliver 8.45% to his investors in 2006. To deliver 8.45% net, after Fairfield Sentry's 1% management fee and 20% participation, Bernie would have had to have earned 11.56% gross during a historically low volatility period. In other words, with the VIX hovering at record lows and call options selling for peanuts, he purports to have earned 11.56%. It didn't happen because it is mathematically impossible.

Fund type (key words): **Market Neutral Equity**
Investment strategy detail
Style: **Market Neutral (equity)**
Market: **EQ Energy (all cap)**
Geography: **AMER US**
Currency Class: **US Dollars (USD)**
Lehman/HFN Index Fund: **Yes**

Fairfield Sentry Ltd

The Fund seeks to obtain capital appreciation of its assets principally through the utilization of a nontraditional options trading strategy described as "split strike conversion", to which the Fund allocates the predominant portion of its assets. This strategy has defined risk and profit parameters, which may be ascertained when a particular position is established. Set forth below is a description of the "split strike conversion" strategies ("SSC Investments"). The establishment of a typical position entails (i) the purchase of a group or basket of equity securities that are intended to highly correlate to the S&P 100 Index, (ii) the sale of out-of-the-money S&P 100 Index call options in an equivalent contract value dollar amount to the basket of equity securities, and (iii) the purchase of an equivalent number of out-of-the-money S&P 100 Index put options. An index call option is out-of-the-money when its strike price is greater than the current price of the index; an index put option is out-of-the-money when the strike price is lower than the current price of the index. The basket typically consists of approximately 35 to 45 stocks in the S&P 100. The logic of this strategy is that once a long stock position has been established, selling a call against such long position will increase the standstill rate of return, while allowing upward movement to the short call strike price. The purchase of an out-of-the-money put, funded with part or all of the call premium, protects the equity position from downside risk. A bullish or bearish bias of the positions can be achieved by adjustment of the strike prices in the S&P 100 puts and calls. The further away the strike prices are from the price of the S&P 100, the more bullish the strategy. However, the dollar value underlying the put options always approximates the value of the basket of stocks.

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YTD*:	**8.45%**
2006 Return:	**8.45%**
Total Return:	**496.58%**
Fund Assets:	**5500mm**
Strategy Assets:	**5500mm**
Firm Assets:	**10600mm**
Max Drawdown:	**-0.55%**
Losing Streak:	**1 Months**
Sharpe Ratio:	**2.51**
Typ. Net Exposure:	**N/A**
Typical Leverage:	**N/A**
***YTD Through:**	**Nov - 2006**

Frank ← received from Frank Casey

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Tuesday, February 20, 2007 9:58 AM
To: 'Frank Casey'
Subject: RE: but Bernie tips off himself, doesn't he?

Bernie is so good he has perfect foreknowledge of stock prices, so you're right, he tips himself off

-----Original Message-----
From: Frank Casey [mailto[redacted]
Sent: Tuesday, February 20, 2007 9:30 AM
To: Harry Markopolos
Subject: but Bernie tips off himself, doesn't he?

Wall Street's next scandal
Mon, 19 Feb 2007, 12:20
CNNMoney/Fortune

In early February, the SEC confirmed that it was investigating whether the major brokerage houses were tipping off hedge funds to the trades the brokers handle for big clients like mutual funds. If that's happening, it would be a scandal. The SEC is also likely to scour trading records to see if the brokers are using info about clients' moves to invest their own capital. If the SEC finds evidence that they are, the scandal would be enormous - and go to the heart of Wall Street's profit machine.

Frank R. Casey, Director of Marketing, Benchmark Plus Management LLC

[redacted]

Benchmark Plus is a hedged, fund-of-hedge-funds targeting market-neutral, zero-beta absolute returns.
Past Performance Is Not Necessarily Indicative of Future Results!

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Wednesday, February 28, 2007 6:29 PM
To: Frank Casey [redacted]
Cc: Neil Chelo [redacted]
Subject: Bernie Update

Frank, Neil

The Wall Street Journal's John Wilke has been a big dissappointment. Obviously they were the wrong choice. Eventually Bernie will blow up and everybody will say, "I told you so." Feel free to buy 45 day OTM puts once the first news of the Madoff blowup comes out. I suspect he'll be considered the Enron of hedge funds while [redacted] will be called the Tyco of Hedge Funds. Both funds are bogus as three dollar bills.
Why doesn' [redacted] start a Ponzi Strategy? I'll bet [redacted] lots of aum with 10% returns and 2% vol.

Harry

Harry Markopolos

From: Harry Markopolos[redacted]
Sent: Tuesday, April 03, 2007 3:12 PM
To: 'Frank Casey'
Subject: RE: To Catch a Thief

Frank,

If Doug Reid doesn't know about Bernie I'd be surprised, since his fund is 2/3rds Bernie and 1/3rd other managers. Either he's stupid or he's corrupt, maybe even both at the same time. Besides, what are the odds that Fairfield could pull $8 billion out from Madoff and see any of the money? My bet is BM would fold like a cheap tent if someone made a large cash call. The SEC is basically worthless when it comes to derivatives fraud.

Harry

-----Original Message-----
From: Frank Casey [mailto[redacted]
Sent: Tuesday, April 03, 2007 2:47 PM
To: Harry Markopolos
Subject: To Catch a Thief

MAYBE YOU SHOULD SEND HIM AN EMAIL ON BERNIE?

TO CATCH A THIEF

21 Mar 2007

Imogen Rose-Smith

In the 1955 Alfred Hitchcock movie To Catch a Thief, it takes reformed cat burglar Cary Grant to capture the thief responsible for a series of jewelry heists across the French Riviera.

In the 1955 Alfred Hitchcock movie To Catch a Thief, it takes reformed cat burglar Cary Grant to capture the thief responsible for a series of jewelry heists across the French Riviera. Douglas Reid, managing director and investment committee member for $12 billion alternative management firm Fairfield Greenwich Group, believes the same approach holds true in creating and operating funds of hedge funds.

"Who better than a hedge fund manager to understand the business of another fund manager?" asks Reid, who joined New York–based FGG in January 2007, from Moore Capital Management, also in New York, to handle selection and oversight of external multistrategy and single-strategy hedge funds. FGG, which added $2 billion in capital last year, is keen to expand its global reach.

Frank R. Casey, Director of Marketing, Benchmark Plus Management LLC

[redacted]

Benchmark Plus is a hedged, fund-of-hedge-funds targeting zero-beta market-neutral returns to create Real Alpha™ share classes. Benchmark Plus utilizes Real Alpha™ to create enhanced indexes via portable-alpha. **Past Performance Is Not Necessarily Indicative of Future Results!**

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Friday, June 29, 2007 4:54 PM
To: Neil Chelo [redacted]
Subject: Madoff

Neil,

If Prospect Capital has hoodwinked [redacted] into selling a total return swap that levers Bernie up by 3.00 - 3.25 times, one has to wonder who's minding the risk management shop at [redacted] The HSBC risk head I met in Geneva was super sharp and saw right thru short vol strategies, but that was 4 years ago and since then short vol has made lots of money. Either that or the guy left HSBC.

This is so odd though. If you're a Ponzi why would you allow leverage? You end up paying well over double for each new dollar "invested." Is this a signal that BM is at the end of his rope and needs to offer juicier returns in order to keep the Ponzi going? Is he this desparate for cash? My bet is Bernie is nearing the end of his run if he's allowing triple leverage.

Let's see now, if BM is a fraud and I am your typical dumb HNW client and purchase the total return swap, when the underlying returns are found to be bogus, does that mean I receive nothing back or do I get my principal back and nothing else? What if BM is waiting for a systemic market crises to occur and then says, "Oops, sorry, I bet wrong and lost 90% of your money, so sorry, here's the 10% that's left, we're closing down and want you to have it back." That would be a great way out for him.

How is [redacted] managing their long hedge? Are they actually investing with BM? This is unlikely. Or, more likely, have they analyzed his return stream and found a spurious correlation to some set of factors that they can replicate using long futures in some sort of blend? If [redacted] is actually investing with BM, now that would be interesting.

Harry

Harry Markopolos

Leon Gross is Citigroup's Head of Global Equity Derivatives Research

From: Harry Markopolos [redacted]
Sent: Friday, June 29, 2007 5:23 PM
To: Leon Gross [redacted]
Subject: Bernie Madoff Returns Levered up 3.25 times via Swap offered by [redacted]

Leon,

Long time no hear but I know you'll love this. Wickford is offering a [redacted] swap on Bernie Madoff that provides 3.0 - 3.25 X's exposure to Bernie Madoff. How they're plannng on hedging this should be telling. If they aren't getting full visibility to Madoff's positions, then I'm very suspicious. If [redacted] is running a blind factor model to predict Madoff's return stream and then replicating it, I'm even more suspicious. If Madoff is allowing a 3rd party marketer to pitch this sort of product, my guess is that he's running low on new investors cash in-flows and needs to feed the Ponzi beast or face ruin. Any insight on your part on what you might be hearing? Is Madoff running short of new cash?

We all know how Ponzi Schemes turn out,

Harry Markopolos, CFA
[redacted]

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Friday, June 29, 2007 5:35 PM
To: 'Neil Chelo'
Subject: RE: Fraud Update on Bernie Madoff

Neil

Bill Eigen is a buddy of mine running a long vol, long credit spread's widening Fixed Income strategy for Highbridge. When credit speads widen and then explode during the next market crisés, he'll do well. He's the type of manager that will thrive during a market crises. The capital markets are dysfunctional and due for a blow up.

I've never met Nassim. I heard that he did great after 9-11[redacted] I haven't read the new book yet either. The Bookstaber book is very good, probably more practicle than the Taleb book too.

Now that I'm not teaching in the CFA program or attending Qwafafew meetings regularly, I don't know who the up and coming talent is in town. There's one fellow who's 24 answering the phones at Fidelity. He passed CFA Level III at age 23 and he reads calculus books and programs in C++ at home for fun. He's so smart that Fidelity's analysts tried to have him transfered to FMR Co, but the HR department said that once trained a phone rep owes Fido 1 year on the phones before he's allowed to transfer to the investment arm. He doesn't have his masters degree yet, but he's very quanty. You'd need to see what types of programs he could write for you and if they look good, he'd be worth a close look. His mom's got her Ph.D. in biochemistry from someplace like Harvard or MIT, I forget which, so brains run in the family.

You can always take out an ad with Boston QWAFAFEW for a couple hundred bucks. They'd see that your job posting went onto the QWAFAFEW International website and all sorts of quants would see it.

Harry

-----Original Message-----
From: Neil Chelo [mailto:[redacted]
Sent: Friday, June 29, 2007 5:21 PM
To: Harry Markopolos
Subject: RE: Fraud Update on Bernie Madoff

There is some much leverage in the system it is scary.

We funded a great manager last month. Bunch of guys out of Highbridge. Virtually everything they do is long volatility, long gamma, long convexity. In the last three months we invested nearly $300m into strategies like this. We expect to make some good money when things get rough in the market. Our competition continues to load up on short volatility and long credit strategies. I can't wait for the market to go south.

I met Nassim Taleb the other week. [redacted]. He is running nearly $2 Billion. I have not had a chance to read his new book yet.

(Growth at Benchmark is crazy. We were $400m when I got here. We are now over $2 Billion and could easily be $3 B by year end. Frank keeps shooting elephants and raising big chunks of money. Looking to hire more analysts, if you have anyone in mind let me know).

Neil

From: Harry Markopolos [mailto:[redacted]
Sent: Friday, June 29, 2007 3:13 PM
To: Neil Chelo
Subject: RE: Fraud Update on Bernie Madoff

Not to mention that Manny muffed the catch in the 11th inning that handed the 3rd game to Seattle.

You know, maybe you, Frank, Scott and I should launch a fund just like Bernies only we'll offer slightly higher returns with a 4% sigma. We raise $2 billion in maybe a year or 18 months, divide it into four parts and flee to a country without extradition. We then sell our story to Larry King and point out that we only did it to alert investors to the much larger Bernie Madoff Ponzi Scheme and that Bernie is our hero for teaching us how to really run a good Ponzi. Bernie then goes down, we look like heroes, and we live happily ever after in Switzerland. When the ducks are quacking for high sharpe ratios, you gotta feed them high sharpe ratios, irrespective of reality. Why be honest and let our CFA Charters hold us back?

My bet is [redacted] is using a blind factor return model to manage their end of the swap and that they do not have visibility into Madoff's proprietary holdings. If that's the case, [redacted] tomorrow.

Just kidding,

Harry

-----Original Message-----
From: Neil Chelo [mailto:[redacted]
Sent: Friday, June 29, 2007 5:02 PM
To: Harry Markopolos
Subject: RE: Fraud Update on Bernie Madoff

Sounds good, I will fill you in with more details next week. I will be having drinks with a 3rd party marketing guy that is selling this crap. So I should have some more dirt soon.

I went to the Seattle Red Sox game on Tuesday. Manny is getting paid way too much. [redacted] took three strikes in a row to lose the game. Seattle swept the Sox. Hard to believe because Seattle does not have a great team.

From: Harry Markopolos [mailto:[redacted]
Sent: Friday, June 29, 2007 2:56 PM
To: Neil Chelo
Subject: FW: Fraud Update on Bernie Madoff

Neil

I forwarded the information on BM to Meaghan Cheung, NYC's Branch Chief on the Madoff Inquiry and cced Ed Manion in the Boston office. Your name's erased from the e-mail so they won't be able to tie you in. Since you're in the industry, it's best you maintain a low profile. BM's got lots of industry connections.

Thanks for the updated performance data,

Harry
-----Original Message-----
From: Harry Markopolos [mailto[redacted]
Sent: Friday, June 29, 2007 3:58 PM
To: Meaghan Cheung ([redacted]@sec.gov)
Cc: CFA Ed Manion ([redacted]sec.gov)

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Friday, June 29, 2007 5:07 PM
To: John Wilke [redacted]@wsj.com)
Subject: FW: Fraud Update on Bernie Madoff

John

1. I sent this to Meaghan Cheung, SEC branch chief in the New York Office and cced Ed Manion, CFA in the Boston office who is convinced that Madoff is totally bogus but he's in Boston not New York.

2. If Madoff is allowing 3 - 3.25 leverage, he must be desparate for cash. The juicy return streams would definitely attract witless high net worth investors like a moth to a flame.

3. The key is the [redacted] total return swap and how [redacted] plans on hedging it. If [redacted] is replicating a levered long position in Madoff using a blend of long futures positions that tells us that even [redacted] is not privy to Madoff's proprietary positions and is just doing a blind factor analysis of Madoff's returns. If [redacted] doesn't have full visibility of Madoff's portfolio positions, it's a fraud and HSBC is going to be one very embarrassed victim. If HSBC does have full visibility into Madoff's investment positions, then I'm wrong and he's the world's greatest money manager that you never heard of.

4. I heard you guys were out on strike yesterday morning. Keep it up. Murdoch would be poison for the paper. As far as editorial freedom, the WSJ's editorials are so bad right now I actually think Murdoch could only improve them. It's the WSJ's unsurpassed content outside of those whack-job editorials that I worry about. WSJ reporters are the world's best business reporters bar none. If the WSJ falls prey to Murdoch, that'll leave only the FT and the Economist as world class repositories for serious, insightful financial journalism. You guys really need to start slamming Murdoch on the front pages.

Regards,

Harry

-----Original Message-----
From: Harry Markopolos [mailto:[redacted]
Sent: Friday, June 29, 2007 3:58 PM
To: Meaghan Cheung [redacted]
Cc: CFA Ed Manion [redacted]
Subject: Fraud Update on Bernie Madoff

Hello Meaghan,

1. Attached are some very troubling documents that show the Madoff fraud scheme is gettng even more brazen.

2. Wickford is showing a monthly estimated pro forma set of returns of an investment in Madoff that is leveraged by a factor of 3.0 to 3.25 times and earns annual returns ranging between a low of 11.75% (2005) to a hihg of 33.42% (1997).

3. Madoff couldn't possibly be managing the billions in this strategy unlevered, much less levered. I thought you would want to see these Wickford documents.

4. When Madoff finally does blow up, it's going to be spectacular, and lead to massive selling by hedge fund, fund of funds as they face investor redemptions.

Regards,

Harry Markopolos, CFA
Financial Fraud Investigator
[redacted]

CC: Ed Manion, CFA
Boston SEC Office

Greenwich Sentry Financials Transmittal Cover Page

Date: 12/14/2008

Documents Included in this PDF File:

1. July 10, 2007 e-mail from Neil Chelo, CFA, FRM, sending me the financial statements he received from Michael Bockner at Singletrack Advisors.
2. Greenwich Sentry, L.P. Financial Statements for 2004, 2005 & 2006

My Comments on the financial statements:

1. Bernie Madoff was 100% "invested" in US Treasury Bills at each year- end for the years 2004 – 2006. I would have received these statements after my 2005 SEC submission and therefore I never sent these to the SEC. I forgot to include them with my April 2, 2008 SEC submission so if the SEC has seen these, they would not have come from me. And if they had seen them, they have even more explaining to do.

2. No stock and OEX index option positions are listed for Madoff's "Split-Strike Strategy" which should have aroused glaring red flags with fiduciaries.

3. To explain how he rarely lost money in down markets, Mr. Madoff told investors that advance knowledge of the market's order flow that he would see at his Broker/Dealer unit allowed him to sell his stock and option positions and go to cash ahead of market declines. Clearly this is preposterous since Madoff Securities' order flow came only from its customers. The firm did not have access to the entire market's order flow, only a limited sub-set of trade orders from brokerage customers that could be right or wrong with their trade orders. How any market professional acting in a fiduciary capacity could swallow this hook, line and sinker is beyond comprehension.

4. Did these US Treasury bills really exist? We know that Bernie Madoff had access to software that allowed him to print falsified trade confirms. Did fiduciaries then take the extra step and check with DTC to substantiate that these US Treasury bills were in fact traded by Bernie Madoff? Why didn't fiduciaries take the extra step to confirm Madoff's trades through DTC?

Harry Markopolos

Harry Markopolos, CFA, CFE
Chartered Financial Analyst
Certified Fraud Examiner

-----Original Message----- From: Neil Chelo [mailto:nchelo@bpfunds.com] Sent: Tuesday, 7/31/2007 2:37 PM
Categories: **Case 16 Madoff**

-----Original Message-----
From: Neil Chelo [mailto:[redacted]
Sent: Tuesday, July 10, 2007 11:51 AM
To: Harry Markopolos
Subject: FW: Madoff Audits

From: Michael Bockner [mailto:mbockner@[redacted]
Sent: Tuesday, July 10, 2007 9:50 AM
To: Neil Chelo
Subject: RE: Madoff Audits

The year end audits only show the snapshot of what the fund is holding on Dec 31 of that year (and the prior year for comparison purposes). Madoff is always in T-Bills at year end so that is all you see.

If you look at the '04 audit it shows a trading income of ~12.3m and a T-Bill interest income of ~$1.8m, then the '05 audit shows the snapshot of the portfolio on Dec 31 2004 and it is all T-Bills, so he has closed out his trades and put the money into treasuries for year end which is typical for him.

I know it is odd, I am still working on getting the actual trade examples for you and again, I am happy to get you in touch with someone at the Sentry Fund to walk you through how the trade works and the process.

MICHAEL BOCKNER

Singletrack Advisors

tel [redacted]

fax [redacted]

cell [redacted]

mbockner@[redacted]

From: Neil Chelo [mailto:[redacted]
Sent: Tuesday, July 10, 2007 9:32 AM
To: Michael Bockner
Subject: RE: Madoff Audits

Isn't odd that holdings only show T-Bills every year.

From: Michael Bockner [mailto:mbockner@[redacted]]
Sent: Tuesday, July 10, 2007 9:27 AM
To: Neil Chelo
Subject: Madoff Audits

Neil:

I have attached the last three audits for the Fairfield Sentry fund which is the domestic Madoff strategy. I am still working on getting the actual trades for you. Additionally I can make available someone from the Sentry fund to walk you through a typical trade.

Hope you had a nice 4th and I will talk to you soon.

Best regards,

Mike

MICHAEL BOCKNER

Singletrack Advisors

tel [redacted]

fax [redacted]

cell [redacted]

mbockner@[redacted]

GREENWICH SENTRY, L.P.

FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

GREENWICH SENTRY, L.P.
FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

CONTENTS

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers LLP
Chartered Accountants
PO Box 82
Royal Trust Tower, Suite 3000
Toronto Dominion Centre
Toronto, Ontario
Canada M5K 1G8
Telephone +1 416 863 1133
Facsimile +1 416 365 8215

April 24, 2007

Report of Independent Auditors

To the Partners of
Greenwich Sentry, L.P.

In our opinion, the accompanying statement of assets, liabilities and partners' capital, including the schedule of investments, and the related statements of operations, changes in partners' capital and cash flows present fairly, in all material respects, the financial position of **Greenwich Sentry, L.P.** (the "Partnership") as of December 31, 2006 and the results of its operations, the changes in its partners' capital and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Partnership's management; our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these financial statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by the Partnership's management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

Chartered Accountants, Licensed Public Accountants

GREENWICH SENTRY, L.P.
STATEMENTS OF ASSETS, LIABILITIES AND PARTNERS' CAPITAL
AT DECEMBER 31, 2006 AND 2005

	Notes	2006	2005
Assets			
Investments in securities, at market value	2.1	$ 148,788,428	$ 120,831,952
(cost 2006: USD 148,788,428, 2005: USD 120,831,952)			
Cash and cash equivalents	2.2	997,800	194,943
Dividends and interest receivable		138,982	59,477
Prepaid expenses		-	19,151
Total assets		149,925,210	121,105,523
Liabilities			
Accrued expenses and accounts payable	3.1	459,319	59,558
Contributions received in advance		318,525	-
Withdrawals payable	2.8	4,840,679	13,406,921
Total liabilities		5,618,523	13,466,479
Partners' Capital		$ 144,306,687	$ 107,639,044

The accompaning notes are an integral part of these financial statements

GREENWICH SENTRY, L.P.
SCHEDULE OF INVESTMENTS
AT DECEMBER 31, 2006 AND 2005

December 31, 2006

Investment in securities, at market value	Principal Amount	Cost	Market value	Percentage of partners' capital
Debt securities				
United States				
U S Treasury bill due 2/1/2007	10,025,000	$ 9,980,589	$ 9,980,589	6.92%
U S Treasury bill due 2/8/2007	10,025,000	9,971,066	9,971,066	6.91%
U S Treasury bill due 2/15/2007	10,025,000	9,960,740	9,960,740	6.90%
U S Treasury bill due 2/22/2007	10,025,000	9,951,216	9,951,216	6.90%
U S Treasury bill due 3/1/2007	10,025,000	9,941,392	9,941,392	6.89%
U S Treasury bill due 3/8/2007	10,025,000	9,931,768	9,931,768	6.88%
U S Treasury bill due 3/15/2007	10,025,000	9,922,545	9,922,545	6.88%
U S Treasury bill due 3/22/2007	10,025,000	9,912,419	9,912,419	6.87%
U S Treasury bill due 3/29/2007	10,075,000	9,952,085	9,952,085	6.90%
U S Treasury bill due 4/5/2007	10,075,000	9,942,212	9,942,212	6.89%
U S Treasury bill due 4/12/2007	10,025,000	9,883,648	9,883,648	6.85%
U S Treasury bill due 4/19/2007	10,025,000	9,874,124	9,874,124	6.84%
U S Treasury bill due 4/26/2007	10,025,000	9,864,299	9,864,299	6.83%
U S Treasury bill due 5/3/2007	10,025,000	9,854,776	9,854,776	6.83%
U S Treasury bill due 5/10/2007	10,025,000	9,845,549	9,845,549	6.82%
Total United States		$ 148,788,428	$ 148,788,428	103.11%
Total Debt securities		$ 148,788,428	$ 148,788,428	103.11%
Total Investment in securities, at market value		$ 148,788,428	$ 148,788,428	103.11%

December 31, 2005

Investment in securities, at market value	Principal Amount	Cost	Market value	Percentage of partners' capital
Debt securities				
United States				
U S Treasury bill due 2/2/2006	12,150,000	$ 12,105,288	$ 12,105,288	11.25%
U S Treasury bill due 2/9/2006	12,150,000	12,096,418	12,096,418	11.24%
U S Treasury bill due 2/16/2006	12,150,000	12,087,427	12,087,427	11.23%
U S Treasury bill due 2/23/2006	12,150,000	12,078,194	12,078,194	11.22%
U S Treasury bill due 3/2/2006	12,150,000	12,068,231	12,068,231	11.21%
U S Treasury bill due 3/9/2006	12,150,000	12,057,782	12,057,782	11.20%
U S Treasury bill due 3/16/2006	12,150,000	12,048,669	12,048,669	11.19%
U S Treasury bill due 3/23/2006	12,150,000	12,037,977	12,037,977	11.19%
U S Treasury bill due 3/30/2006	12,150,000	12,028,865	12,028,865	11.18%
U S Treasury bill due 5/4/2006	12,150,000	11,976,984	11,976,984	11.13%
U S Treasury bill due 5/11/2006	125,000	123,111	123,111	0.11%
U S Treasury bill due 5/18/2006	125,000	123,006	123,006	0.11%
Total United States		$ 120,831,952	$ 120,831,952	112.26%
Total Debt securities		$ 120,831,952	$ 120,831,952	112.26%
Total Investment in securities, at market value		$ 120,831,952	$ 120,831,952	112.26%

GREENWICH SENTRY, L.P.
STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

	Notes	2006	2005
Investment income			
Interest income		$ 1,946,832	$ 2,778,271
Dividends		2,096,782	1,390,981
Total investment income		4,043,614	4,169,252
Expenses			
Management fees	3.1	282,277	-
Administration fees	3.1	113,953	122,236
Expense reimbursement	3.1	136,829	170,989
Other expenses		179,544	45,826
Total expenses		712,603	339,051
Net investment income		$ 3,331,011	$ 3,830,201
Realized gain investments			
Net realized gain on investments		$ 11,982,382	$ 10,262,579
Net realized gain on investments		$ 11,982,382	$ 10,262,579
Net increase in net assets resulting from operations		$ 15,313,393	$ 14,092,780

The accompaning notes are an integral part of these financial statements

GREENWICH SENTRY, L.P.
STATEMENTS OF CHANGES IN PARTNERS' CAPITAL
FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

	General Partner	Limited Partners	Total
Balance as of January 1, 2005	$ 1,609,367	$ 165,556,079	$ 167,165,446
Contributions	-	14,965,120	14,965,120
Withdrawals	(2,582,739)	(86,001,563)	(88,584,302)
Net investment income	81,763	3,748,438	3,830,201
Net realized gain on investments	204,619	10,057,960	10,262,579
Reallocation to General Partner	2,451,275	(2,451,275)	-
Balance as of December 31, 2005	1,764,285	105,874,759	107,639,044
Contributions	-	75,453,459	75,453,459
Withdrawals	(4,200,000)	(49,899,209)	(54,099,209)
Net investment income	73,991	3,257,020	3,331,011
Net realized gain on investments	266,163	11,716,219	11,982,382
Reallocation to General Partner	2,928,945	(2,928,945)	-
Balance as of December 31, 2006	$ 833,384	$ 143,473,303	$ 144,306,687

The accompaning notes are an integral part of these financial statements

GREENWICH SENTRY, L.P.
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

	2006	2005
Cash flows (used in) / provided by operating activities		
Net increase in net assets resulting from operations	$ 15,313,393	$ 14,092,780
Adjustments for:		
Net (increase)/decrease in financial assets at fair value through profit or loss	(27,956,476)	46,283,050
Net (increase) in dividends and interest receivable	(79,505)	(54,791)
Net decrease/(increase) prepaid expenses	19,151	(14,764)
Net increase/(decrease) in accrued expenses and accounts payable	399,761	(13,692)
Net cash (used in) / provided by operating activities	(12,303,676)	60,292,583
Cash flows provided by / (used in) financing activities		
Contributions	75,453,459	14,965,120
Withdrawals	(54,099,209)	(88,584,302)
Net (decrease)/increase in withdrawals payable	(8,566,242)	13,367,421
Net increase in contributions received in advance	318,525	-
Net cash provided by / (used in) financing activities	13,106,533	(60,251,761)
Net increase in cash and cash equivalents	802,857	40,822
Cash and cash equivalents at beginning of the year	194,943	154,121
Cash and cash equivalents at end of the year	$ 997,800	$ 194,943

The accompaning notes are an integral part of these financial statements

Notes to the financial statements

1 - Organization

Greenwich Sentry, L.P. (the "Partnership") is organized as a Delaware limited partnership and operates as a private investment partnership. The Partnership's investment objective seeks to obtain capital appreciation of its assets principally through the utilization of a nontraditional options trading strategy described as "split strike conversion", to which the Partnership allocates the predominant portion of its assets.

The Partnership was formed in November 1992 and commenced operations on January 1, 1993.

On December 23, 2004 Fairfield Greenwich (Bermuda) Ltd., a Bermuda corporation, assigned its general partnership agreement to Greenwich Bermuda Limited, a Bermuda corporation. The beneficial owners of Fairfield Greenwich (Bermuda) Limited have beneficial interests in the new General Partner. Effective March 1, 2006 Fairfield Greenwich (Bermuda) Ltd., became the General Partner of the Partnership (the "General Partner"). On March 27, 2006, Fairfield Greenwich (Bermuda) Ltd. filed to become a registered investment advisor with the Securities and Exchange Commission. This registration became effective April 20, 2006.

On April 30, 2006, the Partnership was converted to a 3(c)(7) fund from a 3(c)(1) fund under the Investment Company Act of 1940 in order to accommodate additional investors. Investors who were not qualified purchasers in the Partnership had their partnership interests transferred to Greenwich Sentry Partners, L.P. effective May 1, 2006 which was created as a new 3(c)(1) fund.

2 – Summary of significant accounting policies

The preparation of the financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts and disclosures in the financial statements. Actual results could differ from such estimates.

2.1 Investments

Investments in listed securities are valued at the last reported sales or bid price as determined on the exchange on which such securities are principally traded.

Investment transactions are accounted for on a trade-date basis.

2.2 Cash and cash equivalents

Cash and cash equivalents comprise balances with banks and brokers with original maturities of three months or less and are short-term highly liquid investments that are readily convertible to known amounts of cash and which are subject to insignificant changes in value.

2 – Summary of significant accounting policies (continued)

2.3 Options

An option is a contractual arrangement under which the seller (writer) grants the purchaser (holder) the right, but not the obligation, to either buy (a call option) or sell (a put option) at or by a set date or during a set period, a specific amount of securities or a financial instrument at a predetermined price. The seller receives a premium from the purchaser in consideration for the assumption of future securities price. The Partnership is exposed to credit risk on purchased options only to the extent of their carrying amount, which is their fair value.

2.4 Income taxes

No provision has been made for United States income taxes because income taxes are not levied against the Partnership. Each partner must include their share of the Partnership's taxable income or loss on their income tax return.

2.5 Income and expense recognition

Realized gains and losses on investment transactions are determined on the specific identification method. Interest income is accrued as earned and dividend income is recorded on the ex-dividend date, net of any applicable withholding taxes. Other expenses are recorded on the accrual basis as incurred.

2.6 Determination of Gains or Losses on Sale of Investments

Gains and losses from trading activity and valuations of securities and options are computed by marking to market the value of all securities at the close of business. Costs of investments are determined on a specific identification basis.

2.7 Allocation of profits and losses

The financial statements only include the assets and liabilities of the Limited Partnership and do not include other assets and liabilities, including income and related taxes of the partners.

Income (loss) of the Partnership is allocated to the Partners at the end of each month in proportion to their capital accounts (sum of cash contributions plus or minus income or loss allocated through the end of the immediately preceding month less redemptions and distributions through the same date) at the beginning of the allocation month.

2.8 Withdrawals payable

The Partnership changed its method of recognizing withdrawals in 2005 in conjunction with its adoption of FASB Statement No. 150, *Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity, as effected by* FASB Staff Position No. FAS 150-3. Withdrawals are recognized as liabilities, net of incentive allocation, when the amount requested in the withdrawal notice becomes fixed. This generally may occur either at the time of the receipt of the notice, or on the last day of a fiscal period, depending on the nature of the request. As a result, withdrawals paid after the end of the year, but based upon year-end capital balances are reflected as withdrawals payable at December 31, 2006. Withdrawal notices received for which the dollar amount is not fixed remains in capital until the amount is determined. Withdrawals payable may be treated as capital for purposes of allocations of gains/losses pursuant to the Partnership's governing documents.

3 – Notes to the financial statements

3.1 Related party transactions

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions.

Management fee
Effective May 1, 2006 the General Partner began charging Limited Partners a monthly management fee. The management fee is paid in arrears and is calculated at the annual rate of approximately 1% (0.0833% per month) of each Limited Partner's capital account based on the value of each Limited Partner's capital account, as of the end of each month.

The General Partner may agree to a different management fee arrangement in respect of any capital account of a Limited Partner, or waive or reduce the management fee in respect of any capital account of a Limited Partner, in its discretion. This will not entitle the Limited Partner that holds such account, or any other Limited Partner, to such a different arrangement, waiver or reduction in respect of any other capital account.

Expense reimbursement
Fairfield Greenwich Advisors LLC, an affiliate of the investment manager, receives an expense reimbursement from the Partnership. The expense reimbursement is payable quarterly based on the beginning quarterly net asset value, after subscriptions and redemptions, computed at the rate of 0.10% per annum.

3 – Notes to the financial statements (continued)

Administration fees
The administrator of the Partnership was GlobeOp Financial Services, LLC through August 31, 2006. Commencing September 1, 2006 the administrator was Citco Fund Services (Europe) B.V. The administrator is responsible for maintaining the financial books and records, calculating the net asset value, handling shareholder communications and supervising the payment of expenses by the Partnership.

The Partnership pays a monthly service fee, in advance, based on the beginning monthly net asset value, after subscriptions and redemptions, of the Partnership. The administrator is also reimbursed for certain out-of-pocket expenses incurred on behalf of the Partnership.

Performance Allocation
At the end of each quarter, 20% of the capital appreciation after expenses allocated to a Limited Partner's capital account is reallocated to the General Partner. If there is no capital appreciation in a given quarter, no reallocation is made until there is net capital appreciation on a cumulative basis, starting with the first quarter that no reallocation was made. The performance allocation in 2006 was $2,928,945 (2005: $2,451,275).

Accrued expenses

	2006	2005
Management fee	$282,277	$ -
Expense reimbursement	67,050	30,878
Administration fee	25,251	8,680
Professional fees	84,741	20,000
	$459,319	$59,558

3.2 Risks

It is the policy of the Partnership to transact the majority of its securities and contractual commitment activity with broker-dealers, banks and regulated exchanges that the General Partner
considers to be well established.

The Partnership's investment activities expose it to the various types of risks taken by the Partnership and the manager of the underlying investment which is associated with the financial instruments and markets in which they invest. The following summary is not intended to be comprehensive of all risks.

3 – Notes to the financial statements (continued)

Interest rate risk
The majority of the Partnership's financial assets are short term in nature; as a result, the Partnership is not subject to significant amounts of risk due to fluctuations in the prevailing levels of market interest rates.

Market price risk
The Partnership's investments and financial instruments are susceptible to market price risk arising from uncertainties about future prices of the instruments. The Partnership's overall market

positions are monitored reviewed monthly by the General Partner.

Credit risk
Credit risk is the risk that an issuer or counterparty will be unable or unwilling to meet a commitment that it has entered into with the Partnership. Financial assets, which potentially expose the Partnership to credit risk, consist principally of cash due from brokers and receivables for investments sold. The Partnership's cash balances are primarily with high credit quality, well established financial institutions. The extent of the Partnership's exposure to credit risk in respect of these financial assets approximates their carrying value as recorded in the Partnership's balance sheet.

Liquidity risk
A lack of liquidity may also result from limited trading opportunities. The Partnership's listed securities are considered to be readily realizable as they are listed for the major part on European and American stock exchanges. With some investment partnerships, investors can sell their interests at certain dates, which may occur monthly, quarterly or even annually. A lack of liquidity may also result from limited trading opportunities in alternative investment products.

Off-balance sheet risks
An off-balance sheet market risk exist when the maximum potential loss on a particular investment is greater than the value of such investment as reflected in the Company's balance.

3.3 Subsequent events

In January 2007 the limited partners made capital contributions $318,525.

4 – Financial highlights

Financial highlights for the year are as follows:

Total return	
Total return before reallocation to General Partner	12.80 %
Reallocation to General Partner	(2.50) %
Total return after reallocation to General Partner	10.30 %
Ratio to average Limited Partners' capital	
Expenses	0.60 %
Reallocation to General Partner	2.35 %
Expenses and reallocation to General Partner	2.95 %
Net investment income	2.40 %

The total return is defined as the change in value of a theoretical investment made at the beginning of the period. The returns are calculated as geometrically linked monthly returns for each month during the respective year. Monthly returns are calculated as net increase/(decrease) in net assets resulting from operations for the month (after monthly proportion for the management fee payable by the Limited Partners' of the Partnership at the end of each month) divided by the opening Partners' capital (net assets) for the month.

Opening Partners' capital (net assets) represents the balance of Limited Partners' capital at the beginning of each month, after taking into account contributions, allocations and withdrawals. This required methodology could differ significantly from an internal rate of return.

The ratios of operating expenses and net investment income to average Limited Partners' capital are computed by dividing net investment income and operating expenses by average net assets.

Financials highlights are calculated for the Partnership taken as a whole. An individual limited partner's return and ratios may vary based on different management fee and incentive arrangements and the timing of capital transactions. The net investment income (loss) ratio does not reflect the effects of the reallocation to the General Partner.

GREENWICH SENTRY, L.P.

FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

GREENWICH SENTRY, L.P.
FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

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PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers
Accountants N.V.
Fascinatio Boulevard 350
3065 WB Rotterdam
P.O. Box 8800
3009 AV Rotterdam
The Netherlands
Telephone +31 (10) 407 55 00
Facsimile +31 (10) 456 43 33
www.pwc.com/nl

To the Partners of
Greenwich Sentry L.P.

Report of independent auditors

In our opinion, the accompanying balance sheet and the related statements of operations, partners' capital and cash flows present fairly, in all material respects, the financial position of Greenwich Sentry L.P. as at December 31, 2005, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Partnership's management; our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinion. The financial statements of the Partnership as at December 31, 2004 and for the year then ended were audited by other auditors whose report dated February 21, 2005 expressed an unqualified opinion on those statements.

Rotterdam, June 26, 2006

PricewaterhouseCoopers Accountants N.V.

H.F.M. Gertsen RA

FG-1413u-av-00457493001

GREENWICH SENTRY, L.P.
STATEMENTS OF ASSETS, LIABILITIES AND PARTNERS' CAPITAL
FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

	Notes	2005	2004
Assets			
Securities at market value	2.1	$ 120,866,796	$ 167,155,080
(cost 2005: USD 120,866,796; 2004: 167,155,080)			
Cash at banks and brokers	2.2	160,099	114,043
Dividends receivable		59,477	4,686
Withdrawal paid in advance		2,582,739	-
Prepaid expenses		19,151	4,387
Total assets		123,688,262	167,278,196
Liabilities			
Accrued expenses and accounts payable	3.5	59,558	73,250
Total liabilities		59,558	73,250
Net assets		$ 123,628,704	$ 167,204,946
Net assets represented by Partners' capital		$ 167,204,946	$ 145,357,954
Capital (withdrawals) / contributions		(57,669,022)	6,811,219
Net investment result		3,830,201	2,767,000
Net realized gain on investments		10,262,579	12,268,773
Total Partners' capital		$ 123,628,704	$ 167,204,946

The accompanying notes are an integral part of these financial statements

GREENWICH SENTRY, L.P.
SCHEDULE OF INVESTMENTS
FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

December 31, 2005

Purchase Date	Description	Cost	Market value	Percentage of net assets
12/30/2005	U S Treasury bill due 2/2/2006	$ 12,105,288	$ 12,105,288	9.792%
12/30/2005	U S Treasury bill due 2/9/2006	12,096,418	12,096,418	9.784%
12/30/2005	U S Treasury bill due 2/16/2006	12,087,427	12,087,427	9.777%
12/30/2005	U S Treasury bill due 2/23/2006	12,078,194	12,078,194	9.770%
12/30/2005	U S Treasury bill due 3/2/2006	12,068,231	12,068,231	9.762%
12/30/2005	U S Treasury bill due 3/9/2006	12,057,782	12,057,782	9.753%
12/30/2005	U S Treasury bill due 3/16/2006	12,048,669	12,048,669	9.746%
12/30/2005	U S Treasury bill due 3/23/2006	12,037,977	12,037,977	9.737%
12/30/2005	U S Treasury bill due 3/30/2006	12,028,865	12,028,865	9.730%
12/30/2005	U S Treasury bill due 5/4/2006	11,976,984	11,976,984	9.688%
12/30/2005	U S Treasury bill due 5/11/2006	123,111	123,111	0.100%
12/30/2005	U S Treasury bill due 5/18/2006	123,006	123,006	0.099%
12/30/2005	Fidelity Spartan U S Treasury Money Market	34,844	34,844	0.028%
	Total 2005	$120,866,796	$120,866,796	97.766%

December 31, 2004

Purchase Date	Description	Cost	Market Value	Percentage of net assets
12/31/2004	U S Treasury bill due 4/7/2005	$ 13,965,138	$ 13,965,138	8.352%
12/31/2004	U S Treasury bill due 4/14/2005	13,956,708	13,956,708	8.347%
12/31/2004	U S Treasury bill due 4/21/2005	13,949,121	13,949,121	8.343%
12/31/2004	U S Treasury bill due 4/28/2005	13,941,815	13,941,815	8.338%
12/31/2004	U S Treasury bill due 5/5/2005	13,932,963	13,932,963	8.333%
12/31/2004	U S Treasury bill due 5/12/2005	13,925,798	13,925,798	8.329%
12/31/2004	U S Treasury bill due 5/19/2005	13,919,194	13,919,194	8.325%
12/31/2004	U S Treasury bill due 5/26/2005	13,910,905	13,910,905	8.320%
12/31/2004	U S Treasury bill due 5/2/2005	13,901,913	13,901,913	8.314%
12/31/2004	U S Treasury bill due 6/9/2005	13,894,467	13,894,467	8.310%
12/31/2004	U S Treasury bill due 6/16/2005	13,887,723	13,887,723	8.306%
12/31/2004	U S Treasury bill due 6/23/2005	13,879,574	13,879,574	8.301%
12/31/2004	U S Treasury bill due 4/7/2005	24,849	24,849	0.015%
12/31/2004	U S Treasury bill due 4/14/2005	24,834	24,834	0.015%
12/31/2004	Fidelity Spartan U S Treasury Money Market	40,078	40,078	0.024%
	Total 2004	$167,155,080	$167,155,080	99.970%

The accompanying notes are an integral part of these financial statements

GREENWICH SENTRY, L.P.
STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

	Notes	2005	2004
Investment income			
Interest income	2.4	$ 2,778,271	$ 1,819,214
Dividends	2.4	1,390,981	1,168,005
Total investment income		4,169,252	2,987,219
Expenses			
Administration fees	3.3	122,236	137,018
Expense reimbursement	3.2	170,989	41,481
Other expenses		45,826	41,720
Total expenses		339,051	220,219
Net investment result		$ 3,830,201	$ 2,767,000
Realized gain investments			
Net realized gain on investments		$ 10,262,579	$ 12,268,773
Net realized gain on investments		$ 10,262,579	$ 12,268,773
Net increase in net assets resulting from operations		$ 14,092,780	$ 15,035,773

The accompanying notes are an integral part of these financial statements

GREENWICH SENTRY, L.P.
STATEMENTS OF CHANGES IN PARTNERS' CAPITAL
FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

	Limited Partners	General Partner	Total
Balance as of January 1, 2004	$ 142,745,087	$ 2,612,867	$ 145,357,954
Contributions	74,254,415	-	74,254,415
Withdrawals	(63,443,196)	(4,000,000)	(67,443,196)
Net investment result	2,700,319	66,681	2,767,000
Net realized gain on investments	11,983,019	285,754	12,268,773
Reallocation to General Partner	(2,644,065)	2,644,065	-
Balance as of December 31, 2004	165,595,579	1,609,367	167,204,946
Contributions	14,965,120	-	14,965,120
Withdrawals	(72,634,142)	-	(72,634,142)
Net investment result	3,748,438	81,763	3,830,201
Net realized gain on investments	10,057,960	204,619	10,262,579
Reallocation to General Partner	(2,451,275)	2,451,275	-
Balance as of December 31, 2005	$ 119,281,680	$ 4,347,024	$ 123,628,704

The accompanying notes are an integral part of these financial statements

GREENWICH SENTRY, L.P.
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

	2005	2004
Cash flows used in operating activities		
Net increase in net assets resulting from operations	$ 14,092,780	$ 15,035,773
Net realized (gain) on investments	(10,262,579)	(12,268,773)
Interest and dividends – investment account	(4,039,137)	(2,987,219)
Adjustments for:		
Increase in dividends receivable	(54,791)	(4,686)
Increase in prepaid expenses	(14,764)	(4,387)
Decrease in accrued expenses and accounts payable	(13,692)	3,973
Net Cash Used In Operating Activities	(292,183)	(225,319)
Cash flows provided by / (used in) investing activities		
Cash transferred from investment account	71,050,000	(14,538,438)
Cash transferred to investment account	(10,460,000)	8,041,025
Net Cash Provided by / (Used In) Investing Activities	60,590,000	(6,497,413)
Cash flows (used in) / provided by financing activities		
Partner withdrawals	(72,634,142)	(15,230,828)
2004 partner withdrawals distributed in 2003	-	5,000
2003 partner withdrawals distributed in 2004	-	(282)
Partner contributions	14,965,120	22,042,047
2004 partner contributions received in 2003	-	(5,122,733)
2006 partner withdrawals distributed in 2005	(2,582,739)	-
Net Cash (Used In) / Provided By Financing Activities	(60,251,761)	1,693,204
Net increase / (decrease) in cash and cash equivalents	46,056	(5,029,528)
Cash and cash equivalents at beginning of the year	114,043	5,143,571
Cash and cash equivalents at end of the year	$ 160,099	114,043
Non-Cash Financing Activities:		
Partner Contributions		52,212,368
Partner Withdrawals		(52,212,368)

The accompanying notes are an integral part of these financial statements

Notes to the financial statements

1 - Organization

Greenwich Sentry, L.P. (the "Partnership") was organized as a limited partnership under the laws of the State of Delaware in November, 1992 and began operations on January 1, 1993.

The Partnership is engaged in securities trading. The Partnership's investment objective is to achieve capital appreciation through the purchase and sale of securities by utilizing an options trading strategy know as "split strike conversion".

On December 23, 2004 Fairfield Greenwich (Bermuda) Limited assigned its general partnership agreement to Greenwich Bermuda Limited, a Bermuda corporation. The beneficial owners of Fairfield Greenwich (Bermuda) Limited have beneficial interests in the new general partner.

2 – Summary of significant accounting policies

The preparation of the financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts and disclosures in the financial statements. Actual results could differ from such estimates.

2.1 Investments

Investments in listed securities are valued at the last reported sales or bid as determined on the exchange on which such securities are principally traded.

Investment transactions are accounted for on a trade basis.

2.2 Cash at banks and brokers

Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to insignificant changes in value.

2 – Summary of significant accounting policies (continued)

The Partnership maintains cash deposits in a bank. At times, such deposits exceed applicable insurance limits. The Partnership reduces its exposure to credit risk by maintaining such deposits with a high quality financial institution.

2.3 Income taxes

Income taxes are not levied against the Partnership. Each partner must include their share of the Partnership's taxable income or loss on their income tax return.

2.4 Income and expense recognition

Realized gains and losses on investment transactions are determined on the specific identification method. Interest income/expense is accrued as earned/incurred and dividend income/expense is recorded on the ex-dividend date, net of any applicable withholding taxes. Other expenses are recorded on the accrual basis as incurred.

2.5 Determination of Gains or Losses on Sale of Investments

Both realized and unrealized gains and losses on investments are taken as income and losses as incurred. Gains and losses from trading activity and valuations of securities and options are computed by marking to the market the value of all securities at the close of business. Costs of investments are determined on a specific identification basis.

2.6 Allocation of profits and losses

Income (loss) of the Partnership is allocated to the Partners at the end of each month in proportion to their capital accounts (sum of cash contributions plus or minus income or loss allocated through the end of the immediately preceding month less redemptions and distributions through the same date) at the beginning of the allocation month.

3 – Notes to the financial statements

3.1 Expense reimbursement

Fairfield Greenwich Advisors LLC, an affiliate of the investment manager, receives an expense reimbursement from the Partnership. The expense reimbursement is payable monthly based on the beginning monthly net asset value, after subscriptions and redemptions, computed at the rate of 0.10% per annum. Fairfield Greenwich Advisors LLC waived their fee for the first three quarters of 2004.

3 – Notes to the financial statements (continued)

3.2 Administration fees

The administrator of the Partnership is GlobeOp Financial Services, LLC. The administrator is responsible for maintaining the financial books and records, calculating the net asset value, handling shareholder communications and supervising the payment of expenses by the Partnership.

The Partnership pays a monthly service fee, in advance, based on the beginning monthly net asset value, after subscriptions and redemptions, of the Partnership. The administrator is also reimbursed for certain out-of-pocket expenses incurred on behalf of the Partnership.

3.3 Performance Allocation

At the end of each quarter, 20% of the capital appreciation after expenses allocated to a limited partner's capital account, is reallocated to the general partner. If there is no capital appreciation in a given quarter, no reallocation is made until there is net capital appreciation on a cumulative basis, starting with the first quarter that no reallocation was made. The performance allocation in 2005 was $2,451,275 ($2,644,065: 2004)

3.4 Accrued expenses and accounts payable

	2005	2004
Expense reimbursement	$30,878	$41,503
Administration fee	8,680	21,547
Legal and professional fees	20,000	10,200
	$59,558	$73,250

3 – Notes to the financial statements (continued)

3.5 Financial highlights

The following summarizes the Partnership's financial highlights for the years ended December 31, 2005 and 2004:

	2005	2004
Total return, annualized	8.17%	7.77%
Operating expenses to average net assets, annualized	-0.22%	-0.14%
Net investment result to average net assets, annualized	9.18%	9.33%

These financial highlights are calculated for the Limited Partners' capital, exclusive of the General Partner's capital representing the managing interest in the Partnership.

The total return is defined as the change in value of a theoretical investment made in the beginning of the period. The returns are calculated as geometrically linked monthly returns for each month during the respective year. Monthly returns are calculated as net increase/(decrease) in net assets resulting from operations for the month divided by opening Partners' capital (net assets) for the month.

Opening Partners' capital (net assets) represents the balance of Limited Partners' capital at the beginning of each month, after taking into account contributions, allocations and redemptions. This required methodology could differ significantly from an internal rate of return.

The ratios of operating expenses and net investment income to average Limited Partners' capital are computed by dividing net investment income and operating expenses by average net assets.

3 – Notes to the financial statements (continued)

3.6 Risks

It is the policy of the Partnership to transact the majority of its securities and contractual commitment activity with broker-dealers, banks and regulated exchanges that the General Partner considers to be well established.

The Partnership's investment activities expose it to the various types of risks taken by the Partnership and the manager of the underlying investment which is associated with the financial instruments and markets in which they invest. The following summary is not intended to be comprehensive of all risks and investors should refer to the Private Placement Memorandum for a more detailed discussion of the risks inherent to investing in the Partnership.

Interest rate risk

The majority of the Partnership's financial assets and liabilities are non-interest bearing; as a result, the Partnership is not subject to significant amounts of risk due to fluctuations in the prevailing levels of market interest rates.

The Partnership is exposed to risks associated with the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows.

Market price risk

The Partnership's investments and financial instruments are susceptible to market price risk arising from uncertainties about future prices of the instruments. The Partnership's overall market positions are monitored by the Company's investment manager and reviewed monthly by the General Partner.

Credit risk

Credit risk is the risk that an issuer or counterparty will be unable or unwilling to meet a commitment that it has entered into with the Partnership. Financial assets, which potentially expose the Partnership to credit risk, consist principally of cash due from brokers and receivables for investments sold. The Partnership's cash balances are primarily with high credit quality, well established financial institutions. The extent of the Partnership's exposure to credit risk in respect of these financial assets approximates their carrying value as recorded in the Partnership's balance sheet.

Liquidity risk

A lack of liquidity may also result from limited trading opportunities. The Partnership's listed securities are considered to be readily realisable as they are listed for the major part on European and American stock exchanges. With some investment partnerships, investors can sell their interests at certain dates, which may occur monthly, quarterly or even annually. A lack of liquidity may also result from limited trading opportunities in alternative investment products.

Off-balance sheet risks

An off-balance sheet market risk exists when the maximum potential loss on a particular investment is greater than the value of such investment as reflected in the Company's balance sheet.

3.7 Subsequent events – partners' capital

In January 2006 the limited partners made capital contributions and withdrawals of $2,353,920 and $13,410, 846, respectively and the general partner made a $2,582,739 withdrawal.

Effective March 1, 2006 Fairfield Greenwich (Bermuda) Ltd. became the general partner of the Partnership. On March 27, 2006, Fairfield Greenwich (Bermuda) Ltd. filed to become a registered investment advisor with the Securities and Exchange Commission. This registration became effective April 20, 2006.

GREENWICH SENTRY, L.P.

FINANCIAL STATEMENTS

FOR THE YEAR ENDED DECEMBER 31, 2004

GREENWICH SENTRY, L.P.
FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

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Berkow,
Schechter
& Company LLP

Certified Public Accountants

350 Bedford Street · Stamford, Connecticut 06901 · Tel (203) 356-1061 · Fax (203) 356-1283

INDEPENDENT CERTIFIED PUBLIC ACCOUNTANT'S REPORT

To the Partners of Greenwich Sentry, L.P.

We have audited the accompanying balance sheet of Greenwich Sentry, L.P. as of December 31, 2004 and the related statements of income, partners' capital and cash flows for the year then ended. These financial statements are the responsibility of the general partner. Our responsibility is to express an opinion on these financial statements based on our audit.

We have conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Greenwich Sentry, L.P. as of December 31, 2004 and the results of its operations and cash flows for the year then ended in conformity with generally accepted accounting principles.

Berkow, Schechter & Company LLP

Berkow, Schechter & Company LLP

February 21, 2005

GREENWICH SENTRY, L.P.
BALANCE SHEET
DECEMBER 31, 2004

ASSETS	
Cash	$ 114,043
Investments - securities, at market value	167,155,080
Dividends receivable	4,686
TOTAL ASSETS	$ 167,273,809
LIABILITIES AND PARTNERS' CAPITAL	
Accrued expenses and accounts payable	$ 68,863
Partners' capital	167,204,946
TOTAL LIABILITIES AND PARTNERS' CAPITAL	$ 167,273,809

See notes to financial statements

GREENWICH SENTRY, L.P.
STATEMENT OF INCOME
FOR THE YEAR ENDED DECEMBER 31, 2004

Trading income	$ 12,268,773
U.S. Treasury bill interest income	1,819,214
Dividend income	1,168,005
Total Income	15,255,992
Less: Administration fees	137,018
Expense reimbursement	41,481
Other expenses	41,720
NET INCOME	$ 15,035,773

See notes to financial statements

GREENWICH SENTRY, L.P.
STATEMENT OF PARTNERS' CAPITAL
FOR THE YEAR ENDED DECEMBER 31, 2004

	Limited Partners	General Partners	Total
Partners' capital at December 31, 2003	$ 142,745,087	$ 2,612,867	$ 145,357,954
Cash contributions	74,254,415	-	74,254,415
Cash withdrawals	(63,443,196)	(4,000,000)	(67,443,196)
Net income allocated	12,039,273	2,996,500	15,035,773
Partners' capital at December 31, 2004	$ 165,595,579	$ 1,609,367	$ 167,204,946

See notes to financial statements

GREENWICH SENTRY, L.P.
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2004

CASH FLOWS FROM OPERATING ACTIVITIES:	
Net income	$ 15,035,773
Adjustments for:	
Undistributed income from investments	(15,255,992)
Increase in dividends receivable	(4,686)
Decrease in accrued expenses	(414)
Net Cash Used By Operating Activities	(225,319)
CASH FLOWS FROM INVESTING ACTIVITIES:	
Cash transferred to investment account	(14,538,438)
Cash transferred from investment account	8,041,025
Net Cash Used In Investing Activities	(6,497,413)
CASH FLOWS FROM FINANCING ACTIVITIES:	
Partner contributions	22,042,047
2004 partner contributions received in 2003	(5,122,733)
Partner withdrawals	(15,230,828)
2004 partner withdrawals distributed in 2003	5,000
2003 partner withdrawal distributed i+A14n 2004	(282)
Net Cash Provided By Financing Activities	1,693,204
Decrease in cash	(5,029,528)
Cash - Beginning of Year	5,143,571
CASH - END OF YEAR	$ 114,043
NON-CASH FINANCING ACTIVITIES:	
Partner contributions	52,212,368
Partner withdrawals	52,212,368

See notes to financial statements

GREENWICH SENTRY, L.P.
NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 1 - ORGANIZATION AND BUSINESS

The Partnership was organized as a limited partnership under the laws of the State of Delaware in November, 1992 and began operations on January 1, 1993.

The Partnership is engaged in securities trading. The Partnership's investment objective is to achieve capital appreciation through the purchase and sale of these securities.

On July 1, 2003 Fairfield Greenwich Limited withdrew as general partner and Fairfield Greenwich (Bermuda) Limited became the general partner of the Partnership. This former general partner wholly owns Fairfield Greenwich (Bermuda) Limited.

On December 23, 2004 Fairfield Greenwich (Bermuda) Limited assigned its general partnership agreement to Greenwich Bermuda Limited, a Bermuda corporation. Fairfield Greenwich Limited's partners have beneficial interests in the new general partner. The capital account of Fairfield Greenwich (Bermuda) Limited is shown as general partner income and capital.

NOTE 2 - ACCOUNTING POLICIES

Determination of Gains or Losses on Sale of Investments

Gains and losses from trading activity and valuations of securities and options are computed by marking to the market the value of all securities at the close of business. Cost of investments are determined on a specific identification basis.

Income and Expenses

Income and expenses are recorded on the accrual basis.

Taxation

Income taxes are not levied against the Partnership. Each partner must include their share of the Partnership's taxable income or loss on their income tax return.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

NOTE 2 - ACCOUNTING POLICIES (Continued)

Cash and Cash Equivalents

Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to insignificant changes in value.

NOTE 3 - INVESTMENTS - SECURITIES

At December 31, 2004, securities owned by the Partnership were United States Treasury Bills, due April/May/June 2005, purchased on December 31, 2004 at a cost of $167,115,002. In addition, the investment account included United States Treasury money market funds of $40,078.

NOTE 4 - RISKS ASSOCIATED WITH FINANCIAL INSTRUMENTS

The Partnership's investment activities expose it to the various types of risks taken by the Partnership and the manager of the underlying investment which is associated with the financial instruments and markets in which they invest. These risks include interest risk, market price risk, credit risk, liquidity risk and off-balance sheet risks.

NOTE 5 - ALLOCATION OF INCOME (LOSS) TO PARTNERS

Income (loss) of the Partnership is allocated to the Partners at the end of each month in proportion to their capital accounts (sum of cash contributions plus or minus income or loss allocated through the end of the immediately preceding month less redemptions and distributions through the same date) at the beginning of the allocation month.

NOTE 6 - PERFORMANCE ALLOCATION

At the end of each quarter, 20% of the capital appreciation after expenses allocated to a limited partner's capital account, is reallocated to the general partner. If there is no capital appreciation in a given quarter, no reallocation is made until there is net capital appreciation on a cumulative basis, starting with the first quarter that no reallocation was made. The performance allocation in 2004 was $2,644,065.

NOTE 7 - MANAGEMENT FEES

As of July 1, 2003 the investment manager of the Partnership is Fairfield Greenwich (Bermuda) Limited. Through December 23, 2004, the investment manager was also the general partner. In 2004 the investment manager's fees were solely the performance allocation described in Note 6.

NOTE 8 - EXPENSE REIMBURSEMENT

Effective July 1, 2003, Fairfield Greenwich Advisors LLC, an affiliate of the investment manager, receives an expense reimbursement from the Partnership. The expense reimbursement is payable monthly based on the beginning monthly net asset value, after subscriptions and redemptions, computed at the rate of .10% per annum. Fairfield Greenwich Advisors LLC waived their fee for the first three quarters of 2004.

NOTE 9 - ADMINISTRATION FEES

The administrator of the Partnership is GlobeOp Financial Services, LLC. The administrator is responsible for maintaining the financial books and records, calculating the net asset value, handling shareholder communications and supervising the payment of expenses by the Partnership.

The Partnership pays a monthly service fee, in advance, based on the beginning monthly net asset value, after subscriptions and redemptions, of the Partnership. The administrator is also reimbursed for certain out-of-pocket expenses incurred on behalf of the Partnership.

NOTE 10 - SUBSEQUENT EVENTS - PARTNERS' CAPITAL

In January 2005 the limited partners made capital contributions and withdrawals of $352,800 and $39,500, respectively.

Feb 2007 Madoff Portfolio Transmittal Cover Page

Date: 12/13/208

Documents included in this PDF File:

2- page Excel worksheet of a Madoff Portfolio priced 02/28/2007

My comments:

1. I can't remember who sent me this particular Madoff portfolio but I took it in from one of my many industry contacts who agreed with me that Madoff was a fraud, prettied it up a bit, ran some extensions on the profit and loss, position by position, then totaled them up an analyzed them.
2. At the bottom of page two you will see that:
   A. the OEX Long Put gained $24,618,440 or + 2.15%
   B. the Long Stock Position lost ($33,547,460.92) or (2.92%)
   C. the OEX Short Call gained $5,207,600 or .45%
   D. The total Portfolio turned in a ($3,721,420.92) loss for the month
3. Note how Bernie Madoff purported to hold 51 different large cap stocks that replicated the OEX Standard & Poor's 100 index. Most of the Madoff marketing literature listed a 30 – 35 stock portfolio that replicated the OEX Standard & Poor's 100 stock index. A 51 stock basket would replicate the OEX index better than a 35 stock basket. I did not run a regression of the 51 stocks listed here to see if they replicated the OEX index but it wasn't necessary, the single stock risk assumed in this portfolio would have overwhelmed any chance of earning significant returns after trading costs. Madoff only needed one of these 51 stocks to crater to kill this portfolio's chances of earning money. His OEX index put would not have offered much protection.
4. Oddly, what are those $176,800,000 in US Treasury Bills of May 10, 2007 doing in a hedge fund portfolio that needs to earn double-digit returns per anum?
5. Bottom Line: This is a portfolio that would have a very difficult time even breaking even, much less earning double-digit returns. How did so many miss this? Does the SEC even have a clue?

Harry Markopolos

Harry Markopolos, CFA, CFE
Chartered Financial Analyst
Certified Fraud Examiner

Harry Markopolos

From: Harry Markopolo[redacted]

Sent: Tuesday, July 31, 2007 4:11 PM

To: Neil Chelo [redacted]

Subject: Madoff Portfolio as of 28.02.2007.xls

Neil,

Print out the Madoff portfolio worksheet that I modified.

1. Madoff:

A. Bot a 51 large cap stock portfolio with varying weights in each stock which lost 2.92% and for which he has 100% exposure to single stock risk in the event one or more of these stocks tank
B. Sold OEX March 675 calls which made him 45 bps
C. Bot OEX March 665 puts which made him 2.15%
D. total portfolio return is minus 32 bps

2. I find it strange that he says he's bot and sold 14,780 OEX index puts and calls. That's huge size for OEX these days.

3. He didn't sell even one single stock call. For a guy who is supposed to have 100% perfect forecasting ability on single stocks I'm rather surprised.

4. Looking at the portfolio and the 2004, 2005 and 2006 year end "audits" that show only T-bills worth $160 million or so on a $1.147 billion portfolio has me wondering where did the missing $1 billion go??? There's more holes in the Madoff portfolio than all the golf courses in Florida. Why is he in T-bills at year end? Name a broker that he trades thru? How can he afford to trade so many contracts in the thinly traded OEX? Name a pit trader in the OEX pit who has seen his trades?

Keep sending any Madoff materials along, I always enjoy seeing it. I sure wish I could figure out a way to profit from it other than buying 45 day 5% OTM puts as soon as he gets exposed,

Harry

N	28-Feb-07 LONG POSITIONS	Security ID	Quantity	Local Market Price	Current Local Cost	Local Market Value	Unrealized gain loss	% Invest	% NAV
	American Put Option								
	S&P 100 Index 665 Put 03/17/2007	DT31712	14,780	21.20	6,715,160.00	31,333,600.00	$24,618,440.00	2.73	2.72
1	**Equity**								
2	3M Co	2595708	118,240	74.08	9,012,038.32	8,759,219.20	($252,819.12)	0.76	0.76
3	AT&T Inc	2831811	975,480	36.80	36,307,595.40	35,897,664.00	($409,931.40)	3.13	3.11
4	Abbott Laboratories	2002305	236,480	54.62	12,440,957.68	12,916,537.60	$475,579.92	1.13	1.12
5	Altria Group Inc	2692632	325,160	84.28	27,987,236.78	27,404,484.80	($582,751.98)	2.39	2.38
6	American Express Co	2026082	187,219	56.87	10,806,825.16	10,647,144.53	($159,680.63)	0.93	0.92
7	American International Group	2027342	399,060	67.10	27,630,161.40	26,776,926.00	($853,235.40)	2.33	2.32
8	Amgen Inc	2023607	182,281	64.26	12,376,410.29	11,713,377.06	($663,033.23)	1.02	1.02
9	Bank of America Corp	2295677	694,660	50.87	37,213,981.02	35,337,354.20	($1,876,626.82)	3.08	3.06
10	Boeing Co	2108601	118,240	87.27	10,619,205.36	10,318,804.80	($300,400.56)	0.9	0.89
11	Bristol-Myers Squibb Co	2126335	310,380	26.39	8,529,923.49	8,190,928.20	($338,995.29)	0.71	0.71
12	Chevron Corp	2838555	344,861	68.61	24,800,864.41	23,660,913.21	($1,139,951.20)	2.06	2.05
13	Cisco Systems Inc	2198163	955,327	25.94	26,216,352.02	24,781,182.38	($1,435,169.64)	2.16	2.15
14	Citigroup Inc	2297907	768,560	50.40	41,395,952.20	38,735,424.00	($2,660,528.20)	3.38	3.36
15	Coca-Cola Co	2206657	319,787	46.68	15,355,213.22	14,927,657.16	($427,556.06)	1.3	1.29
16	Comcast Corp Cl A	2044545	480,359	25.72	13,051,178.72	12,354,820.62	($696,358.10)	1.08	1.07
17	ConocoPhillips (USD)	2685717	256,181	65.42	16,994,202.82	16,759,361.02	($234,841.80)	1.46	1.45
18	Dell Inc	2261526	349,799	22.85	8,356,520.93	7,992,907.15	($363,613.78)	0.7	0.69
19	Exxon Mobil Corp	2326618	911,874	71.68	68,381,134.40	65,363,128.32	($3,018,006.08)	5.7	5.67
20	General Electric Co	2380498	1,611,020	34.92	57,694,584.37	56,256,818.40	($1,437,765.97)	4.9	4.88
21	Goldman Sachs Group Inc	2407966	59,120	201.60	12,659,774.56	11,918,592.00	($741,182.56)	1.04	1.03
22	Google Inc Cl A	B020QX2	29,560	449.45	13,649,711.66	13,285,742.00	($363,969.66)	1.16	1.15
23	Hewlett-Packard Co	2424006	428,620	39.38	18,174,656.06	16,879,055.60	($1,295,600.46)	1.47	1.46
24	Home Depot Inc	2434209	325,160	39.60	13,408,641.54	12,876,336.00	($532,305.54)	1.12	1.12
25	Intel Corp	2463247	901,580	19.85	18,885,649.43	17,896,363.00	($989,286.43)	1.56	1.55
26	International Business Machines	2005973	236,480	93.01	23,300,198.64	21,995,004.80	($1,305,193.84)	1.92	1.91
27	JPMorgan Chase & Co	2190385	537,453	49.40	27,342,402.08	26,550,178.20	($792,223.88)	2.31	2.3
28	Johnson & Johnson	2475833	458,180	63.05	29,970,274.28	28,888,249.00	($1,082,025.28)	2.52	2.5
29	McDonald's Corp	2550707	192,140	43.72	8,635,097.25	8,400,360.80	($234,736.45)	0.73	0.73
30	Medtronic Inc	2575465	177,360	50.36	9,553,108.40	8,931,849.60	($621,258.80)	0.78	0.77
31	Merck & Co Inc	2578312	339,940	44.16	14,991,630.09	15,011,750.40	$20,120.31	1.31	1.3
32	Merrill Lynch & Co Inc	2580986	133,020	83.68	12,207,905.19	11,131,113.60	($1,076,791.59)	0.97	0.96
33	Microsoft Corp	2588173	1,354,822	28.17	39,238,531.74	38,165,335.74	($1,073,196.00)	3.33	3.31
34	Morgan Stanley	2262314	162,580	74.92	13,224,017.85	12,180,493.60	($1,043,524.25)	1.06	1.06

N	28-Feb-07 LONG POSITIONS	Security ID	Quantity	Local Market Price	Current Local Cost	Local Market Value	Unrealized gain loss	% Invest	% NAV
35	Oracle Corp	2661568	625,681	16.43	10,444,660.82	10,279,938.83	($164,721.99)	0.9	0.89
36	Pepsico Inc	2681511	251,260	63.15	16,071,284.35	15,867,069.00	($204,215.35)	1.38	1.38
37	Pfizer Inc	2684703	1,128,201	24.96	29,660,773.13	28,159,896.96	($1,500,876.17)	2.45	2.44
38	Procter & Gamble Co	2704407	493,113	63.49	31,817,485.66	31,307,744.37	($509,741.29)	2.73	2.71
39	Schlumberger Ltd	2779201	182,281	62.80	11,561,676.76	11,447,246.80	($114,429.96)	1	0.99
40	Sprint Nextel Corp	2922447	438,479	19.28	8,087,409.59	8,453,875.12	$366,465.53	0.74	0.73
41	Target Corp	2259101	133,020	61.53	8,298,370.89	8,184,720.60	($113,650.29)	0.71	0.71
42	Time Warner Inc	2712165	620,760	20.35	13,288,628.92	12,632,466.00	($656,162.92)	1.1	1.1
43	Tyco International Ltd	2038010	310,380	30.83	9,891,341.94	9,569,015.40	($322,326.54)	0.83	0.83
44	US Bancorp	2736035	275,899	35.66	10,000,498.18	9,838,558.34	($161,939.84)	0,86	0.85
45	United Parcel Service Inc Cl B	2517382	162,580	70.19	12,054,864.70	11,411,490.20	($643,374.50)	0.99	0.99
46	United Technologies Corp	2915500	157,659	65.63	10,661,511.81	10,347,160.17	($314,351.64)	0.9	0.9
47	Verizon Communications Inc	2090571	453,259	37.43	17,238,396.26	16,965,484.37	($272,911.89)	1.48	1.47
48	Wachovia Corp	2341860	295,600	55.37	17,075,496.80	16,367,372.00	($708,124.80)	1.43	1.42
49	Wal-Mart Stores Inc	2936921	379,359	48.30	18,407,901.67	18,323,039.70	($84,861.97)	1.6	1.59
50	Walt Disney Co	2270726	320,239	34.26	11,039,814.75	10,971,388.14	($68,426.61)	0.96	0.95
51	Wells Fargo & Co	2649100	532,080	34.70	19,030,126.92	18,463,176.00	($566,950.92)	1.61	1.6
						Stock-Gain (loss)	**($33,547,460.92)**		
	Fixed Income								
	USD								
	US Treasury Bill 0% 5.10.2007	B1H1WY0	88,400,000	99.01	87,459,424.00	87,523,047.25	$63,623.25	7.63	7.59
	US Treasury Bill 0% 5.10.2007	B1HM9T7	88,400,000	98.91	87,371,024.00	87,436,587.63	$65,563.63	7.62	7.58
	SHORT POSITIONS								
	S&P 100 Index 675 Call 03/17/2007	DT31267	-14,780	0.20	-5,503,200.00	-295,600.00	$5,207,600.00	-0.03	-0.03
						1,147,492,353.87		**100.02**	**99.46**
						OEX Long Put Gain	$24,618,440.00	2.15%	
						Long Stock Loss	($33,547,460.92)	-2.92%	
						OEX Short Call Gain	$5,207,600.00	0.45%	
						Portfolio Gain (Loss)	($3,721,420.92)	-0.32%	

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Tuesday, July 10, 2007 12:32 PM
To: Neil Chelo [redacted]
Subject: Bernie Madoff's amazing audit reports

Neil

1. This is beyond incredible. And, the PWC office looks to be offshore, so I bet they don't have deep pockets. Great scheme since it relies upon fund of funds not to conduct due diligence and not to ask too many questions, so they're screening their clients to ensure that only stupid ones invest with them.

2. I also suspect that the HFOF's want to believe because they need a steady eddy type of fund that earns double digit returns with low vol and gives them access. So it's a symbiotic relationship between the two parties. He fills their needs, so they don't ask questions, and both parties get rich milking their [redacted] HNW [redacted] for fees. The only losers are the HNW investors. When Bernie gets exposed, they're toast. Bernie goes to prison years later, the HFOF management team retires and hopefully has protected their money off-shore so they can't be sued for gross negligence, and the HNW investors losses approach 100%.

3. What say, you, Frank and I start a Madoff beater fund? We'll deliver returns with an even higher Sharpe Ratio. Once we've got $1 billion in aum, we split the country for Switzerland [redacted], and live under our new identities, get plastic surgery, and only [redacted]. Whatever Madoff can do, we'll do better. If his clients are stupid, we'll carefully select our clients to be even stupider. Too bad our CFA charters hold us back from bilking clients that way.

4. The SEC is clearly incompetent although you never know, they might have gotten called off the investigation by Washington. I'll bet Bernie donates lots of cash to [redacted]

Absolutely amazing, when they disect this fraud after it collapses, the entire hedge fund industry is going to get a huge black eye

Harry

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Friday, August 10, 2007 3:27 PM
To: 'Frank Casey'
Subject: RE: from NakedShorts.com

Frank,

That's an awesome sounding product! Who do I call to get an allocation? I want to take down a small peice first, say $100 million, then pitch them to the French HFOF's as a higher return, slightly higher vol product than Madoff.

Harry

-----Original Message-----
From: Frank Casey [mailto:fcasey@bpfunds.com]
Sent: Friday, August 10, 2007 3:09 PM
To: Harry Markopolos
Cc: Gary Ketselman
Subject: from NakedShorts.com

Investment dealers are excited to announce the newest structured finance product—Constant Obligation Leveraged Originated Structured Oscillating Money Bridged Asset Guarantees, or COLOSTOMY BAGS. Designed to accommodate the most sophisticated investment strategies, Colostomy Bags contain the equity tranches of Structured High Interest Taxable derivatives, or SHIT, and are leveraged an infinite amount of times through the innovative use of derivatives.

Frank R. Casey, Director-Marketing
Benchmark Plus Management, LLC
[redacted]

Benchmark Plus is a hedged, fund-of-hedge-funds targeting zero-beta market-neutral returns to create Real Alpha™ share classes. Benchmark Plus utilizes Real Alpha™ to create enhanced indexes via portable-alpha. **Past Performance Is Not Necessarily Indicative of Future Results!**

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Tuesday, August 14, 2007 10:33 AM
To: 'Ocrant, Michael (NY)'
Subject: RE: An Interesting Perspective on how AAA rated CDO's are going to blow up by HaymanJuly07.pdf .pdf

Michael

Thanks, I'm always eager to follow Bernie's "success."

Harry

-----Original Message-----
From: Ocrant, Michael (NY) [mailto:[redacted]
Sent: Tuesday, August 14, 2007 9:52 AM
To: Harry Markopolos
Subject: RE: An Interesting Perspective on how AAA rated CDO's are going to blow up by HaymanJuly07.pdf .pdf

Thanks, Harry, the reason I was asking is that a consultant I know was recently looking at the fund and was asking me questions while expressing the same sort of skepticism.

I will let you know if I hear anything specific.

Best,

Michael Ocrant
Director, Alternative Investments Conferences
Institutional Investor
[redacted]

From: Harry Markopolos [mailto[redacted]
Sent: Tuesday, August 14, 2007 10:34 AM
To: Ocrant, Michael (NY)
Subject: RE: An Interesting Perspective on how AAA rated CDO's are going to blow up by HaymanJuly07.pdf .pdf

Michael,

1. Yes, I've seen his 2004, 2005, and 2006 year-end audits. He's totally in T-bills holding roughly $160 million of them at those year-ends with no trading positions on. However, it's for a multi-billion dollar fund, so one would ask, "where's the billions, all I see here are $160 million in T-bills?" Yes, he's definitely a Ponzi.

2. I've also seen his positions for one month end. He's long 50 large cap stocks, long OTM OEX puts and short OTM OEX calls, or so he says. The put costs more than the call, so he isn't making any money there. And his long stocks are unprotected against company specific risk, since an index put only protects against market declines. He's in a position where it would be impossible to beat T-bills and in many months it would be hard to even beat a 0% return. He's as bogus as a three dollar bill.

3. Let's see how he posts his August 2007 returns. It's rather easy to come out looking good when you're a Ponzi. When it ends, it's going to be ugly and all I can say is that his investors really deserve every dollar

of losses they have coming. But he's gone on like this for a decade and a half, there's no reason he can't keep going. If he hasn 't been caught yet, the odds are in his favor.

If you hear anything please give me a call

Harry

-----Original Message-----
From: Ocrant, Michael (NY) [[redacted]m]
Sent: Monday, August 13, 2007 5:45 PM
To: Harry Markopolos
Subject: RE: An Interesting Perspective on how AAA rated CDO's are going to blow up by HaymanJuly07.pdf .pdf

Thanks, Harry. Heard anything new about Madoff recently?

Michael Ocrant
Director, Alternative Investments Conferences
Institutional Investor
[redacted]

From: Harry Markopolos [redacted]
Sent: Monday, August 13, 2007 12:43 PM
To: John Nagorniak; K. P. Rajan; Kenneth A. Shea; Louis Markopolos; Martin Duffy; Michael F. Wilcox; Ocrant, Michael (NY)
Subject: An Interesting Perspective on how AAA rated CDO's are going to blow up by HaymanJuly07.pdf .pdf

A pretty good read which explains how this toxic waste bot their way to a AAA rating and who owns this crap (Chinese banks, Chinese government, Taiwanese Banks, Korean Banks, German Banks, French Banks, UK Banks). No doubt it's in their "investment accounts" and not their "trading accounts" so it's not being marked to market and knowing the Asians, they'll put off acknowledging the losses as long as possible. IKB Bank had this junk stuffed in a Channel Islands off-balance sheet structure that has them under criminal investigation. No doubt other banks have done the same.

It should get rather interesting.....

Harry

Harry Markopolos

From: Harry Markopolos[redacted]
Sent: Tuesday, August 14, 2007 9:34 AM
To: 'Frank Casey'
Subject: RE: Amazing we have't heard about Bernie....

You're right, the HFOF's that have Bernie are going to look a lot better this month than the ones that don't. I wouldn't be surprised if he gets a ton of money next month as those "smart french and swiss HFOF's" take money away from their losing managers and give it to their stable ace, Bernie Madofff.

-----Original Message-----
From: Frank Casey [mailto:[redacted]
Sent: Tuesday, August 14, 2007 9:26 AM
To: Harry Markopolos
Subject: RE: Amazing we have't heard about Bernie....

Hey, don't give Ponzi such a relative bad rap.

Frank R. Casey
Benchmark Plus Management

From: Harry Markopolos [mailt[redacted]
Sent: Tuesday, August 14, 2007 10:24 AM
To: Frank Casey; Neil Chelo
Subject: RE: Amazing we have't heard about Bernie....

He's the best! It's easy to avoid losses when you're a Ponzi Scheme.

-----Original Message-----
From: Frank Casey [mailto:[redacted]
Sent: Tuesday, August 14, 2007 8:56 AM
To: Harry Markopolos; Neil Chelo
Subject: Amazing we have't heard about Bernie....

I'll bet that he has called every market turn intra-day perfectly! Probably another +1% month in August due.

Frank R. Casey, Director-Marketing
Benchmark Plus Management, LLC
[redacted]

Benchmark Plus is a hedged, fund-of-hedge-funds targeting zero-beta market-neutral returns to create Real Alpha™ share classes. Benchmark Plus utilizes Real Alpha™ to create enhanced indexes via portable-alpha. **Past Performance Is Not Necessarily Indicative of Future Results!**

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Wednesday, August 22, 2007 6:11 PM
To: 'Neil Chelo'
Subject: Madoff Question List

Neil,

1. **COMPANY SPECIFIC RISK**: you own index puts yet hold a diversified basket of 50 or so individual stocks that replicate the OEX index. If two stocks, with a total portfolio weight of 4% drop 50% due to company specific risk (say sub-prime exposure), how are you protected against a 2% portfolio loss? Your index put doesn't hedge against company specific risk.
2.. **CALENDAR:** A robust investment strategy should be all-weather and independent of the calendar.
A. Why are you in T-bills at year-end?
B. Are their other periods when you go into T-bills? When? Why?
3. **AUM:**
A. What are your total assets under management? I'm hearing numbers in the $30 - $50 billion range....
B. What is the maximum size that your strategy can handle without watering down returns?
C. How do you calculate that maximum?
D. Do you limit a single investor to some pre-set limit such that if that one investor pulls out, the other investors are not negatively affected?
E. Are their gates that limit withdrawals so that my investment is not adversely affected by large withdrawals unrelated to your firm's performance? Say for example, a HFOF was overly exposed to sub-prime CDO's and needs to raise cash, how does your firm protect me from their withdrawal?
4. **CBOE**:
A. What percentage of the open interest are you at the CBOE?
B. How do you model the liquidity risk of being able to open and close positions of this magnitude?
C. What do you calculate your transaction costs to be on the CBOE including bid/ask spread, price impact, commission, etc....?
D. Can I see your breakdown on transaction costs?
E. Are you the CBOE"s largest client?
F. What is your interaction with the CBOE, do you advise them on policy issues?
5. **OTC TRADES:**
A. What percentage of your trades are done on the listed exchanges vs. the OTC market?
B. What is the typical price concession in additional transaction costs measured in either vol points or basis points that your fund experiences trading in the higher transaction cost OTC markets?
C. What are the collateral requirements for these OTC positions?
D. How do you guard against counter-party credit risk in your OTC trades if, for example, your counter-party went under and you had a winning trade on?
6. **BROKERS:**
A. Who are your leading brokers for stocks? And, who's the absolute best options broker in your opinion?
B. How do you select them?
C. Who are your leading brokers for options?
D. How do you select them?
E. Do you prefer to phone in your traders or trade electronically?
F. What, in your opinion, is the best electronic trade platform for your type of index option trading? Why?
G. Do you soft-dollar?
H. What percentage of your trades are soft-dollar vs. execution only?
I. Given your size, is front-running a problem?
J. How do you guard against front-running?
7. **STRATEGY RETURNS:**
A. Experienced options traders have looked at your strategy of long index put, long index replicating stock basket, and short index call option, saying it is incapable of beating T-bills after accounting for transaction costs and management fees. How do you respond to those naysayers?
B. How do you explain the extremely low, below .03, correlation to the stock market given you own stocks albeit with a long index put and a short index call.

C. How do you explain your lack of a big down month? Odds are that the 1995 Mexican Peso Crises, 1997 Asian FX Crises, 1998 Russian Debt / LTCM Crises, or 2000 - 2003 Bear Market would have hit certain of your stock holdings very hard.
8. **FUTURES HEDGING:**
A. Do you ever use stock index futures to hedge out portfolio risk?
B. What is the low, mean, and high range of your net futures equivalent exposure in a given month?
9. **MADOFF INTERNAL TRADERS**:
A. Who are your traders?
B. What is their experience level?
C. Where did they learn how to trade your strategy?
D. Who teaches them? How long does the training last?
E. What is their education level?
F. Do you have resumes on file for these traders that I can review? I don't want to take them out of the room, I just want to glance at them.
G. What is your employee turnover on the trading desk? If employees have left, what is to prevent them from setting up a competing shop using your proprietary trading methods? How have you kept this strategy secret for so long? How do you incentivize them to stay with you? What's their average time on the desk?
H. Can I sit on your trading desk for a day to get a feel for how you run your operation?
10. **PRIME BROKER**:
A. Where do you house your positions?
B. Do you CMTA and hold positions at one single broker for ease of closing out positions and ease of collateralizing your trades?
C. If you don't CMTA, how many brokers hold your positions?
11. **BROKER REFERENCES**: Please provide me with the names and contact information of five (5) brokers who recieve order flow from your firm who will vouch for you. Obviously, since they likely recieve plenty in commissions from your firm, I expect they will all say positive things about your firm.
12. **BUSINESS MODEL:** Why haven't you set up your own hedge fund instead of relying upon third parties to market your excellent product?
13. **WORST-CASE SCENARIO RISK MODELLING:**
A. What scenario keeps you up at night?
B. What are your strategies worst-case scenarios?
C. How much can you lose for each of them?
D. If the Option Clearing Corp failed, how would you fare?
E. If the CBOE failed, how would you unwind your positions?
F. If half of your long stocks sank X% and the other half rallied X%, what does X have to be in percent for you to experience a 10% down month?
G. If your Prime Broker pulled a REFCO and failed, what's your contingency plan?
14. **COMPLIANCE:**
A. How large is your compliance staff?
B. Can I see their resumes?
C. Who do they report to?
D. Is there an independent board of directors at Madoff?
E. Who exercises performance oversight of the investment staff?
F. Have you had to discipline staff and if yes, for what offenses without, of course, naming names?
15. **REGULATORY:**
A. What regulators, US and foreign, have regulatory oversight of Madoff?
B. Are you registered with the SEC, NASD, or any other US Regulatory body?
C. Have you ever responded to routine inquiries from US based regulators? For what? When? What were the dispositions of those inquiries?
D. Has the firm ever been disciplined by a regulator? For what? When? Is the disposition a matter of public record?
E. Have employees of the firm every been disciplined by a regulator either before or during employment at Madoff? What for? When?
16. **PERSONAL QUESTIONs:** You inherit a billion dollars from a rich uncle tomorrow.
A. How much of that $1 billion would you allocate to this strategy?
B. What other strategies and managers would you allocate to?
C. Where do you believe Bernie Madoff ranks among hedge fund managers? His Sharpe Ratio is right up their with the best....
17. **CLIENT COMMUNICATIONS:**
A. How often does Madoff report results to clients?
B. Is there a daily P&L that's available to clients via the web?

C. Do you hold annual client conferences?
D. How often does Madoff provide position reports to clients? How much of a time lag is there in releasing positions to clients in order to guard against a rogue client front-running your loyal and honest clients.

Gee, I could write questions all night. Somehow I think they're not going to answer many of these questions in great detail in order to protect their proprietary trading methodology,

Good luck,

Harry

-----Original Message-----
From: Neil Chelo [mailto[redacted]
Sent: Wednesday, August 22, 2007 4:53 PM
To: Harry Markopolos
Subject: Madoff

I am speaking with Madoff's people on Friday. Send me a list of questions you would like to ask.

Neil Chelo, CFA, FRM
BENCHMARK*PLUS*
Senior Analyst
[redacted]

Original Message-----
Categories: **Case 16 Madoff**

8/24/2007 3:58 PM

Original Message-----
From: Neil Chelo [mailto:[redacted]
Sent: Friday, August 24, 2007 3:47 PM
To: Harry Markopolos
Cc: Frank Casey
Subject: Madoff

OK,

While I know it was a complete waste of time, I could not help myself given the opportunity. I had a chance to spend 45 min. on the phone with Amit Zijayvergiya (Head of Risk Management for Fairfield).

Here is what they told me:

- Fairfield has been doing business with Madoff since 1990. They have $7B with him. While they don't know the exact number, they estimate that Madoff has a total of $14B under management with a dozen people. You would think head of risk management would want to know for sure???

- How does Madoff make money? They said Bernie makes about 90bps annually on average from commissions. Hence $126m a year on $14B.

- Why would Madoff not set up his own hedge fund? Why would he let his dozen clients earn 2/20% fees while he only earns 90bps? They said Bernie does not have the operational capability to set up a hedge fund structure, no desire too, and does not have distribution to clients in Asia, Middle East, South America, Europe, etc. This was the worst answer possible, by not setting up his own fund, Bernie is leaving 100s of millions of dollars a year on the table. When I mentioned this point again I got no answer, "Couldn't Bernie establish a hedge fund and hire all the right people for less than $20m a year so he could retain these earnings?" Silence!

- Bernie is SEC registered this year and has $640m in capital in his BD operation

- Strategy: Bernie has a proprietary model (3 core factors, momentum, volatility, liquidity) that tells him when it is safe to buy stock. Meaning he is market timing the entry and exits of all his trades. While this model is quantitative, Bernie has final authority to approve the 'green light go' signal of the model. They said his ability to market time his split-strike conversions generates 70% of the alpha. The other 30% is from superior execution. To quote Amit "Bernie is long when markets go up and out of the market when it is not favorable". So for 17 years, he has had perfect market timing!

- When model says go, he starts buying basket of stocks in OEX with 95% correlation. Typically trades $1.5B at a time. As he is buying he gets OTC quotes from 12 largest BDs so he can sell a call and buy a put on the OEX (custom strikes in front month). There may be a 3-4 hour time lag between the time he buys his long stock and the time he buys puts to protect the position and sells calls to fund the put. 20% of the time he legs into calls. All option trades are OTC.

- I asked why others could not duplicate strategy. Answer: People don't have proprietary model to know when to enter and exit bull split strike trades.

- I asked Amit how dealers hedge themselves. He had no answer and had never thought about it. He thinks they simple go into the market and trade stock, SPX, or OEX options. I also asked Amit the cost to transact OTC vs. listed. Again, he had no answer.

- Madoff have 12 traders that do stock purchases and work with dealers for OTC option trades. Only does 4/5 meaningful trades a year. 2/3rds of the year there is no trading.

- Assets are custody at Madoff securities. No shit! This keeps the fraud going.

- All trade tickets are from Madoff including OTC trades. OTC trades have no time stamp.

- He said PWC audits Fairfeild and hence Madoff and confirms tickets with DTC and OTC trades with BDs, but I would want to talk to auditor. PWC is most likely being duped.

I am convinced more than ever that these guys are a fraud. I can't believe they have kept this ponzi scheme going on for this long.

EmailSig_NC

Go to source: Message

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Friday, August 24, 2007 4:35 PM
To: 'Neil Chelo'
Subject: RE: Madoff

My what a surprise!

-----Original Message-----
From: Neil Chelo [mailto[redacted]
Sent: Friday, August 24, 2007 4:28 PM
To: Harry Markopolos
Subject: RE: Madoff

I told them that I would be willing to do a separate account done with my prime broker and with only listed OEX options.

As you would expect, the answer was no.

From: Harry Markopolos [mailto:[redacted]]
Sent: Friday, August 24, 2007 2:05 PM
To: Neil Chelo
Subject: RE: Madoff

Neil,

I'm not sure sending the SEC anything would help those morons solve the case. They're so lame, I'll bet they don't even catch colds in the winter.

Harry

-----Original Message-----
From: Neil Chelo [mailto[redacted]
Sent: Friday, August 24, 2007 3:59 PM
To: Harry Markopolos
Subject: RE: Madoff

Feel free to pass my notes onto SEC. Just remove my name.

From: Harry Markopolos [mailto[redacted]
Sent: Friday, August 24, 2007 1:58 PM
To: Neil Chelo
Subject: RE: Madoff

Neil,

1. Yes, we knew it was a 100% waste of time going in. My belief is that the HFOF's like Fairfield are either in on the scheme or willfully blind. Willful blindness is not a defense.
2. Phil Wogsberg refused to meet with me to discuss my proof that Bernie was a fraud, no doubt because 45% of Access International's $1.2 billion in aum was with Bernie at the time (2002). Phil is Access's Head of Risk Management.
3. Yeah, Bernie settles for 90 bps because he's a good guy and doesn't want to set up a hedge fund

structure.
4. Bernie custodies the assets, what a surprise (not).
5. Bernie prints his own trade tickets, another big surprise (not).
6. Bernie only uses OTC options, another surprise (not)
7. Bernie puts his orders out to bid, no way, 11 of the 12 B/D's would purposely lose the bid so they could front-run.
8. Bottom Line: the Ponzi continues.

What say you, me and Frank start up a fund "that's even better than Bernie?" Once we hit $1 billion in aum, we flee to South America.

Thanks for taking the time to reconfirm that Bernie Madoff is the biggest Ponzi out there,

Harry

-----Original Message-----
From: Neil Chelo [redacted]
Sent: Friday, August 24, 2007 3:47 PM
To: Harry Markopolos
Cc: Frank Casey
Subject: Madoff

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Here is what they told me:

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- Why would Madoff not set up his own hedge fund? Why would he let his dozen clients earn 2/20% fees while he only earns 90bps? They said Bernie does not have the operational capability to set up a hedge fund structure, no desire too, and does not have distribution to clients in Asia, Middle East, South America, Europe, etc. This was the worst answer possible, by not setting up his own fund, Bernie is leaving 100s of millions of dollars a year on the table. When I mentioned this point again I got no answer, "Couldn't Bernie establish a hedge fund and hire all the right people for less than $20m a year so he could retain these earnings?" Silence!
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correlation. Typically trades $1.5B at a time. As he is buying he gets OTC quotes from 12 largest BDs so he can sell a call and buy a put on the OEX (custom strikes in front month). There may be a 3-4 hour time lag between the time he buys his long stock and the time he buys puts to protect the position and sells calls to fund the put. 20% of the time he legs into calls. All option trades are OTC.

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I am convinced more than ever that these guys are a fraud. I can't believe they have kept this ponzi scheme going on for this long.

Neil Chelo, CFA, FRM
BENCHMARKPLUS
[redacted]

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Friday, August 24, 2007 4:03 PM
To: Neil Chelo [redacted]
Subject: One more thought on Bernie

Neil,

It really is unfortunate that all of the HFOF's that have Bernie will simply fold up and enter bankruptcy, so there are no deep pockets to go after. Even PWC is only the Bermudean branch of PWC, so they can file for bankruptcy too - besides they're small.

I hate to say it but Bernie's pulled off the perfect crime. He finds HFOF's that need his return stream to sell to their stupid HNW clients. Bernie's got to be at least $30 billion. Every French and Swiss HFOF I met (about 2 dozen) had lots of Bernie and bragged that he was their best manager. They also each told me "they had special access and could get Bernie to accept new money."

Harry

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Friday, September 28, 2007 10:39 AM
To: 'Frank Casey'
Subject: RE: how much of it is Bernie?

Frank,

Not yet. My guess is he'll use the opportunity to show a small loss in order to instill confidence in his suckers, I mean investors. If the average hedge fund was down 8%, he'd want to show a down .8% or down 1.2% just so he could attribute the loss to market irrationality. And by comparison he'd look so great that his HFOF's would use it as a marketing advantage pointing out that he was down only a fraction of what the other funds were.

P.S. If we were smart, you, Neil and I would launch a Bernie like fund off-shore with no right for our investors to audit, collect $3 billion in 3 years. Then we'd wait for a big down month on Wall Street and say we lost 100% of the fund. They couldn't prove we didn't and we'd pocket the money. I call it Ponzi Plus because we'd zero out the suckers and get away with the scheme unlike most Ponzis which just implode with the managers going to prison. Obviously thievery on Wall Street is legal under the Bush Regime.

Harry

-----Original Message-----
From: Frank Casey [mailto[redacted]
Sent: Friday, September 28, 2007 9:28 AM
To: Harry Markopolos
Subject: RE: how much of it is Bernie?

Any word on how Bernie did in August?

Frank R. Casey
Benchmark Plus Management

From: Harry Markopolos [mailto[redacted]
Sent: Friday, September 28, 2007 10:38 AM
To: Frank Casey; Neil Chelo
Subject: RE: how much of it is Bernie?

Frank,

My guess is that over half is BM. Access (the French HFOF) in NYC had a 45% allocation to BM. [redacted] has a similarly large allocation because Bernie's Sharpe Ratio is so high, he makes your HFOF look a lot better than your peers so you get the inflows. In other words, either the HFOF's know that BM's a fraud (which means they're smart) or they don't know (which means they're stupid). The bottom line is, Bernie's numbers sell, so no one looks too hard for fear of what they'll find. In legal terms it's called willful negligence. In the meantime, these HFOF's experience inflows, increasing salaries and bonuses, and it's all thanks to Bernie. They've got a vested interest in Bernie's continued "success."

Harry

-----Original Message-----
From: Frank Casey [redacted]
Sent: Thursday, September 27, 2007 3:35 PM

To: Harry Markopolos; Neil Chelo
Subject: how much of it is Bernie?

Fairfield Greenwich Group adds Maria Teresa Pulido as partner and head of global sales
Fairfield Greenwich Group ("FGG"), a global alternative asset management firm with over USD $15 billion assets under management, today announced that it has added a senior professional to its team at the hedge fund specialist's Madrid representative office. Maria Teresa Pulido will join as a Partner and Head of Global Sales.

Frank R. Casey, Director-Marketing
Benchmark Plus Management, LLC
[redacted]

Benchmark Plus is a hedged, fund-of-hedge-funds targeting zero-beta market-neutral returns to create Real Alpha™ share classes. Benchmark Plus utilizes Real Alpha™ to create enhanced indexes via portable-alpha. **Past Performance Is Not Necessarily Indicative of Future Results!**

Harry Markopolos

From: Harry Markopolos [redacted]
Sent: Friday, September 28, 2007 10:39 AM
To: 'Frank Casey'
Subject: RE: Fairfield Sentry

Amazing! Bernie's the Best ever!! And to think I thought he'd show a loss just to prove he's not an alien from outer space with perfect market-timing ability. Geez, the Sci-Fi Channel should feature him.

Harry

-----Original Message-----
From: Frank Casey [mailto[redacted]
Sent: Friday, September 28, 2007 9:34 AM
To: Harry Markopolos; Neil Chelo
Subject: Fairfield Sentry

July 0.17%C

That guy is good!

2005	0.51%E	0.37%E	0.85%C	0.14%C	0.63%C	0.46%E	0.13%E	0.16%C	0.89%C	1.61%C
2006	0.70%C	0.20%C	1.31%C	0.94%C	0.70%C	0.51%C	1.06%E	0.77%E	0.68%E	0.42%E
2007	0.29%C	-0.11%C	1.64%C	0.98%C	0.81%C	0.22%C	0.17%C	0.31%C	--	--

Frank R. Casey, Director-Marketing
Benchmark Plus Management, LLC
[redacted]

Benchmark Plus is a hedged, fund-of-hedge-funds targeting zero-beta market-neutral returns to create Real Alpha™ share classes. Benchmark Plus utilizes Real Alpha™ to create enhanced indexes via portable-alpha. **Past Performance Is Not Necessarily Indicative of Future Results!**

2008 Madoff Case Activity Cover Letter

Analysis Date: 12/28/2008

Documents included in this PDF File:

1. Microsoft Outlook V-card for Jonathan Sokobin, Ph.D.; SEC's Director of Risk Assessment in Washington, DC
2. March 31, 2008 e-mail from Dr. Sokobin requesting that we have a chat about emerging risk to the marketplace and my April 1, 2008 reply agreeing to talk with him.
3. April 2, 2008 e-mail cover letter accompanying my updated December 22, 2005 Submission to the SEC with 5 attachments.
4. December 16, 2008 SEC Press Release 2008-297: 3rd paragraph mentions my repeated, credible and specific submissions to the SEC over a period of several years.
5. December 18, 2008 Wall Street Journal Cover Story regarding my 8½ year long Madoff investigation.

My comments:

1. Dr. Sokobin and I had a very nice chat about emerging risks to the marketplace. I discussed the concept of "exchange risk" whereby investment banks and banks now owned many of the seats and specialist posts on major exchanges such that if these banks faced bankruptcy they could take certain exchanges down with them. I provided him with the LIFFE example where the LIFFE (a London based derivatives exchange) shared a margin facility with the London Metals Exchange during a copper squeeze in the 1990's. If the LME had gone bust, which it almost did, then its failure would have taken the LIFFE with it. I also discussed how Credit Default Swaps were risk magnifiers not risk mitigators as former FED Chairman Greenspan thought. I then e-mailed him the latest information that I had on Bernie Madoff. I called a few times afterwards but Dr. Sokobin never called back. After this I just gave up and figured eventually Bernie would blow up and prove me right. I had no inkling that this would occur in 2008.

2. You will notice that I sent Dr. Sokobin my December 22, 2005 Submission to the SEC. That's because I never bothered to update that submission past that point in time. I felt it was good enough and if the SEC couldn't follow that trail of breadcrumbs directly to the heart of the fraud, then the SEC's staff were either incompetent, politically influenced by the Madoff family's longstanding relationships with the SEC and NASDAQ, or were bought off and not to be trusted.

3. In the December 22, 2005 Submission to the SEC contained herein you will see a handwritten notation near the top of page one "*actually it was May 2000.*" I believe that I may have made a mistake as to the date of my first meeting with the SEC's Boston Office and incorrectly listed it as May 1999 in my SEC Submissions when the data suggest my first meeting actually took place in May 2000.

4. By 2008 I had truly given up and, to date, I cannot locate any 2008 e-mail correspondence between myself, Neil Chelo and Frank Casey about Madoff. Apparently we all had given up on the SEC and the Wall Street Journal's appetite to investigate this case. The capital markets were dropping precipitously so Neil and Frank were busy with their hedge fund of funds businesses. Meanwhile, I was busy investigating other large financial fraud cases, so this April 2008 e-mail exchange, telephone conversation and document submission is the only meaningful activity that took place with regard to the case until Madoff turned himself in on Thursday, December 11, 2008. I think that the only person who hadn't given up on Madoff was Ed Manion, CFA of the SEC's Boston Office. Mr. Manion and I talked about the Madoff Ponzi Scheme on a frequent basis throughout my entire 8½ year journey through whistleblower hell. If the SEC has an employee of the decade award, it should go to Ed Manion for his diligence, perseverance, and moral courage. Ed's the guy that kept me going throughout. Without his continued encouragement and unwavering belief in my analysis, I would have given up after my May 2000 presentation to the SEC's Boston Office. In my opinion, Ed Manion is an American hero and deserves to be recognized as such.

5. While attending my children's martial arts lesson, at approximately 5:15 pm on Thursday, December 11, 2008, my cell phone buzzed to let me know that I had received two voice-mail messages. The first message was from Andre Mehta, CFA (Managing Director at Cambridge Associates Boston Office where he is responsible for Alternative Investments). Andre informed me that Madoff was in federal custody and admitted to running a Ponzi Scheme. I called Andre back immediately from the hallway and we chatted about the possible impact on the capital markets. The second call was from David Henry, CFA (formerly Chief Investment Officer of Carruth Management LLC in Boston) and the same message ensued so I called Dave Henry and we discussed Madoff's arrest and its implications for the capital markets the next day.

6. That same evening, shortly after the two phone calls referenced above, Mr. Greg Zuckerman of the Wall Street Journal's New York Bureau called me to say that CNBC was reporting the existence of a Madoff whistleblower and he asked me if I was that whistleblower. I replied yes and he asked me if I would grant the Wall Street Journal an exclusive on the story. I agreed and spent the next six days faxing, copying, scanning and e-mailing Mr.

Zuckerman case documents. In the interim my family, my former employer, my friends, and colleagues in professional organizations were deluged by media requests. I quickly learned to ignore these requests so that I could get the story out using the Wall Street Journal as my single point of contact figuring that it was important to tell the story well and have it fact-checked before going to print. I also agreed to work with one TV show (CBS's 60 Minutes) and one radio outlet (National Public Radio's WBUR Boston Affiliate) in order to simplify my life and ensure that the story was properly reported. I knew that I needed to avoid "drive-by shooting" journalism from multiple media outlets that would result in a large number of confusing 15 second sound bites that misinformed victims and investors. My media strategy was to pick the best of breed venues from print, TV and radio and work with them to conduct in-depth, accurate, fact-checked reporting. I later relented and agreed to a Boston Globe interview since I live and work here but hope not to do any more media interviews beyond those listed above.

Harry Markopolos

Harry Markopolos, CFA, CFE
Chartered Financial Analyst
Certified Fraud Examiner

Harry Markopolos

Full Name:	Jonathan Sokobin
Last Name:	Sokobin
First Name:	Jonathan
Job Title:	Director
Company:	SEC Office of Risk Assessment
Business Address:	SEC Office of Risk, Assessment
Business:	(202) 551-[redacted]
E-mail:	[redacted]@sec.gov
E-mail Display As:	Jonathan Sokobin[redacted]@sec.gov)

Harry Markopolos

Subject: FW: Hoping to talk

-----Original Message-----
From: Harry Markopolos [mailto[redacted]
Sent: Tuesday, April 01, 2008 2:54 PM
To: 'Sokobin, Jonathan'
Cc: Rudi Schadt (rschadt@[redacted]
Subject: RE: Hoping to talk

Jonathan,

Yes, I'd love to chat with you about some new areas of risk that I don't think are on the radar screen but need to be researched. I've learned to respect anyone who survived the University of Chicago Ph.D. program. If you're available tomorrow (Wednesday), name your best times and I'll call.

Regards,

Harry Markopolos
[redacted]

-----Original Message-----
From: Sokobin, Jonathan [mailto:[redacted]
Sent: Monday, March 31, 2008 7:58 AM
To: harry[redacted]
Cc: Schadt, Rudi
Subject: Hoping to talk

Harry,

Our mutual friend, Rudi Schadt has suggested that I contact you. Rudi tells me that he has great respect for you and that I would do well to listen. Please let me know when you might have some time to chat. Thanks in advance.

-Jonathan

Jonathan Sokobin

SEC, Office of Risk Assessment

[redacted]sec.gov [redacted]

Harry Markopolos

Subject: FW: $30 Billion Equity Derivatives Hedge Fund Fraud in New York

-----Original Message-----
From: Harry Markopolos [mailto[redacted]]
Sent: Wednesday, April 02, 2008 11:13 AM
To: Jonathan Sokobin ([redacted]ec.gov)
Subject: $30 Billion Equity Derivatives Hedge Fund Fraud in New York

Jonathan,

1. Thank you for taking the time to chat with me today.

2. Attached is a submission I've made to the SEC three times in Boston. Each time Boston sent this to New York. Meagan Cheung, branch chief, in New York actually investigated this but with no result that I am aware of. In my conversations with her, I did not believe that she had the derivatives or mathematical background to understand the violations.

3. Interestingly, a former derivatives PM's who I know who is now DOR at a HFOF tells me that a counter-part at another HFOF pulled his money out of Madoff after asking Madoff for trade tickets. He then went to the OPRA time & sales price feed and discovered that none of the Madoff trade tickets matched any time & sales reports on OPRA. He quickly concluded that Madoff was a fraud and pulled significant assets out of the fund.

4. Another good source of leads is the press. At the NY Times, Alex Berenson, Gretchen Morgenstern, and Jenny ? are pretty much in the know. The Wall Street Journal's reporters, particularly John Wilke, senior investigative reporter for the WSJ's Washington Bureau would be well worth your time taking out for drinks since he's local and knows so much. John's nickname is "front-page" for all of the exposes he's landed on page one at the WSJ. He broke the stories on 3 Congressmen last year, all of whom are under DOJ investigation and two of whom are under federal criminal indictment. John's a former Boston Globe reporter and a huge Red Sox fan.

Best of luck in your new position,

Harry

The World's Largest Hedge Fund is a Fraud

December 22, 2005 Submission to the SEC
Madoff Investment Securities, LLC
www.madoff.com

Actually it was
MAY 2000

Opening Remarks:

I am the original source for the information presented herein having first presented my rationale, both verbally and in writing, to the SEC's Boston office in May, 1999 before any public information doubting Madoff Investment Securities, LLC appeared in the press. There was no whistleblower or insider involved in compiling this report. I used the Mosaic Theory to assemble my set of observations. My observations were collected first-hand by listening to fund of fund investors talk about their investments in a hedge fund run by Madoff Investment Securities, LLC, a SEC registered firm. I have also spoken to the heads of various Wall Street equity derivative trading desks and every single one of the senior managers I spoke with told me that Bernie Madoff was a fraud. Of course, no one wants to take undue career risk by sticking their head up and saying the emperor isn't wearing any clothes but....

I am a derivatives expert and have traded or assisted in the trading of several billion $US in options strategies for hedge funds and institutional clients. I have experience managing split-strike conversion products both using index options and using individual stock options, both with and without index puts. Very few people in the world have the mathematical background needed to manage these types of products but I am one of them. I have outlined a detailed set of Red Flags that make me very suspicious that Bernie Madoff's returns aren't real and, if they are real, then they would almost certainly have to be generated by front-running customer order flow from the broker-dealer arm of Madoff Investment Securities. LLC.

Due to the sensitive nature of the case I detail below, its dissemination within the SEC must be limited to those with a need to know. The firm involved is located in the New York Region.

As a result of this case, several careers on Wall Street and in Europe will be ruined. Therefore, I have not signed nor put my name on this report. I request that my name not be released to anyone other than the Branch Chief and Team Leader in the New York Region who are assigned to the case, without my express written permission. The fewer people who know who wrote this report the better. I am worried about the personal safety of myself and my family. Under no circumstances is this report or its contents to be shared with any other regulatory body without my express permission. This report has been written solely for the SEC's internal use.

As far as I know, none of the hedge fund, fund of funds (FOF's) mentioned in my report are engaged in a conspiracy to commit fraud. I believe they are naïve men and women with a notable lack of derivatives expertise and possessing little or no quantitative finance ability.

There are 2 possible scenarios that involve fraud by Madoff Securities:

1. Scenario # 1 **(Unlikely):** I am submitting this case under Section 21A(e) of the 1934 Act in the event that the broker-dealer and ECN depicted is actually providing the stated

returns to investors but is earning those returns by front-running customer order flow. Front-running qualifies as insider-trading since it relies upon material, non-public information that is acted upon for the benefit of one party to the detriment of another party. Section 21A(e) of the 1934 Act allows the SEC to pay up to 10% of the total fines levied for insider-trading. We have obtained approval from the SEC's Office of General Counsel, the Chairman's Office, and the bounty program administrator that the SEC is able and willing to pay Section 21A(e) rewards. This case should qualify if insider-trading is involved.

2. Scenario # 2 **(Highly likely)** Madoff Securities is the world's largest Ponzi Scheme. In this case there is no SEC reward payment due the whistle-blower so basically I'm turning this case in because it's the right thing to do. Far better that the SEC is proactive in shutting down a Ponzi Scheme of this size rather than reactive.

Who: The politically powerful Madoff family owns and operates a New York City based broker-dealer, ECN, and what is effectively the world's largest hedge fund. Bernard "Bernie" Madoff, the family patriarch started the firm.

According to the www.madoff.com website, *"Bernard L. Madoff was one of the five broker-dealers most closely involved in developing the NASDAQ Stock Market. He has been chairman of the board of directors of the NASDAQ Stock Market as well as a member of the board of governors of the NASD and a member of numerous NASD committees. Bernard Madoff was also a founding member of the International Securities Clearing Corporation in London.*

His brother, Peter B. Madoff *has served as vice chairman of the NASD, a member of its board of governors, and chairman of its New York region. He also has been actively involved in the NASDAQ Stock Market as a member of its board of governors and its executive committee and as chairman of its trading committee. He also has been a member of the board of directors of the Security Traders Association of New York. He is a member of the board of directors of the Depository Trust Corporation.*

What:

1. The family runs what is effectively the world's largest hedge fund with estimated assets under management of <u>at least $20 billion to perhaps $50 billion</u>, but no one knows exactly how much money BM is managing. That we have what is effectively the world's largest hedge fund operating underground is plainly put shocking. But then again, we don't even know the size of the hedge fund industry so none of this should be surprising. A super-sized fraud of this magnitude was bound to happen given the lack of regulation of these off-shore entities. My best guess is that approximately $30 billion is involved.
2. However the hedge fund isn't organized as a hedge fund by Bernard Madoff (BM) yet it acts and trades exactly like one. BM allows third party Fund of Funds (FOF's) to private label hedge funds that provide his firm, Madoff Securities, with equity tranch funding. In return for equity tranch funding, BM runs a trading strategy, **as agent**, whose returns flow to the third party FOF hedge funds and their investors who put up equity capital to

fund BM's broker-dealer and ECN operations. *BM tells investors it earns its fees by charging commissions on all of the trades done in their accounts.*

Red Flag # 1: *Why would a US broker-dealer organize and fund itself in such an unusual manner? Doesn't this seem to be an unseemly way of operating under the regulator's radar screens? Why aren't the commissions charged fully disclosed to investors? Can a SEC Registered Investment Advisor charge **both** commissions and charge a principle fee for trades? **MOST IMPORTANTLY**, why would BM settle for charging only undisclosed commissions when he could earn standard hedge fund fees of 1% management fee + 20% of the profits? Doing some simple math on BM's 12% average annual return stream to investors, the hedge fund, before fees, would have to be earning average annual returns of 16%. Subtract out the 1% management fee and investors are down to 15%. 20% of the profits would amount to 3% (.20 x 15% = 3% profit participation) so investors would be left with the stated 12% annual returns listed in Attachment 1 (Fairfield Sentry Ltd. Performance Data). Total fees to the third party FOF's would amount to 4% annually. Now why would BM leave 4% in average annual fee revenue on the table unless he were a Ponzi Scheme? Or, is he charging a whole lot more than 4% in undisclosed commissions?*

3. The third parties organize the hedge funds and obtain investors but 100% of the money raised is actually managed by Madoff Investment Securities, LLC in a purported hedge fund strategy. The investors that pony up the money don't know that BM is managing their money. That Madoff is managing the money is purposely kept secret from the investors. Some prominent US based hedge fund, fund of funds, that "invest" in BM in this manner include:
   A. Fairfield Sentry Limited (Arden Asset Management) which had $5.2 billion invested in BM as of May 2005; 11th Floor, 919 Third Avenue; New York, NY 10022; Telephone 212.319.606; The Fairfield Greenwich Group is a global family of companies with offices in New York, London and Bermuda, and representative offices in the U.S., Europe and Latin America. Local operating entities are authorized or regulated by a variety of government agencies, including Fairfield Greenwich Advisors LLC, a U.S. SEC registered investment adviser, Fairfield Heathcliff Capital LLC, a U.S. NASD member broker-dealer, and Fairfield Greenwich (UK) Limited, authorized and regulated by the Financial Services Authority in the United Kingdom.
   B. Access International Advisors; www.aiagroup.com; a SEC registered investment advisor, telephone # 212.223.7167; Suite 2206; 509 Madison Avenue, New York, NY 10022 which had over $450 million invested with BM as of mid-2002. The majority of this FOF's investors are European, even though the firm is US registered.
   C. Broyhill All-Weather Fund, L.P. had $350 million invested with BM as of March 2000.
   D. Tremont Capital Management, Inc. Corporate Headquarters is located at 555 Theodore Fremd Avenue; Rye, New York 10580; T: (914) 925-1140 F: (914) 921-3499. Tremont oversees on an advisory and fully discretionary basis over $10.5 billion in assets. Clients include institutional investors, public and private pension plans, ERISA plans, university endowments, foundations, and financial institutions, as well as high net worth individuals. Tremont is owned by Oppenhiemer Funds Inc. which is owned by Mass Mutual Insurance Company so they should have sufficient reserves to make investors whole. Mass Mutual is currently under investigation by the Massachusetts Attorney General, the Department of Justice, and the SEC.

E. Kingate Fund run by FIM Advisers LLP is headquartered in London at 20 St. James Street; London SW1A 1ES; telephone # +44 20 7389 8900; fax # +44 20 7389 8911; www.fim-group.com/ However, their US subsidiary, FIM (USA) Inc. is located at 780 Third Avenue; New York, NY 10017; telephone # 212.223.7321 or fax # 212.223.7592.

F. During a 2002 marketing trip to Europe every hedge fund FOF I met with in Paris and Geneva had investments with BM. They all said he was their best manager! A partial list of money managers and Private Banks that invest in BM is included at the end of this report in Attachment 3.

4. Here's what smells bad about the idea of providing equity tranch funding to a US registered broker-dealer:

   A. The investment returns passed along to the third party hedge funds are equivalent to BM borrowing money. These 12 month returns from 1990 – May 2005 ranged from a low of 6.23% to a high of 19.98%, with an average 12 month return during that time period of 12.00%. Add in the 4% in average annual management & participation fees and BM would have to be delivering average annual returns of 16% in order for the investors to receive 12%. No Broker-Dealer that I've ever heard of finances its operations at that high of an implied borrowing rate (source: Attachment 1; Fairfield Sentry Limited return data from December 1990 – May 2005). Ask around and I'm sure you'll find that BM is the only firm on Wall Street that pays an average of 16% to fund its operations.

   B. BD's typically fund in the short-term credit markets and benchmark a significant part of their overnight funding to LIBOR plus or minus some spread. LIBOR + 40 basis points would seem a more realistic borrowing rate for a broker-dealer of BM's size.

   C. **Red Flag # 2**: *why would a BD choose to fund at such a high implied interest rate when cheaper money is available in the short-term credit markets? One reason that comes to mind is that BM couldn't stand the due diligence scrutiny of the short-term credit markets. If Charles Ponzi had issued bank notes promising 50% interest on 3 month time deposits instead of issuing unregulated Ponzi Notes to his investors, the State Banking Commission would have quickly shut him down. The key to a successful Ponzi Scheme is to promise lucrative returns but to do so in an unregulated area of the capital markets. Hedge funds are not due to fall under the SEC's umbrella until February 2006.*

5. The third party hedge funds and fund of funds that market this hedge fund strategy that invests in BM don't name and aren't allowed to name Bernie Madoff as the actual manager in their performance summaries or marketing literature. Look closely at Attachment 1, Fairfield Sentry Ltd.'s performance summary and you won't see BM's name anywhere on the document, yet BM is the actual hedge fund manager with discretionary trading authority over all funds, as agent.

   Red Flag # 3: ***Why the need for such secrecy?*** *If I was the world's largest hedge fund and had great returns, I'd want all the publicity I could garner and would want to appear as the world's largest hedge fund in all of the industry rankings. Name one mutual fund company, Venture Capital firm, or LBO firm which doesn't brag about the size of their largest funds' assets under management. Then ask yourself, why would the world's* *largest hedge fund manager be so secretive that he didn't even want his investors to know he was managing their money? Or is it that BM doesn't want the SEC and FSA to know that he exists?*

6. The third party FOF's never tell investors who is actually managing their money and describe the investment strategy as: This hedge fund's objective is long term growth on a consistent basis with low volatility. The investment advisor invests exclusively in the U.S. and utilizes a strategy often referred to as a "split-strike conversion." Generally this style involves purchasing a basket of 30 – 35 large-capitalization stocks with a high degree of correlation to the general market (e.g. American Express, Boeing, Citigroup, Coca-Cola, Dupont, Exxon, General Motors, IBM, Merck, McDonalds). To provide the desired hedge, the manager then sells out-of-the-money OEX index call options and buys out-of-the-money OEX index put options. The amount of calls that are sold and puts that are bought represent a dollar amount equal to the basket of shares purchases.
7. I personally have run split-strike conversion strategies and know that BM's approach is far riskier than stated in 6 above. His strategy is wholly inferior to an all index approach and is wholly incapable of generating returns in the range of 6.23% to 19.98%. <u>BM's strategy should not be able beat the return on US Treasury Bills</u> Due to the glaring weakness of the strategy:
    A. <u>Income Part of the strategy</u> is to buy 30 – 35 large-cap stocks, sell out-of-the-money index call options against the value of the stock basket. There are three possible sources of income in this strategy.
        1) We earn income from the stock's dividends. Let's attribute a 2% average return to this source of funds for the 14 ½ year time period. This explains 2% of the 16% average gross annual returns before fees and leaves 14% of the returns unexplained.
        2) We earn income from the sale of OTC OEX index call options. Let's also assume that we can generate an additional 2% annual return via the sale of OTC out-of-the-money OEX index call options which leaves 12% of the 16% gross returns unexplained. On Friday, October 14, 2005 the OEX (S&P 100) index closed at 550.49 and there were only 163,809 OEX index call option contracts outstanding (termed the "open interest"). 163,809 call option calls outstanding x $100 contact multiplier x 550.49 index closing price = $9,017, 521,641 in stock equivalents hedged.
        3) We can earn income from capital gains by selling the stocks that go up in price. This portion of the return stream would have to earn the lion's share of the hedge fund strategy's returns. We have 12% of the return stream unexplained so far. However, the OTC OEX index puts that we buy will cost AT LEAST <8%> per year (a lot more in most years but I'm giving BM the benefit of every doubt here). Therefore, BM's stock selection would have to be earning an average of 20% per year. That would mean that he's been the world's best stock-picker since 1990 beating out such luminaries as Warren Buffet and Bill Miller. Yet no one's ever heard of BM as being a stock-picker, much less the world's best stock-picker. Why isn't he famous if he was able to earn 20% average annual returns?

Red Flag # 4: *$9.017 billion in total OEX listed call options outstanding is not nearly enough to generate income on BM's total amount of assets under management which I estimate to range between $20 - $50 billion. Fairfield Sentry Ltd. alone has $5.1 billion with BM. And, while BM may say he only uses Over-the-Counter(OTC) index options, there is no way that this is possible. The OTC market should never be several times larger than the exchange listed market for this type of plain vanilla derivative.*

B. Protection Part of the strategy is to buy out-of-the-money OEX index put options. This costs you money each and every month. This hurts your returns and is the main reason why BM's strategy would have trouble earning 0% average annual returns much less the 12% net returns stated in Fairfield Sentry Ltd.'s performance summary. Even if BM earns a 4% return from the combination of 2% stock dividends and 2% from the sale of call options, the cost of the puts would put this strategy in the red year in and year out. No way he can possibly be delivering 12% net to investors. The math just doesn't support this strategy if he's really buying index put options.

Red Flag # 5: *BM would need to be purchasing at-the-money put options because he has only 7 small monthly losses in the past 14 ½ years. His largest monthly loss is only <0.55%>, so his puts would have to be at-the-money. At-the-money put options are very, very expensive. A one-year at-the-money put option would cost you <8%> or more, depending upon the market's volatility. And <8%> would be a cheap price to pay in many of the past 14 ½ years for put protection!! Assuming BM only paid< 8%> per year in put protection, and assuming he can earn +2% from stock dividends plus another +2% from call option sales, he's still under-water <4%> performance wise. <8%> put cost + 2% stock dividends + 2% income from call sales = <4%>. And, I've proven that BM would need to be earning at least 16% annually to deliver 12% after fees to investors. That means the rest of his returns would have to be coming from stock selection where he picked and sold winning stocks to include in his 35-stock basket of large-cap names. Lots of luck doing that during the past stock market crises like 1997's Asian Currency Crises, the 1998 Russian Debt / LTCM crises, and the 2000-2002 killer bear market. And index put option protection was a lot more expensive during these crises periods than 8%. Mathematically none of BM's returns listed in Attachment 1 make much sense. They are just too unbelievably good to be true.*

C. The OEX index (S&P 100) closed at 550.49 on Friday, October 14, 2005 meaning that each put option hedged $55,049 dollars worth of stock ($100 contract multiplier x 550.49 OEX closing index price = $55,049 in stock hedged). As of that same date, the total open interest for OEX index put options was 307,176 contracts meaning that a total of $16,909,731,624 in stock was being hedged by the use of OEX index puts (307,176 total put contracts in existence as of Oct 14th x $55,049 hedge value of 1 OEX index put = $16,909,731,624 in stock hedged). Note: I excluded a few thousand OEX LEAP index put options from my calculations because these are long-term options and not relevant for a split-strike conversion strategy such as BM's.

Red Flag # 6: *At my best guess level of BM's assets under management of $30 billion, or even at my low end estimate of $20 billion in assets under management,* *BM would have to be over 100% of the total OEX put option contract open interest in order to hedge his stock holdings as depicted in the third party hedge funds marketing literature. In other words, there are not enough index option put contracts in existence to hedge the way BM says he is hedging! And there is no way the OTC market is bigger than the exchange listed market for plain vanilla S&P 100 index put options.*

D. Mathematically I have proven that BM cannot be hedging using listed index put and call options. One hedge fund FOF has told me that BM uses only Over-the-Counter options and trades exclusively thru UBS and Merrill Lynch. I have not called those two firms to check on this because it seems implausible that a BD would trade $20 - $50 billion worth of index put options per month over-the-counter thru only 2 firms. That plus the fact that if BM was really buying OTC index put options, then there is no way his average annual returns could be positive!! At a minimum, using the cheapest way to buy puts would cost a fund <8%> per year. To get the put cost down to <8%>, BM would have to buy a one-year at-the-money put option and hold it for one-year. No way his call sales could ever hope to come even fractionally close to covering the cost of the puts.

   Red Flag # 7: *The counter-party credit exposures for UBS and Merrill would be too large for these firms credit departments to approve. The SEC should ask BM for trade tickets showing he has traded OTC options thru these two firms. Then the SEC should visit the firms' OTC derivatives desks, talk the to heads of trading and ask to see BM's trade tickets. Then ask the director of operations to verify the tickets and ask to see the inventory of all of the stock and listed options hedging the OTC puts and calls. If these firms can't show you the off-setting hedged positions then they are assisting BM as part of a conspiracy to commit fraud. If any other brokerage firms equity derivatives desk is engaged in a conspiracy to cover for BM, then this scandal will be a doozy when it hits the financial press but at least investors would have firms with deep pockets to sue.*

   Red Flag # 8: *OTC options are more expensive to trade than listed options. You have to pay extra for the customization features and secrecy offered by OTC options. Trading in the size of $20 - $50 billion per month would be impossible and the bid-ask spreads would be so wide as to preclude earning any profit whatsoever. These Broker/Dealers would need to offset their short OTC index put option exposure to a falling stock market by hedging out their short put option risk by either buying listed put options or selling short index futures and the derivatives markets are not deep and liquid enough to accomplish this without paying a penalty in prohibitively expensive transaction costs.*

   Red Flag # 9: *Extensive and voluminous paperwork would be required to keep track of and clear each OTC trade. Plus, why aren't Goldman, Sachs and Citigroup involved in handling BM's order flow? Both Goldman and Citigroup are a lot larger in the OTC derivatives markets than UBS or Merrill Lynch.*

E. My experience with split-strike conversion trades is that the best a good manager is likely to obtain using the strategy marketed by the third-party FOF's is T-bills less management fees. And, if the stock market is down by more than 2%, the return from this strategy will range from a high of zero return to a low of a few percent depending upon your put's cost and how far out-of-the-money it is.

F. In 2000 I ran a regression of BM's hedge fund returns using the performance data from Fairfield Sentry Limited. BM had a .06 correlation to the equity market's return which confirms the .06 Beta that Fairfield Sentry Limited lists in its return numbers.

Red Flag # 10: *It is mathematically impossible for a strategy using index call options and index put options to have such a low correlation to the market where its returns are supposedly being generated from. This makes no sense! The strategy depicted retains 100% of the single-stock downside risk since they own only index put options and not single stock put options. Therefore if one or more stocks in their portfolio were to tank on bad news, BM's index put would offer little protection and their portfolio should feel the pain. However, BM's performance numbers show only 7 extremely small losses during 14 ½ years and these numbers are too good to be true. The largest one month loss was only -55 basis points (-0.55%) or just over one-half of one percent! And BM never had more than a one month losing streak! Either BM is the world's best stock and options manager that the SEC and the investing public has* **never** *heard of or he's a fraud. You would have to figure that at some point BM owned a WorldCom, Enron, GM or HealthSouth in their portfolio when bad or really bad news came out and caused these stocks to drop like a rock.*

8. **Red Flag # 11** *Two press articles, which came to print well after my initial May 1999 presentation to the SEC, do doubt Bernie Madoff's returns and they are:*

A. The May 7, 2001 edition of Barron's, in an article entitled, ***"Don't Ask, Don't Tell; Bernie Madoff is so secretetive, he even asks his investors to keep mum,"*** written by Erin Arvedlund, published an expose about Bernie Madoff a few years ago with no resulting investigation by any regulators. Ms. Arvedlund has since left Barron's. I have attached a copy of the Barrons' article which lists numerous red flags.

B. Michael Ocrant, formerly a reporter for MAR Hedge visited Bernie Madoff's offices and wrote a very negative article entitled, "Madoff tops charts; skeptics ask how," that doubted the source of BM's returns. This article was published on May 1, 2001 and is attached (see Attachment 5). Mr. Ocrant has graciously agreed to cooperate fully with the SEC and awaits the SEC's telephone call to arrange a meeting. The SEC should contact him directly. Michael Ocrant is currently serving as the Director of Alternative Investments; Institutional Investor; New York, NY 10001; Telephone # 212-224-3821 or 212-213-6202; Email: mocrant@iiconferences.com

9. Fund of funds with whom I have spoken to that have BM in their stable of funds continually brag about their returns and how they are generated thanks to BM's access to his broker-dealer's access to order flow. They believe that BM has perfect knowledge of the market's direction due to his access to customer order flow into his broker-dealer.

Red Flag # 12: *Yes, BM has access to his customer's order flow thru his broker-dealer but he is only one broker out of many, so it is impossible for him to know the market's direction to such a degree as to only post monthly losses once every couple of years. All of Wall Street's big wire houses experience trading losses on a more regular frequency* *that BM. Ask yourself how BM's trading experience could be so much better than all of the other firms on Wall Street. Either he's the best trading firm on the street and rarely ever has large losing months unlike other firms or he's a fraud.*

10. **Red Flag # 13:** *I believe that BM's returns can be real ONLY if they are generated from front-running his customer's order flow. In other words, yes, if he's buying at a penny above his customer's buy orders, he can only lose one penny if the stock drops but can make several pennies if the stock goes up. For example, if a customer has an order to buy 100,000 shares of IBM at $100, BM can put in his own order to buy 100,000 share of IBM at $100.01. This is what's known as a right-tail distribution and is very similar to the payoff distribution of a call option. Doing this could easily generate returns of 30% - 60% or more per anum. He could be doing the same thing by front-running customer sell orders. However, if BM's returns are real but he's generating them from front-running there are two problems with this:*
    A. *Problem # 1: front-running is one form of insider-trading and is illegal*
    B. *Problem # 2: generating real returns from front-running but telling hedge fund investors that you are generating the returns via a complex (but unworkable) stock and options strategy is securities fraud.*

Some time ago, during different market conditions, I ran a study using the Black-Scholes Option Pricing Model to analyze the value of front-running with the goal of putting a monetary value on front-running where the insider knew the customer's order and traded ahead of it. When I ran the study the model inputs were valued at: OEX component stocks annualized volatility on a cap-weighted basis was 50% (during a bear market period), the T-bill rate was 5.80%, and the average stock price was $46. I then calculated the value of an at-the-money call options over time intervals of 1 minute, 5 minutes, 10 minutes, and 15 minutes. I used a 253 trading day year. The SEC should be able to duplicate these results:

1 minute option = 3 cents worth of trade information value
5 minute option = 7 cents worth of trade information value
10 minute option = 10 cents worth of trade information value
15 minute option = 12 cents worth of trade information value

Conclusion: Bernie Madoff used to advertise in industry trade publications that he would pay 1 cent per share for other broker's order flow. If he was paying 1 cent per share for order flow and front-running these broker's customers, then he could easily be earning returns in the 30% - 60% or higher annually. In all time intervals ranging from 1 minute to 15 minutes, having access to order flow is the monetary equivalent of owning a valuable call option on that order. The value of these implicit call options ranges between 3 – 12 times the one penny per share paid for access to order flow. If this is what he's doing, then the returns are real but the stated investment strategy is illegal and based solely on insider-trading.

NOTE: I am pretty confident that BM is a Ponzi Scheme, but in the off chance he is front-running customer orders and his returns are real, then this case qualifies as insider-trading under the SEC's bounty program as outlined in Section 21A(e) of the 1934 Act. However, if BM was front-running, a highly profitable activity, then he wouldn't need to borrow funds from investors at 16% implied interest. Therefore it is far more likely that BM is a Ponzi Scheme. Front-running is a very simple fraud to commit and requires only access to inside information. The elaborateness of BM's fund-raising, his need for secrecy, his high 16% average cost of funds, and reliance on a derivatives investment scheme that few investors (or regulators) would be capable of comprehending lead to a weight of the evidence conclusion that this is a Ponzi Scheme.

11. **Red Flag # 14:** *Madoff subsidizes down months! Hard to believe (and I don't believe this) but I've heard two FOF's tell me that they don't believe Madoff can make money in big down months either. They tell me that Madoff "subsidizes" their investors in down months, so that they will be able to show a low volatility of returns. These types of stories are commonly found around Ponzi Schemes. These investors tell me that Madoff only books winning tickets in their accounts and "eats the losses" during months when the market sells off hard. The problem with this is that it's securities fraud to misstate either returns or the volatility of those returns. These FOF professionals who heard BM tell them that he subsidizes losses were professionally negligent in not turning BM into the SEC, FSA and other regulators for securities fraud.*
    Red Flag # 15: *Why would a fund of funds investor believe any broker-dealer that commits fraud in a few important areas – such as misstating returns and misstating volatility of returns – yet believe him in other areas? I'd really like to believe in the tooth fairy, but I don't after catching my mother putting a quarter underneath my pillow one night.*
12. **Red Flag # 16:** *Madoff has perfect market-timing ability. One investor told me, with a straight face, that Madoff went to 100% cash in July 1998 and December 1999, ahead of market declines. He said he knows this because Madoff faxes his trade tickets to his firm and the custodial bank. However, since Madoff owns a broker-dealer, he can generate whatever trade tickets he wants. And, I'll bet very few FOF's ask BM to fax them trade tickets. And if these trade tickets are faxed, have the FOF's then matched them to the time and sales of the exchanges? For example, if BM says he bot 1 million shares of GM, sold $1 million worth of OTC OEX calls and bot $1 million worth of OTC OEX puts, we should see prints somewhere. The GM share prints would show on either the NYSE or some other exchange while the broker-dealers he traded OTC options thru would show prints of the hedges they traded to be able to provide BM with the OTC options at the prices listed on BM's trade tickets.*
13. **Red Flag # 17:** *Madoff does not allow outside performance audits. One London based hedge fund, fund of funds, representing Arab money, asked to send in a team of Big 4 accountants to conduct a performance audit during their planned due diligence. They were told "No, only Madoff's brother-in-law who owns his own accounting firm is allowed to audit performance for reasons of secrecy in order to keep Madoff's proprietary trading strategy secret so that nobody can copy it. Amazingly, this fund of funds then agreed to invest $200 million of their client's money anyway, because the low volatility of returns was so attractive!! Let's see, how many hedge funds have faked an audited performance history?? Wood River is the latest that comes to mind as does the Manhattan Fund but the number of bogus hedge funds that have relied upon fake audits has got to number in the dozens.*

14. **Red Flag # 18**: *Madoff's returns are not consistent with the one publicly traded option income fund with a history as long as Madoff's. In 2000, I analyzed the returns of Madoff and measured them against the returns of the Gateway Option Income Fund (Ticker GATEX). During the 87 month span analyzed, Madoff was down only 3 months versus GATEX being down 26 months. GATEX earned an annualized return of 10.27% during the period studied vs. 15.62% for Bernie Madoff and 19.58% for the S&P 500. GATEX has a more flexible investment strategy than BM, so GATEX's returns should be superior to BM's but instead they are inferior. This makes no sense. How could BM be better using an inferior strategy?*
15. **Red Flag # 19**: *There have been several option income funds that went IPO since August 2004. None of them have the high returns that Bernie Madoff has. How can this be? They use similar strategies only they should be making more than BM in up months because most of these option income funds don't buy expensive index put options to protect their portfolios. Thus the publicly traded option income funds should make more money in up markets and lose more than Madoff in down markets. Hmm....that Madoff's returns are so high yet he buys expensive put options is just another reason to believe he is running the world's largest Ponzi Scheme. A good study for the SEC would be to compare 2005 performance of the new option income funds to Bernie Madoff while accounting for the cost of Bernie's index put option protection. There's no way Bernie can have positive returns in 2005 given what the market's done and where volatility is.*
16. **Red Flag # 20**: *Madoff is suspected of being a fraud by some of the world's largest and most sophisticated financial services firms. Without naming names, here's an abbreviated tally:*
    A. A managing director at Goldman, Sachs prime brokerage operation told me that his firm doubts Bernie Madoff is legitimate so they don't deal with him.

B. From an Email I received this past June 2005 I now suspect that the end is near for BM. All Ponzi Schemes eventually topple of their own weight once they become too large and it now appears that BM is having trouble meeting redemptions and is attempting to borrow sizeable funds in Europe.

ABCDEFGH and I had dinner with a savvy European investor that studies the HFOF market. He stated that both RBC and Socgen have removed Madoff some time ago from approved lists of individual managers used by investors to build their own tailored HFOFs.

More importantly, Madoff was turned down, according to this source, for a borrowing line from a Euro bank, I believe he said Paribas. Now why would Madoff need to borrow more funds? This Euro Investor said that Madoff was in fact running "way over" our suggested $12-14 billion (Fairfield Sentry is running $5.3 BB by themselves!) . Madoff's 12 month returns is about 7% net of the feeder fund's fees. Looks like he is stepping down the pay out.

C. An official from a Top 5 money center bank's FOF told me that his firm wouldn't touch Bernie Madoff with a ten foot pole and that there's no way he's for real.

17. **Red Flag # 21:** *ECN's didn't exist prior to 1998. Madoff makes verbal claims to his third party hedge FOF's that he has private access to ECN's internal order flow, which Madoff pays for, and that this is a substantial part of the return generating process. If this is true, then where did the returns come from in the years 1991 – 1997, prior to the ascendance of the ECN's? Presumably, prior to 1998, Madoff only had access to order flow on the NASDAQ for which he paid 1 cent per share for. He would have no such advantage pre-1998 on the large-*

cap, NYSE listed stocks the marketing literature says he buys (Exxon, McDonalds, American Express, IBM, Merck, etc...).

18. **Red Flag # 22:** *The Fairfield Sentry Limited Performance Chart (Attachment 1) depicted for Bernie Madoff's investment strategy are misleading. The S&P 500 return line is accurate because it is moving up and down, reflecting positive and negative returns. Fairfield Sentry's performance chart is misleading, it is almost a straight line rising at a 45 degree angle. This chart cannot be cumulative in the common usage of the term for reporting purposes, which means "geometric returns." The chart must be some sort of arithmetic average sum, since a true cumulative return line, given the listed monthly returns would be exponentially rising (i.e. curving upward at an increasing rate). My rule of thumb is that if the manager misstates his performance, you can't trust him. Yet somehow Madoff is now running the world's largest, most clandestine hedge fund so clearly investors aren't doing their due diligence. And why does he provide the S&P 500 as his benchmark when he is actually managing using a S&P 100 strategy? Shouldn't the performance line presented be the S&P 100's (OEX) performance?*

19. **Red Flag # 23:** *Why is Bernie Madoff borrowing money at an average rate of 16.00% per anum and allowing these third party hedge fund, fund of funds to pocket their 1% and 20% fees bases upon Bernie Madoff's hard work and brains? Does this make any sense at all? Typically FOF's charge only 1% and 10%, yet BM allows them the extra 10%. Why? And why do these third parties fail to mention Bernie Madoff in their marketing literature? After all he's the manager, don't investors have a right to know who's managing their money?*

20. **Red Flag # 24:** *Only Madoff family members are privy to the investment strategy. Name one other prominent multi-billion dollar hedge fund that doesn't have outside, non-family professionals involved in the investment process. You can't because there aren't any. Michael Ocrant, the former MAR Hedge Reporter listed above saw some highly suspicious red flags during his visit to Madoff's offices and should be interviewed by the SEC as soon as possible.*

21. **Red Flag # 25:** *The Madoff family has held important leadership positions with the NASD, NASDAQ, SIA, DTC, and other prominent industry bodies therefore these organizations would not be inclined to doubt or investigate Madoff Investment Securities, LLC. The NASD and NASDAQ do not exactly have a glorious reputation as vigorous regulators untainted by politics or money.*

22. **Red Flag # 26:** *BM goes to 100% cash for every December 31st year-end according to one FOF invested with BM. This allows for "cleaner financial statements" according to this source. Any unusual transfers or activity near a quarter-end or year-end is a red flag for fraud. Recently, the BD REFCO Securities engaged in "fake borrowing" with Liberty, a hedge fund, that made it appear that Liberty owed REFCO over $400 million in receivables. This allowed REFCO to mask its true debt position and made all of their equity ratios look better than they actually were. And of course, Grant Thorton, REFCO's external auditor missed this $400 million entry. As did the two lead underwriters who were also tasked with due-diligence on the IPO - CSFB and Goldman Sachs. BM uses his brother-in-law as his external auditor, so in this case there isn't even the façade of having an independent and vigilant auditor verifying the accounting entries.*

23. **Red Flag # 27:** *Several equity derivatives professionals will all tell you that the split-strike conversion strategy that BM runs is an outright fraud and cannot possibly achieve 12% average annual returns with only 7 down months during a 14 ½ year time period. Some derivatives experts that the SEC should call to hear their opinions of how and why BM is a fraud and for some insights into the mathematical reasons behind their belief, the SEC should call:*

a. Leon Gross, Managing Director of Citigroup's world-wide equity derivatives research unit; 3rd Floor, 390 Greenwich Street; New York, NY 10013: Tel# 800.492.9833 or 212.723.7873 or leon.j.gross@citigroup.com [Leon can't believe that the SEC hasn't shut down Bernie Madoff yet. He's also amazed that FOF's actually believe this stupid options strategy is capable of earning a positive return much less a 12% net average annual return. He thinks the strategy would have trouble earning 1% net much less 12% net. Leon is a free spirit, so if you ask him he'll tell you but you'd understand it better if you met him at his workplace in a private conference room and tell him he won't need to have Citigroup lawyers present, you're just there for some friendly opinions. He talks derivatives at a high level, so ask simple "yes or no" type questions to start off the interview then drill down.]

b. Walter "Bud"Haslett, CFA; Write Capital Management, LLC; Suite 455; 900 Briggs Road; Mount Laurel, NJ 08065; Tel#: 856.727.1700 or bud.haslett@writecapital.com www.writecapital.com [Bud's firm runs $ hundreds of millions in options related strategies and he knows all of the math.]

c. Joanne Hill, Ph.D.; Vice-President and global head of equity derivatives research, Goldman Sachs (NY), 46th Floor; One New York Plaza, New York, NY 10004; Tel# 212.902.2908 [Again, make sure she doesn't lawyer up or this conversation will be useless to you. Tell her you want her opinion and no one will hold her to it or ever tell she gave the SEC an opinion without legal counsel present.]

24. **Red Flag # 28:** *BM's Sharpe Ratio of 2.55 (Attachment 1: Fairfield Sentry Ltd. Performance Data) is UNBELIEVABLY HIGH compared to the Sharpe Ratios experienced by the rest of the hedge fund industry. The SEC should obtain industry hedge fund rankings and see exactly how outstanding Fairfield Sentry Ltd.'s Sharpe Ratio is. Look at the hedge fund rankings for Fairfield Sentry Ltd. and see how their performance numbers compare to the rest of the industry. Then ask yourself how this is possible and why hasn't the world come to acknowledge BM as the world's best hedge fund manager?*

25. **Red Flag # 29:** *BM tells the third party FOF's that he has so much money under management that he's going to close his strategy to new investments. However, I have met several FOF's who brag about their "special access" to BM's capacity. This would be humorous except that too many European FOF's have told me this same seductive story about their being so close to BM that he'll waive the fact that he's closed his funds to other investors but let them in because they're special. It seems like every single one of these third party FOF's has a "special relationship" with BM.*

26. **Red Flag # 30:** BM's largest one month loss of -0.55% using index puts does not fit in with the prohibitively high cost of the extremely short-dated OTC OEX put options he would have to be buying to protect his portfolio from losses such that those monthly losses never exceeded -0.55% in any one month.

    A. Previously with Red Flag # 4, I mentioned that the cheapest possible put cost for BM would be 8%. That very conservative assumption assumes that he could get away with buying one OTC, at-the-money put per year. However, mathematically that one year at-the-money put would have a delta of .50, meaning that for each 1 point drop in the OEX index, the put's price would only increase .5

of half that amount or 50 cents. Therefore if the market dropped 1.1%, a .50 delta put would increase in price by 0.55%, resulting in a -0.55% loss for the fund.

B. However, for all market drops greater than 1.1%, BM would experience a larger than -0.55% monthly loss and there were numerous instances of monthly market losses greater than -1.1% during the time period.

C. Therefore, BM, in order to limit his losses would be forced to buy a series of shorter dated, higher delta put options with high gamma (a 2nd derivative term denoting that for each $1 change in index price, how much the 1st derivative term delta would change. Gamma is the change in price of Delta and Delta is the change in price of the Option with respect to the Index's Price). If you aren't intimately familiar with calculus, the English translation is that BM would need to be buying a continuing series of 1 day put options because these options and only these options would have the high gamma he would need to ensure that his delta changed rapidly enough to protect his portfolio enough so that he could never experience a greater than 0-0.55% monthly loss. If you've gotten this far, then if a one-year at-the-money OTC OEX index put option cost 8%, a continuing series of 253 (because that's how many trading days are in a year) one-day, at-the-money puts, would cost the square root of 253 or 15.9 times the cost of the one-year put. 15.9 times 8% the one year put's cost = 127.2% is the cost of a continuing series of one-day, at-the-money index put options if a one-year, at-the-money index put's cost is 8%. And this is a very conservative set of calculations! Consider that one would be carrying over stock positions in this strategy over weekends, so therefore you'd want 365 one-day, at-the-money put options and the square root of 365 is 19.1, so a truer cost of put protection would be 19.1 x 8% = 152.8%. That would mean BM's stock picking ability is not only the world's best but that he'd likely have to be an alien from outer-space to be able to pick stocks that went up over 152.8% per year + the 16% gross returns to the HFOF investors + an assumed 4% he's making in commissions. Therefore his stock picking ability would need to return 170% or so per year in order for him to be carrying out his strategy as he says he is in the HFOF third party marketing materials.

D. 170% per year from stock-picking is not likely for any human born on the planet earth so if BM's achieving these types of returns then he may be an alien species from another planet. A DNA test would be sufficient to determine whether this might be the case. However, if BM is an alien being possessing superior stock-picking skills of this magnitude, this would be seen as an unfair advantage in the marketplace and likely would panic the financial markets. Or maybe he's human and just a fraudster – take your pick.

E. Anyone capable of earning 170% per year from stock-picking would not need nor want any investors.

Conclusions:

1. I have presented 174 months (14 ½ years) of Fairfield Sentry's return numbers dating back to December 1990. Only 7 months or 4% of the months saw negative returns. Classify this as "definitely too good to be true!" No major league baseball hitter bats .960, no NFL team has ever gone 96 wins and only 4 losses over a 100 game span, and you can bet everything you own that no money manager is up 96% of the months either. It is inconceivable that BM's largest monthly loss could only be -0.55% and that his longest losing streaks could consist of 1 slightly down month every couple of years. Nobody on earth is that good of a money manager unless they're front-running.

2. There are too many red flags to ignore. REFCO, Wood River, the Manhattan Fund, Princeton Economics, and other hedge fund blow ups all had a lot fewer red flags than Madoff and look what happened at those places.

3. Bernie Madoff is running the world's largest unregistered hedge fund. He's organized this business as "hedge fund of funds private labeling their own hedge funds which Bernie Madoff **secretly** runs for them using a split-strike conversion strategy getting paid only trading commissions which are not disclosed." If this isn't a regulatory dodge, I don't know what is. This is back-door marketing and financing scheme that is opaque and rife with hidden fees (he charges only commissions on the trades). If this product isn't marketed correctly, what is the chance that it is managed correctly? In my financial industry experience, I've found that wherever there's one cockroach in plain sight, many more are lurking behind the corner out of plain view.

4. Mathematically this type of split-strike conversion fund should never be able to beat US Treasury Bills much less provide 12.00% average annual returns to investors net of fees. I and other derivatives professionals on Wall Street will swear up and down that a split-strike conversion strategy cannot earn an average annual return anywhere near the 16% gross returns necessary to be able to deliver 12% net returns to investors.

5. BM would have to be trading more than 100% of the open interest of OEX index put options every month. And if BM is using only OTC OEX index options, it is guaranteed that the Wall Street firms on the other side of those trades would have to be laying off a significant portion of that risk in the exchange listed index options markets. Every large derivatives dealer on Wall Street will tell you that Bernie Madoff is a fraud. Go ask the heads of equity derivatives trading at Morgan Stanley, Goldman Sachs, JP Morgan and Citigroup their opinions about Bernie Madoff. They'll all tell the SEC that they can't believe that BM hasn't been caught yet.

6. The SEC is slated to start overseeing hedge funds in February 2006, yet since Bernie Madoff is not registered as a hedge fund but acting as one but via third party shields, the chances of Madoff escaping SEC scrutiny are very high. If I hadn't written this report, there's no way the SEC would have known to check the facts behind all of these third party hedge funds.

Potential Fall Out if Bernie Madoff turns out to be a Ponzi Scheme:

1. If the average hedge fund is assumed to be levered 4:1, it doesn't take a rocket scientist to realize that there might be anywhere from a few hundred billion on up in selling pressure in the wake of a $20 - $50 billion hedge fund fraud. With the hedge fund market estimated to be $1 trillion, having one hedge fund with 2% - 5% of the industry's assets under management suddenly blow up, it is hard to predict the severity of the resulting shock wave. You just know it'll be unpleasant for anywhere from a few days to a few weeks but the fall out shouldn't be anywhere near as great as that from the Long Term Capital Management Crises. Using the hurricane scale with which we've all become quite familiar with this year, I'd rate BM turning out to be a Ponzi Scheme as a Category 2 or 3 hurricane where the 1998 LTCM Crises was a Category 5.

2. Hedge fund, fund of funds with greater than a 10% exposure to Bernie Madoff will likely be faced with forced redemptions. This will lead to a cascade of panic selling in all of the various hedge fund sectors whether equity related or not. Long –short and market neutral managers will take losses as their shorts rise and their longs fall. Convertible arbitrage managers will lose as the long positions in underlying bonds are sold and the short equity call options are bought to close. Fixed income arbitrage managers will also face losses as credit spreads widen. Basically, most hedge funds categories with two exceptions will have at least one big down month thanks to the unwinding caused by forced redemptions. Dedicated Short Funds and Long Volatility Funds are the two hedge fund categories that will do well.

3. The French and Swiss Private Banks are the largest investors in Bernie Madoff. This will have a huge negative impact on the European capital markets as several large fund of funds implode. I figure one-half to three-quarters of Bernie Madoff's funds come from overseas. The unwinding trade will hurt all markets across the globe but it is the Private European Banks that will fare the worst.

4. European regulators will be seen as not being up to the task of dealing with hedge fund fraud. Hopefully this scandal will serve as a long overdue wake-up call for them and result in increased funding and staffing levels for European Financial Regulators.

5. In the US Fairfield Sentry, Broyhill, Access International Advisors, Tremont and several other hedge fund, fund of funds will all implode. There will be a call for increased hedge fund regulation by scared and battered high net worth investors.

6. The Wall Street wire house FOF's are not invested in Madoff's strategy. As far as I know the wire house's internal FOF's all think he's a fraud and have avoided him like the

plague. But these very same wire houses often own highly profitable hedge fund prime brokerage operations and these operations will suffer contained, but painful nonetheless, losses from loans to some hedge funds that go bust during the panic selling. As a result, I predict that some investment banks will pull out of the prime brokerage business deeming it too volatile from an earnings standpoint. Damage to Wall Street will be unpleasant in that hedge funds and FOF's are a big source of trading revenues. If the hedge fund industry fades, Wall Street will need to find another revenue source to replace them.

7. US Mutual fund investors and other long-term investors in main stream investment products will only feel a month or two's worth of pain from the selling cascade in the hedge fund arena but their markets should recover afterwards.

8. Congress will be up in arms and there will be Senate and House hearings just like there were for Long Term Capital Management.

9. The SEC's critics who say the SEC shouldn't be regulating private partnerships will be forever silenced. Hopefully this leads to expanded powers and increased funding for the SEC. Parties that opposed SEC entry into hedge fund regulation will fall silent. The SEC will gain political strength in Washington from this episode but only if the SEC is proactive and launches an immediate, full scale investigation into all of the Red Flags surrounding Madoff Investment Securities, LLC. Otherwise, it is almost certain that NYAG Elliot Spitzer will launch his investigation first and once again beat the SEC to the punch causing the SEC further public embarrassment.

10. Hedge funds will face increased due diligence from regulators, investors, prime brokers and counter-parties which is a good thing and long overdue.

Potential Fall Out if Bernie Madoff is found out to be front-running customer order flow:

1. This would be just one more black eye among many for the brokerage industry and the NYSE and NASDAQ. At this point the reputations of both the NYSE and NASDAQ are already at rock bottom, so there's likely little downside left for these two troubled organizations.

2. The industry wouldn't miss a beat other than for the liquidation of Madoff Investment Securities, LLC. Figure it will be similar to REFCO's demise only there won't be a buyer of the firm given that they cheated customers who would all be embarrassed to remain customers once the news they've been ripped off is on the front-pages. These former customers are more likely to sue for damages than remain customers. Unsecured lenders would face losses but other than that the industry would be better off.

3. At least the returns are real, in which case determining restitution could keep the courts busy for years. The Class Action Bar would be thrilled. A lot of the FOF's are registered offshore in places where the long arm of the law might not reach. My guess is that the fight for the money off-shore would keep dozens of lawyers happily employed for many years.

4. The FOF's would suffer little in the way of damage. All could be counted on to say "*We didn't know the manager was generating returns illegally. We relied upon the NYSE and NASDAQ to regulate their markets and prevent front-running therefore we see no reason to return any funds.*"

Attachments:

1. 2 page Summary of Fairfield Sentry Ltd with performance data from December 1990 – May 2005

2. Copy of the May 7, 2001 Barrons' article, ***"Don't Ask, Don't Tell; Bernie Madoff is so secretetive, he even asks his investors to keep mum,"*** written by Erin E. Arvedlund.

3. Partial list of French and Swiss money-managers and private banks with investments in Bernie Madoff's hedge fund. Undoubtedly there are dozens more European FOF's and Private Banks that are invested with BM.

4. 2 page offering memorandum, faxed March 29, 2001, for an investment in what I believe is Fairfield Sentry Ltd., one of several investment programs run by Madoff Investment

Securities, LLC for third party hedge fund, fund of funds. I do not know who the source was who faxed this document since the fax heading is blank. The document number listed at the bottom of the page appears to read I:\Data\WPDOCS|AG_\94021597

ATTACHMENT 1: Fairfield Sentry Performance Data

Fairfield Sentry Ltd

Fund Category(s):
Long/Short Equity

Strategy Description:
The Fund seeks to obtain capital appreciation of its assets principally through the utilization of a nontraditional options trading strategy described as "split strike conversion", to which the Fund allocates the predominant portion of its assets. This strategy has defined risk and profit parameters, which may be ascertained when a particular position is established. Set forth below is a description of the "split strike conversion" strategies ("SSC Investments"). The establishment of a typical position entails (i) the purchase of a group or basket of equity securities that are intended to highly correlate to the S&P 100 Index, (ii) the sale of out-of-the-money S&P 100 Index call options in an equivalent contract value dollar amount to the basket of equity securities, and (iii) the purchase of an equivalent number of out-of-the-money S&P 100 Index put options. An index call option is out-of-the-money when its strike price is greater than the current price of the index; an index put option is out-of-the-money when the strike price is lower than the current price of the index. The basket typically consists of approximately 35 to 45 stocks in the S&P 100. The logic of this strategy is that once a long stock position has been established, selling a call against such long position will increase the standstill rate of return, while allowing upward movement to the short call strike price. The purchase of an out-of-the-money put, funded with part or all of the call premium, protects the equity position from downside risk. A bullish or bearish bias of the positions can be achieved by adjustment of the strike prices in the S&P 100 puts and calls. The further away the strike prices are from the price of the S&P 100, the more bullish the strategy. However, the dollar value underlying the put options always approximates the value of the basket of stocks.

Contact Info		Fees & Structure	
Fund:	Fairfield Sentry Ltd	Fund Assets:	$5100.00million
General Partner:	Arden Asset Management	Strategy Assets:	$5300.00million
Address:	919 Third Avenue 11th th Floor New York NY 10022 USA	Firm Assets:	$8300million
		Min. Investment:	$ 0.10million
		Management Fee:	1.00%
		Incentive Fee:	20.00%
Tel:	212-319-6060	Hurdle Rate:	
Fax:		High Water Mark:	Yes
Email:	fairfieldfunds@fggus.com	Additions:	Monthly
Contact Person:	Fairfield Funds	Redemptions:	Monthly
Portfolio Manager:		Lockup:	
		Inception Date:	Dec-1990
		Money Invested In:	United States
		Open to New Investments:	Yes

Annual Returns

1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
2.83%	18.58%	14.67%	11.68%	11.49%	12.95%	12.99%	14.00%	13.40%	14.18%	11.55%	10.68%	9.33%	8.21%	7.07%	2.52%

Year To Date:	2.52%
Highest 12 Month Return:	19.98%
Lowest 12 Month Return:	6.23%
Average Annual Return:	**12.00%**
Average Monthly Return:	0.96%
Highest Monthly Return:	3.36%
Lowest Monthly Return:	**-0.55%**
Average Gain:	1.01%
Average Loss:	-0.24%
Profitable Percentage:	**95.98%**
Compounded Monthly Return:	0.96%
Longest Losing Streak:	**1 mo.**

Sharpe Ratio (Rolling 12):	2.56
Sharpe Ratio (Annualized):	**2.55**
Std. Dev. (Monthly):	0.75%
Std. Dev. (Rolling 12):	2.74%
Beta:	**0.06**
Alpha:	0.91
R:	0.30
R Squared:	0.09

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
1990	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	2.83% E
1991	3.08% E	1.46% E	0.59% E	1.39% E	1.88% E	0.37% E	2.04% E	1.07% E	0.80% E	2.82% E	0.08% E	1.63% E
1992	0.49% E	2.79% E	1.01% E	2.86% E	**-0.19%**	1.29% E	0.00% E	0.92% E	0.40% E	1.40% E	1.42% E	1.43% E
1993	0.00% E	1.93% E	1.86% E	0.06% E	1.72% E	0.86% E	0.09% E	1.78% E	0.35% E	1.77% E	0.26% E	0.45% E
1994	2.18% E	**-0.36%**	1.52% E	1.82% E	0.51% E	0.29% E	1.78% E	0.42% E	0.82% E	1.88% E	**-0.55%**	0.66% E
1995	0.92% E	0.76% E	0.84% E	1.69% E	1.72% E	0.50% E	1.08% E	**-0.16%**	1.70% E	1.60% E	0.51% E	1.10% E
1996	1.49% E	0.73% E	1.23% E	0.64% E	1.41% E	0.22% E	1.92% E	0.27% E	1.22% E	1.10% E	1.58% E	0.48% E
1997	2.45% E	0.73% E	0.86% E	1.17% E	0.63% E	1.34% E	0.75% E	0.35% E	2.39% E	0.55% E	1.56% E	0.42% E
1998	0.91% E	1.29% E	1.75% E	0.42% E	1.76% E	1.28% E	0.83% E	0.28% E	1.04% E	1.93% E	0.84% E	0.33% E
1999	2.06% E	0.17% E	2.29% E	0.36% E	1.51% E	1.76% E	0.43% E	0.94% E	0.73% E	1.11% E	1.61% E	0.39% E
2000	2.20% E	0.20% E	1.84% E	0.34% E	1.37% E	0.80% E	0.65% E	1.32% E	0.25% E	0.92% E	0.68% E	0.43% E

2002	0.03% E	0.60% E	0.46% E	1.16% E	2.12% E	0.26% E	3.36% E	-0.06%	0.13% E	0.73% E	0.16% E	0.06% E
2003	**-0.27%**	0.04% E	1.97% E	0.10% E	0.95% E	1.00% E	1.44% E	0.22% E	0.93% E	1.32% E	**-0.08%**	0.32% E
2004	0.94% E	0.50% E	0.05% C	0.43% C	0.66% C	1.28% C	0.08% C	1.33% E	0.53% E	0.03% E	0.79% E	0.24% E

END ATTACHMENT # 1 FAIRFIELD SENTRY LTD. PERFORMANCE DATA

Attachment 2: Barron's Article dated May 7, 2001

"Don't Ask, Don't Tell"

Bernie Madoff is so secretive, he even asks investors to keep mum

By ERIN E. ARVEDLUND
Barron's | Monday, May 7, 2001

Two years ago, at a hedge-fund conference in New York, attendees were asked to name some of their favorite and most-respected hedge-fund managers. Neither George Soros nor Julian Robertson merited a single mention. But one manager received lavish praise: Bernard Madoff.

Folks on Wall Street know Bernie Madoff well. His brokerage firm, Madoff Securities, helped kick-start the Nasdaq Stock Market in the early 1970s and is now one of the top three market makers in Nasdaq stocks. Madoff Securities is also the third-largest firm matching buyers and sellers of New York Stock Exchange-listed securities. Charles Schwab, Fidelity Investments and a slew of discount brokerages all send trades through Madoff.

Some folks on Wall Street think there's more to how Madoff (above) generates his enviable stream of investment returns than meets the eye. Madoff calls these claims "ridiculous."

But what few on the Street know is that Bernie Madoff also manages $6 billion-to-$7 billion for wealthy individuals. That's enough to rank Madoff's operation among the world's three largest hedge funds, according to a May 2001 report in MAR Hedge, a trade publication.

What's more, these private accounts, have produced compound average annual returns of 15% for more than a decade. Remarkably, some of the larger, billion-dollar Madoff-run funds have never had a down year.

When Barron's asked Madoff Friday how he accomplishes this, he said, "It's a proprietary strategy. I can't go into it in great detail."

Nor were the firms that market Madoff's funds forthcoming when contacted earlier. "It's a private fund. And so our inclination has been not to discuss its returns," says Jeffrey Tucker, partner and co-founder of Fairfield Greenwich, a New York City-based hedge-fund marketer. "Why Barron's would have any interest in this fund I don't know." One of Fairfield Greenwich's most sought-after funds is Fairfield Sentry Limited. Managed by Bernie Madoff, Fairfield Sentry has assets of $3.3 billion.

A Madoff hedge-fund offering memorandums describes his strategy this way: "Typically, a position will consist of the ownership of 30-35 S&P 100 stocks, most correlated to that index, the

sale of out-of-the-money calls on the index and the purchase of out-of-the-money puts on the index. The sale of the calls is designed to increase the rate of return, while allowing upward movement of the stock portfolio to the strike price of the calls. The puts, funded in large part by the sale of the calls, limit the portfolio's downside."

Among options traders, that's known as the "split-strike conversion" strategy. In layman's terms, it means Madoff invests primarily in the largest stocks in the S&P 100 index -- names like General Electric, Intel and Coca-Cola. At the same time, he buys and sells options against those stocks. For example, Madoff might purchase shares of GE and sell a call option on a comparable number of shares -- that is, an option to buy the shares at a fixed price at a future date. At the same time, he would buy a put option on the stock, which gives him the right to sell shares at a fixed price at a future date.

The strategy, in effect, creates a boundary on a stock, limiting its upside while at the same time protecting against a sharp decline in the share price. When done correctly, this so-called market-neutral strategy produces positive returns no matter which way the market goes.

Using this split-strike conversion strategy, Fairfield Sentry Limited has had only four down months since inception in 1989. In 1990, Fairfield Sentry was up 27%. In the ensuing decade, it returned no less than 11% in any year, and sometimes as high as 18%. Last year, Fairfield Sentry returned 11.55% and so far in 2001, the fund is up 3.52%.

Those returns have been so consistent that some on the Street have begun speculating that Madoff's market-making operation subsidizes and smooths his hedge-fund returns.

How might Madoff Securities do this? Access to such a huge capital base could allow Madoff to make much larger bets -- with very little risk -- than it could otherwise. It would work like this: Madoff Securities stands in the middle of a tremendous river of orders, which means that its traders have advance knowledge, if only by a few seconds, of what big customers are buying and selling. By hopping on the bandwagon, the market maker could effectively lock in profits. In such a case, throwing a little cash back to the hedge funds would be no big deal.

When Barron's ran that scenario by Madoff, he dismissed it as "ridiculous."

Still, some on Wall Street remain skeptical about how Madoff achieves such stunning double-digit returns using options alone. The recent MAR Hedge report, for example, cited more than a dozen hedge fund professionals, including current and former Madoff traders, who questioned why no one had been able to duplicate Madoff's returns using this strategy. Likewise, three option strategists at major investment banks told Barron's they couldn't understand how Madoff churns out such numbers. Adds a former Madoff investor: "Anybody who's a seasoned hedge-fund investor knows the split-strike conversion is not the whole story. To take it at face value is a bit naïve."

Madoff dismisses such skepticism. "Whoever tried to reverse-engineer \, he didn't do a good job. If he did, these numbers would not be unusual." Curiously, he charges no fees for his money-management services. Nor does he take a cut of the 1.5% fees marketers like Fairfield

Greenwich charge investors each year. Why not? "We're perfectly happy to just earn commissions on the trades," he says.

Perhaps so. But consider the sheer scope of the money Madoff would appear to be leaving on the table. A typical hedge fund charges 1% of assets annually, plus 20% of profits. On a $6 billion fund generating 15% annual returns, that adds up to $240 million a year.

The lessons of Long-Term Capital Management's collapse are that investors need, or should want, transparency in their money manager's investment strategy. But Madoff's investors rave about his performance -- even though they don't understand how he does it. "Even knowledgeable people can't really tell you what he's doing," one very satisfied investor told Barron's. "People who have all the trade confirmations and statements still can't define it very well. The only thing I know is that he's often in cash" when volatility levels get extreme. This investor declined to be quoted by name. Why? Because Madoff politely requests that his investors not reveal that he runs their money.

"What Madoff told us was, 'If you invest with me, you must never tell anyone that you're invested with me. It's no one's business what goes on here,'" says an investment manager who took over a pool of assets that included an investment in a Madoff fund. "When he couldn't explain \ how they were up or down in a particular month," he added, "I pulled the money out."

For investors who aren't put off by such secrecy, it should be noted that Fairfield and Kingate Management both market funds managed by Madoff, as does Tremont Advisers, a publicly traded hedge-fund advisory firm.

URL for this article:
http://online.barrons.com/article/SB989019667829349012.html

END ATTACHMENT # 2 BARRON'S ARTICLE

ATTACHMENT 4

Copy of a Fax dated March, 21, 2001 3:57 p.m. from an unknown sender (I forgot who sent it) that explains the Use of Proceeds and Investment Program offered by Fairfield Sentry Ltd but managed by Bernie Madoff. The fax machine header reads NO.880______P.1_______ so it is impossible for me to identify the source at this time. This looks to be pages 6 and 7 of an offering memorandum. I would be happy to turn over my original fax copy to the SEC. The document number listed on both pages is a bit blurry but appears to read I:\DATA\WPDOCS|AG_\94021597

USE OF PROCEEDS

The entire net proceeds from the sale of the interests will be available to the Partnership. The Partnership incurred approximately $5,000 in connection with the initial offering of Interests for the admission of Limited Partners (such costs consisting primarily of legal fees and blue sky filing fees. The General Partners do no intent to pay any commissions or fees to broker-dealers in connection with the offering. However, in the event any fees or commissions are paid, they will be paid by the General Partners rather than the Partnership. The General Partners have not established any maximum amounts for such fees and commissions, none of which have been paid or earned to date.

The Partnership's funds are allocated to an account at Bernard L. Madoff Investment Securities (see "INVESTMENT PROGRAM"). Funds not so allocated will be maintained in cash. Bernard L. Madoff Securities is employed solely as an agent of the Partnership. It has no ownership interest in the Partnership and no role in the overall management of the Partnership.

The Partnership will not make any loans to affiliated entities nor will it invest in any foreign government securities.

INVESTMENT PROGRAM

The Partnership seeks to obtain capital appreciation of its assets through the utilization of nontraditional options trading strategies. The General Partners have established a discretionary account for the Partnership at Bernard L. Madoff Investment Securities ("BLM"), a registered broker-dealer in New York, New York, which utilizes a strategy described as a "split strike conversion". This strategy has defined risk and profit parameters which may be ascertained when a particular position is established. All investment decisions in the account at BLM are effected by persons associated with BLM. The firm, which employs approximately 150 people, acts primarily as a market maker in stocks and convertible securities. Most of the stocks for which it acts as a market maker are also listed on the New York Stock Exchange. Set forth below is a description of the "split strike conversion strategies.

The establishment of a typical position entails (i) the purchase of equity shares, (ii) the sale of a related out of the money call option representing an amount of underlying shares equal to the number of equity shares purchased, and (iii) the purchase of a related put option which is at or out of the money. A call option is sold out of the money when its strike price is greater than the current price of the stock; a put option is out of the money when the strike price is lower than the current price of the stock.

The logic of this strategy is that once a long stock position has been established, selling a call against such along position will increase the standstill rate of return, while allowing upward movement to the short call strike price. The purchase of an at or out of the money put, funded with part or all of the call premium, protects the equity position from downside risk.

Equity index options are also utilized in this trading methodology. Such a strategy involves buying a group of equity securities that together will highly correlate to the S&P 100 Index ("the OEX"). Equivalent contract value dollar amounts of out of the money OEX call options are sold, and out of the money OEX put options are purchased, against the basket of stocks. The basket typically consists of approximately 35 stocks in the S&P 100 Index.

A bullish or bearish bias of the positions can be achieved by adjustment of the strike prices in the OEX puts and calls. The further away the strike prices are from the price of the S&P 100 Index, the more bullish the strategy. However, the dollar value underlying the put options always approximates the value of the basket of stocks.

The Partnership bears the cost of all brokerage fees and commissions charged in connection with the account at BLM. All interest earned on credit balances is credited to the Partnership.

BLM acts as principal in connection with its sale of securities to the Partnership, and the purchase of securities from the Partnership. BLM acts as a market-maker in the stocks purchased and sold by the Partnership. These market making activities enable BLM to trade with the Partnership as principal. See "CERTAIN RISK FACTORS".

The options transactions executed for the benefit of Sentry are effected, primarily, in the over-the-counter, not on a registered options exchange.

There can be no assurance that the investment objectives of the Partnership will be achieved. THE PARTNERSHIP'S INVESMENT PROGRAM IS SPECULATIVE AND ENTAILS SUBSTANTIAL RISKS. MARKET RISKS ARE INHERENT IN ALL SECURITIES TO VARYING DEGREES. NO ASSURANCE CAN BE GIVEN THAT THE PARTNERSHIP'S INVESTMENT OBJECTIVE WILL BE REALIZED. (SEE "CERTAIN RISK FACTORS".)

Attachment 5:

May 1, 2001 article published in MAR Hedge

Madoff tops charts; skeptics ask how

By Michael Ocrant

May-1-2001 - Mention Bernard L. Madoff Investment Securities to anyone working on Wall Street at any time over the last 40 years and you're likely to get a look of immediate recognition.

After all, Madoff Securities, with its 600 major brokerage clients, is ranked as one of the top three market makers in Nasdaq stocks, cites itself as probably the largest source of order flow for New York Stock Exchange-listed securities, and remains a huge player in the trading of preferred, convertible and other specialized securities instruments.

Beyond that, Madoff operates one of the most successful "third markets" for trading equities after regular exchange hours, and is an active market maker in the European and Asian equity markets. And with a group of partners, it is leading an effort and developing the technology for a new electronic auction market trading system called Primex.

But it's a safe bet that relatively few Wall Street professionals are aware that Madoff Securities could be categorized as perhaps the best risk-adjusted hedge fund portfolio manager for the last dozen years. Its $6—7 billion in assets under management, provided primarily by three feeder funds, currently would put it in the number one or two spot in the Zurich (formerly MAR) database of more than 1,100 hedge funds, and would place it at or near the top of any well-known database in existence defined by assets.

More important, perhaps, most of those who are aware of Madoff's status in the hedge fund world are baffled by the way the firm has obtained such consistent, nonvolatile returns month after month and year after year.

Madoff has reported positive returns for the last 11-plus years in assets managed on behalf of the feeder fund known as Fairfield Sentry, which in providing capital for the program since 1989 has been doing it longer than any of the other feeder funds. Those other funds have demonstrated equally positive track records using the same strategy for much of that period.

Those who question the consistency of the returns, though not necessarily the ability to generate the gross and net returns reported, include current and former traders, other money managers, consultants, quantitative analysts and fund-of-funds executives, many of whom are familiar with the so-called split-strike conversion strategy used to manage the assets.

These individuals, more than a dozen in all, offered their views, speculation and opinions on the condition that they wouldn't be identified. They noted that others who use or have used the strategy — described as buying a basket of stocks closely correlated to an index, while concurrently selling out-of-the-money call options on the index and buying out-of-the-money put options on the index — are known to have had nowhere near the same degree of success.

The strategy is generally described as putting on a "collar" in an attempt to limit gains compared to the benchmark index in an up market and, likewise, limit losses to something less than the benchmark in a down market, essentially creating a floor and a ceiling.

Madoff's strategy is designed around multiple stock baskets made up of 30—35 stocks most correlated to the S&P 100 index. In marketing material issued by Fairfield Sentry, the sale of the calls is described as increasing "the standstill rate of return, while allowing upward movement of the stock portfolio to the strike price of the calls." The puts, according to the same material, are "funded in large part by the sale of the calls, [and] limit the portfolio's downside.

"A bullish or bearish bias can be achieved by adjusting the strike prices of the options, overweighting the puts, or underweighting the calls. However, the underlying value of the S&P 100 puts is always approximately equal to that of the portfolio of stocks," the marketing document concludes.

Throughout the entire period Madoff has managed the assets, the strategy, which claims to use OTC options almost entirely, has appeared to work with remarkable results.

Again, take the Fairfield Sentry fund as the example. It has reported losses of no more than 55 basis points in just four of the past 139 consecutive months, while generating highly consistent gross returns of slightly more than 1.5% a month and net annual returns roughly in the range of 15.0%.

Among all the funds on the database in that same period, the Madoff/Fairfield Sentry fund would place at number 16 if ranked by its absolute cumulative returns.

Among 423 funds reporting returns over the last five years, most with less money and shorter track records, Fairfield Sentry would be ranked at 240 on an absolute return basis and come in number 10 if measured by risk-adjusted return as defined by its Sharpe ratio.

What is striking to most observers is not so much the annual returns — which, though considered somewhat high for the strategy, could be attributed to the firm's market making and trade execution capabilities — but the ability to provide such smooth returns with so little volatility.

The best known entity using a similar strategy, a publicly traded mutual fund dating from 1978 called Gateway, has experienced far greater volatility and lower returns during the same period.

The capital overseen by Madoff through Fairfield Sentry has a cumulative compound net return of 397.5%. Compared with the 41 funds in the Zurich database that reported for the same historical period, from July 1989 to February 2001, it would rank as the best performing fund for the period on a risk-adjusted basis, with a Sharpe ratio of 3.4 and a standard deviation of 3.0%. (Ranked strictly by standard deviation, the Fairfield Sentry funds would come in at number three, behind two other market neutral funds.)

Bernard Madoff, the principal and founder of the firm who is widely known as Bernie, is quick to note that one reason so few might recognize Madoff Securities as a hedge fund manager is because the firm makes no claim to being one.

The acknowledged Madoff feeder funds — New York-based Fairfield Sentry and Tremont Advisors' Broad Market; Kingate, operated by FIM of London; and Swiss-based Thema — derive all the incentive fees generated by the program's returns (there are no management fees), provide all the administration and marketing for them, raise the capital and deal with investors, says Madoff.

Madoff Securities' role, he says, is to provide the investment strategy and execute the trades, for which it generates commission revenue.

[Madoff Securities also manages money in the program allocated by an unknown number of endowments, wealthy individuals and family offices. While Bernie Madoff refuses to reveal total assets under management, he does not dispute that the figure is in the range of $6 billion to $7 billion.]

Madoff compares the firm's role to a private managed account at a broker-dealer, with the broker-dealer providing investment ideas or strategies and executing the trades and making money off the account by charging commission on each trade.

Skeptics who express a mixture of amazement, fascination and curiosity about the program wonder, first, about the relative complete lack of volatility in the reported monthly returns.

But among other things, they also marvel at the seemingly astonishing ability to time the market and move to cash in the underlying securities before market conditions turn negative; and the related ability to buy and sell the underlying stocks without noticeably affecting the market.

In addition, experts ask why no one has been able to duplicate similar returns using the strategy and why other firms on Wall Street haven't become aware of the fund and its strategy and traded against it, as has happened so often in other cases; why Madoff Securities is willing to earn commissions off the trades but not set up a separate asset management division to offer hedge funds directly to investors and keep all the incentive fees for itself, or conversely, why it doesn't borrow the money from creditors, who are generally willing to provide leverage to a fully hedged portfolio of up to seven to one against capital at an interest rate of Libor-plus, and manage the funds on a proprietary basis.

These same skeptics speculate that at least part of the returns must come from other activities related to Madoff's market making. They suggest, for example, that the bid-ask spreads earned through those activities may at times be used to "subsidize" the funds.

According to this view, the benefit to Madoff Securities is that the capital provided by the funds could be used by the firm as "pseudo equity," allowing it either to use a great deal of leverage without taking on debt, or simply to conduct far more market making by purchasing additional order flow than it would otherwise be able to do.

And even among the four or five professionals who express both an understanding of the strategy and have little trouble accepting the reported returns it has generated, a majority still expresses the belief that, if nothing else, Madoff must be using other stocks and options rather than only those in the S&P 100.

Bernie Madoff is willing to answer each of those inquiries, even if he refuses to provide details about the trading strategy he considers proprietary information.

And in a face-to-face interview and several telephone interviews, Madoff sounds and appears genuinely amused by the interest and attention aimed at an asset management strategy designed to generate conservative, low risk returns that he notes are nowhere near the top results of well-known fund managers on an absolute return basis.

The apparent lack of volatility in the performance of the fund, Madoff says, is an illusion based on a review of the monthly and annual returns. On an intraday, intraweek and intramonth basis, he says, "the volatility is all over the place," with the fund down by as much as 1%.

But as whole, the split-strike conversion strategy is designed to work best in bull markets and, Madoff points out, until recently "we've really been in a bull market since '82, so this has been a good period to do this kind of stuff."

Market volatility, moreover, is the strategy's friend, says Madoff, as one of the fundamental ideas is to exercise the calls when the market spikes, which with the right stock picks would add to the performance.

In the current bearish environment, when some market experts think the fund should have been showing negative returns, albeit at levels below the benchmark index, managing the strategy has become more difficult, says Madoff, although performance has remained positive or, as in February, flat.

The worst market to operate in using the strategy, he adds, would be a protracted bear market or "a flat, dull market." In a stock market environment similar to what was experienced in the 1970s, for instance, the strategy would be lucky to return "T-bill like returns."

Market timing and stock picking are both important for the strategy to work, and to those who express astonishment at the firm's ability in those areas, Madoff points to long experience, excellent technology that provides superb and low-cost execution capabilities, good proprietary stock and options pricing models, well-established infrastructure, market making ability and market intelligence derived from the massive amount of order flow it handles each day.

The strategy and trading, he says, are done mostly by signals from a proprietary "black box" system that allows for human intervention to take into account the "gut feel" of the firm's professionals. "I don't want to get on an airplane without a pilot in the seat," says Madoff. "I only trust the autopilot so much."

As for the specifics of how the firm manages risk and limits the market impact of moving so much capital in and out of positions, Madoff responds first by saying, "I'm not interested in educating the world on our strategy, and I won't get into the nuances of how we manage risk." He reiterates the undisputed strengths and advantages the firm's operations provide that make it possible.

Avoiding market impact by trading the underlying securities, he says, is one of the strategy's primary goals. This is done by creating a variety of stock baskets, sometimes as many as a dozen, with different weightings that allow positions to be taken or unwound slowly over a one- or two-week period.

Madoff says the baskets comprise the most highly capitalized liquid securities in the market, making the entry and exit strategies easier to manage.

He also stresses that the assets used for the strategy are often invested in Treasury securities as the firm waits for specific market opportunities. He won't reveal how much capital is required to be deployed at any given time to maintain the strategy's return characteristics, but does say that "the goal is to be 100% invested."

The inability of other firms to duplicate his firm's success with the strategy, says Madoff, is attributable, again, to its highly regarded operational infrastructure. He notes that one could make the same observation about many businesses, including market making firms.

Many major Wall Street broker-dealers, he observes, previously attempted to replicate established market making operations but gave up trying when they realized how difficult it was to do so successfully, opting instead to acquire them for hefty sums.

[Indeed, says Madoff, the firm itself has received numerous buyout offers but has so far refused any entreaties because he and the many members of his immediate and extended family who work there continue to enjoy what they do and the independence it allows and have no desire to work for someone else.]

Similarly, he adds, another firm could duplicate the strategy in an attempt to get similar results, but its returns would likely be unmatched because "you need the physical plant and a large operation" to do it with equal success. However, many Wall Street firms, he says, do use the strategy in their proprietary trading activities, but they don't devote more capital to such operations because their return on capital is better used in other operations.

Setting up a proprietary trading operation strictly for the strategy, or a separate asset management division in order to collect the incentive fees, says Madoff, would conflict with his firm's primary business of market making.

"We're perfectly happy making the commissions" by trading for the funds, he says, which industry observers note also gives the firm the entirely legitimate opportunity to "piggyback" with proprietary trading that is given an advantage by knowing when and where orders are being placed.

Setting up a division to offer funds directly, says Madoff, is not an attractive proposition simply because he and the firm have no desire to get involved in the administration and marketing required for the effort, nor to deal with investors.

Many parts of the firm's operations could be similarly leveraged, he notes, but the firm generally believes in concentrating on its core strengths and not overextending itself. Overseeing the capital provided by the funds and its managed accounts, he says, provides another fairly stable stream of revenue that offers some degree of operational diversification.

Madoff readily dismisses speculation concerning the use of the capital as "pseudo equity" to support the firm's market making activities or provide leverage. He says the firm uses no leverage, and has more than enough capital to support its operations.

He notes that Madoff Securities has virtually no debt and at any given time no more than a few hundred million dollars of inventory.

Since the firm makes markets in only the most highly capitalized, liquid stocks generally represented by the S&P 500 index, a majority of which are listed on the NYSE, as well as the 200 most highly capitalized Nasdaq-listed stocks, says Madoff, it has almost no inventory risk.

Finally, Madoff calls ridiculous the conjecture that the firm at times provides subsidies generated by its market making activities to smooth out the returns of the funds in a symbiotic relationship related to its use of the capital as a debt or equity substitute. He agrees that the firm could easily borrow the money itself at a fairly low interest rate if it were needed, and would therefore have no reason to share its profits. "Why would we do that?"

Still, when the many expert skeptics were asked by MAR/Hedge to respond to the explanations about the funds, the strategy and the consistently low volatility returns, most continued to express bewilderment and indicated they were still grappling to understand how such results have been achieved for so long.

Madoff, who believes that he deserves "some credibility as a trader for 40 years," says: "The strategy is the strategy and the returns are the returns." He suggests that those who believe there is something more to it and are seeking an answer beyond that are wasting their time.

FOR IMMEDIATE RELEASE **2008-297**

STATEMENT REGARDING MADOFF INVESTIGATION

Washington, D.C., Dec. 16, 2008 – *Securities and Exchange Commission Chairman Christopher Cox issued the following statement today concerning its ongoing investigation in the case of* SEC v. Madoff:

Since the Commission first took emergency action against Bernard Madoff and his firm, Bernard L. Madoff Investment Securities, LLC, on Thursday, December 11, every necessary resource at the SEC has been dedicated to pursuing the investigation, protecting customer assets and holding both Mr. Madoff and others who may have been involved accountable.

SEC investigators are currently working with the trustee and other law enforcement agencies to review vast amounts of records and information involving Mr. Madoff and his firm. Those records are increasingly exposing the complicated steps that Mr. Madoff took to deceive investors, the public and regulators. Although the information I can share regarding an ongoing investigation is limited, progress to date indicates that Mr. Madoff kept several sets of books and false documents, and provided false information involving his advisory activities to investors and to regulators.

Since Commissioners were first informed of the Madoff investigation last week, the Commission has met multiple times on an emergency basis to seek answers to the question of how Mr. Madoff's vast scheme remained undetected by regulators and law enforcement for so long. Our initial findings have been deeply troubling. The Commission has learned that credible and specific allegations regarding Mr. Madoff's financial wrongdoing, going back to at least 1999, were repeatedly brought to the attention of SEC staff, but were never recommended to the Commission for action. I am gravely concerned by the apparent multiple failures over at least a decade to thoroughly investigate these allegations or at any point to seek formal authority to pursue them. Moreover, a consequence of the failure to seek a formal order of investigation from the Commission is that subpoena power was not used to obtain information, but rather the staff relied upon information voluntarily produced by Mr. Madoff and his firm.

In response, after consultation with the Commission, I have directed a full and immediate review of the past allegations regarding Mr. Madoff and his firm and the reasons they were not found credible, to be led by the SEC's Inspector General. The review will also cover the internal policies at the SEC governing when allegations such as those in this case should be raised to the Commission level, whether those policies were followed, and whether improvements to those policies are necessary. The investigation should also include all staff contact and relationships with the Madoff family and firm, and their impact, if any, on decisions by staff regarding the firm.

The Commission believes strongly that it is vital that SEC investigators, examiners, and enforcement staff be above reproach while conducting their duties, in order to ensure the integrity and effectiveness of the SEC. In addition to the foregoing investigation, I have therefore directed the mandatory recusal from the ongoing investigation of matters related to *SEC v. Madoff* of any SEC staff who have had more than insubstantial personal contacts with Mr. Madoff or his family, under guidance to be issued by the Office of the Ethics Counsel. These recusals will be in addition to those currently required by SEC rules and federal law.

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THE WALL STREET JOURNAL.
WSJ.com

DECEMBER 18, 2008

Madoff Misled SEC in '06, Got Off

By GREGORY ZUCKERMAN and KARA SCANNELL

Securities and Exchange Commission investigators discovered in 2006 that Bernard Madoff had misled the agency about how he managed customer money, according to documents, yet the SEC missed an opportunity to uncover the Ponzi scheme.

Harry Markopolos -- who once worked for a Madoff rival -- sparked the probe with his nearly decadelong campaign to persuade the SEC that Mr. Madoff's returns were too good to be true. In recent days, The Wall Street Journal reviewed emails, letters and other documents that Mr. Markopolos shared with the SEC over the years.

When he first began studying Mr. Madoff's investment performance a decade ago, Mr. Markopolos told a colleague at the time, "It doesn't make any damn sense," he and the colleague recall. "This has to be a Ponzi scheme."

The SEC's documents indicate the agency had Mr. Madoff in its sights amid multiple violations that, if pursued, could have blown open his alleged multibillion-dollar scam. Instead, his firm registered as an investment adviser, at the agency's request, and the public got no word of the violations.

For Mr. Markopolos, the arrest a few days ago of Mr. Madoff was something of a vindication after his long campaign. At a certain point, he says, "I was just the boy who cried wolf."

On Jan. 4, 2006, the SEC's enforcement staff in New York opened an investigation, based on Mr. Markopolos's allegations, into whether Mr. Madoff was, in fact, running a Ponzi scheme. The SEC staff received documents from Mr. Madoff and Fairfield Greenwich, a hedge fund that placed money with Mr. Madoff on behalf of its clients. The SEC also interviewed Mr. Madoff, his assistant, an official from Fairfield Greenwich and another employee.

Among other things, the SEC found that Mr. Madoff personally "misled the examination staff about the nature of the strategy" used by the Fairfield funds and other hedge-fund accounts, and also "withheld from the examination staff information about certain of these customers' accounts," the SEC documents say.

The SEC report said that neither Mr. Madoff nor the Fairfield funds disclosed to investors in the Fairfield funds that Mr. Madoff was the investment adviser.

A lawyer for Fairfield couldn't be reached for comment.

The SEC report also said Mr. Madoff had violated rules requiring investment advisers to register with the SEC, which makes them subject to inspections and examinations. Investment advisers must register if they have more than 15 clients.

The staff recommended closing the investigation because Mr. Madoff agreed to register his investment-advisory business and Fairfield agreed to disclose information about Mr. Madoff to investors. The SEC report said the staff closed the case "because those violations were not so serious as to warrant an enforcement action."

Mr. Markopolos says his suspicions started in late 1999, after a colleague returned from New York with tales of Mr. Madoff's trading prowess. Whether the markets were up, or down, Mr. Madoff managed to clock in with steady gains 12% or so a year, reportedly achieving that by trading a mix trading stocks and stock-index options.

Liked the Look

Mr. Markopolos says his bosses liked the look of those returns -- and asked him why he couldn't do the same thing.

Under pressure to deliver, Mr. Markopolos and a colleague at their Boston investment outfit tried to reconstruct Mr. Madoff's purported strategy. Their results paled in comparison, and Mr. Markopolos began suspecting possible fraud.

His bosses told him to go back and check the math, given Mr. Madoff's renown as a trader.

So Mr. Markopolos turned to Daniel DiBartolomeo, a top financial mathematician in Boston. Mr. DiBartolomeo says he spent hours poring through Mr. Markopolos's data, and ultimately agreed: The strategy Mr. Madoff said he used couldn't have achieved the returns he boasted of.

A lawyer for Mr. Madoff declined to comment on Mr. Markopolos's allegations.

'Sounds Serious'

In early 2000, Mr. Markopolos shared his explosive concerns with Edward Manion, a staff examiner at the SEC's Boston office.

In his documents, Mr. Markopolos said that there's a chance "I'm an idiot for wasting your time." But he argued forcefully that "I believe an SEC visit is warranted" to look into Mr. Madoff's practices.

"This sounds serious," Mr. Manion told him, inviting Mr. Markopolos in for a meeting.

In May 2000, Mr. Markopolos says he sat down with Mr. Manion and an SEC attorney.

Mr. Markopolos argued his case: A key part of Mr. Madoff's strategy relied on buying and selling options on the Standard & Poor's 100-stock index. But Mr. Markopolos said his research showed there weren't enough S&P-100 options in existence at the time to support Mr. Madoff's stated strategy, given all the money he seemed to be managing. So something else must be going on.

Mr. Markopolos, a native of Erie, Pa., who had trained in "unconventional warfare," including intelligence gathering, as a reservist in the Army, says he came to "consider Madoff a domestic enemy."

Outsized Gains

In the months after the initial meeting with the SEC, Mr. Markopolos kept hearing about Madoff's outsized gains, and how the firm was growing -- sparking frequent calls to Mr. Manion to discuss the case.

Over a year passed. Then, in late 2001, Mr. Manion told Mr. Markopolos the case appeared to have fallen through the cracks. He asked Mr. Markopolos to resubmit his documents and arguments, so they could be passed on to the SEC's New York office.

Mr. Markopolos sent the documents, adding three pages arguing that the fraud was growing in size as Madoff's assets under management grew beyond $12 billion.

Mr. Markopolos also diagrammed how he believed the Madoff organization seemed to work, using a Byzantine flow chart with circles, squares, rectangles and arrows.

Mr. Markopolos continued to receive sympathetic calls from Mr. Manion. "He's the one that kept me going, I would have stopped long ago," Mr. Markopolos says.

But Mr. Manion pointed out that any investigation would have to be conducted by the New York office, where Mr. Madoff's firm was based.

Mr. Markopolos says that worried him. "I was told that the relationship between the SEC's Boston and New York offices is about as warm and cordial as the Yankees-Red Sox rivalry," Mr. Markopolos says.

'Sick of Wall Street'

Mr. Markopolos left his firm in 2004, and started a fraud-investigation practice. Mr. Markopolos's old colleagues, prodding him not to give up, spoke by phone for hours at time about Mr. Madoff.

"Some people play fantasy sports, that was how it was with us -- Madoff was our fantasy sport," Mr. Markopolos recalls. "We wanted him nailed."

In 2005, an SEC official in Boston called to say the agency was again looking into the case, and told Mr. Markopolos to contact Meaghan Cheung, a supervisor in SEC's New York office, Mr. Markopolos recalls.

In November 2005, Mr. Markopolos sent Ms. Cheung a 21-page report outlining his concerns.

He presented a series of 29 "red flags," ranging from in-depth mathematical calculations that purported to show the Madoff investment strategy couldn't work, to little more than rumor or innuendo -- such as claims that a group of Arab investors were barred from using a major accounting firm to examine Mr. Madoff's books.

He also questioned the fact that Mr. Madoff, unlike most money managers of his stripe, didn't charge his investors a fee for handling their money. Instead, he seemed to make profits on commissions generated by the trades on investors' behalf.

"Bernie Madoff's returns aren't real," Mr. Markopolos said. "And if they are real," it's because Mr. Madoff might be engaging in "front running," or buying shares for his investors' accounts just before filling orders for other clients that have the potential to send the price higher, an illegal practice.

Mr. Markopolos's allegations against Mr. Madoff were far from bulletproof. Mr. Markopolos provided no definitive evidence of a crime. His reports were laden with frothy opinions.

In his lists of "red flags," he occasionally got things wrong. Sometimes he even misstated the starting date of his own campaign against Mr. Madoff.

Ms. Cheung was a respected attorney known for quickly bringing high-profile charges against executives of cable-television company Adelphia Communications several years earlier, after that company issued a questionable earnings report.

Mr. Markopolos thought he had a chance for his campaign to succeed.

"I had my hopes up, I thought it was a good enough package that they would go and shut this man down," Mr. Markopolos recalls.

He sent an email adding more evidence -- noting that he might be eligible for the SEC's bounty program if it turned out that Mr. Madoff was, in fact, front running.

An SEC spokesman wouldn't comment on the agency's communication with Mr. Markopolos.

In its resulting investigation, the SEC searched for evidence of "front running" but found no indications that was happening, according to an individual familiar with the matter.

Investigators also checked out Mr. Markopolos's claim that Mr. Madoff was running a Ponzi scheme. But the billions of dollars of assets held by Mr. Madoff's asset-management unit appeared to match those that various investment firms said they had placed with Madoff, suggesting that there weren't problems.

Today, it is now known that that Mr. Madoff had many more investors -- such as individuals and charities -- which weren't disclosed in regulatory filings, making it harder for investigators at that time to ascertain precisely how much money he was managing.

On Tuesday, SEC Chairman Christopher Cox also said that Madoff kept several sets of books and false documents. That, too, could have thrown off investigators a few years ago.

Rules Violations

As part of the inquiry, the SEC did find that the firm had violated technical rules about executing trades.

Early this year, Mr. Markopolos made one last major effort after receiving an email from Jonathan Sokobin, an official in the SEC's Washington, D.C., office whose job was to search for big market risks. Mr. Sokobin had heard about Mr. Markopolos and asked him to give him a call, according to an email exchange between them.

With low expectations, Mr. Markopolos got in touch. "The way I figured it," he says, "if they didn't believe you at $5 billion, and not at $10 billion, they didn't believe you at $30 billion, then why would they believe you at $50 billion?"

Funds Pulled

Mr. Markopolos also sent Mr. Sokobin an email -- with the stark subject line "$30 billion Equity Derivative Hedge Fund Fraud in New York" -- saying an unnamed Wall Street pro recently pulled money from Mr. Madoff's firm after trying to confirm trades supposedly done in his account, but discovering that no such trades had been made.

It was his last try. He never heard back.

"I felt pretty low," Mr. Markopolos recalls.

Mr. Sokobin, through an SEC spokesman, declined to comment.

Last Thursday, as Mr. Markopolos watched his children take a karate lesson near his home in Whitman, Mass., 20 miles outside Boston, he checked his voice mail, trying to ignore the noise from the children. Walking out to the foyer, Mr. Markopolos returned one of the calls, and heard an old friend tell him that Mr. Madoff had been arrested.

"I kept firing bigger and bigger bullets" at Mr. Madoff, "but I couldn't stop him," Mr. Markopolos says. With the SEC's mea culpa and Mr. Madoff's arrest, "I finally felt relief."

Write to Gregory Zuckerman at gregory.zuckerman@wsj.com and Kara Scannell at kara.scannell@wsj.com