

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

In the Matter of:)
) File No. OIG-509
OIG-509)

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Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549
DATE: Tuesday, May 5, 2009

The above-entitled matter came on for hearing, pursuant to notice, at 9:59 a.m.

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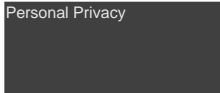
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P R O C E E D I N G S

1
2 MR. KOTZ: On the record at 9:59 a.m. on May 5th,
3 2009, at the United States Securities and Exchange
4 Commission.

5 I'm going to swear you in. Would you please raise
6 your right hand?

7 Whereupon,

8 DAVID OSTROW

9 was called as a witness and, having been first duly sworn,
10 was examined and testified as follows:

EXAMINATION

11
12 BY MR. KOTZ:

13 Q Okay. Could you state and spell your -- spell
14 your full name for the record?

15 A William, W-i-l-l-i-a-m, David, D-a-v-i-d, Ostrow,
16 O-s-t-r-o-w.

17 Q Mr. Ostrow, my name is David Kotz. I'm the
18 Inspector General of the United States Securities and
19 Exchange Commission. I have with me my colleagues Heidi
20 Steiber and Chris Wilson, and you have representing you Ralph
21 Talarico from NTEU.

22 This is an investigation by the Office of Inspector
23 General, Case Number OIG-509, and we're going to ask you
24 certain questions and you'll provide answers under oath.

25 The court reporter will record and later transcribe

1 everything that is said. Please provide therefore verbal
2 answers to the questions. A nod of the head or another
3 non-verbal response won't be able to be picked up by the
4 court reporter.

5 Also, so the record will be clear, please let me
6 finish my question before you provide your response. In
7 addition, it is important that you understand the questions
8 and give accurate answers. If there's anything you don't
9 understand or anything you do not know or are not sure about,
10 please let me know. Otherwise, I will assume that you heard
11 and understood the question.

12 Do you understand those instructions?

13 A Yes.

14 Q Okay. I'll give you the standard Perjury Warning
15 language.

16 As you can see, your responses and statements given
17 today are provided after you've sworn an oath. They will be
18 taken down verbatim by the court reporter.

19 This is an official U.S. Government law enforcement
20 investigation. The claims asserted in this case are serious
21 ones.

22 It is very important that you tell me everything
23 you know about the matter at hand and are completely
24 forthcoming and truthful with me. I'm formally advising you
25 that your testimony today is subject to the laws of perjury
26 and providing false or misleading testimony under oath is a

1 very serious offense. If the evidence shows that the
2 testimony you've given is false, we may refer it as
3 appropriate.

4 Do you understand those instructions?

5 A Yes.

6 Q Okay. I'm going to get some documents in for the
7 record. This is a Warning, Employee Voluntarily Provide
8 Information, Notice of Rights. I think it's been provided to
9 you previously, but if you want to take a look at it, and
10 it's okay to sign it.

11 MR. KOTZ: And then, Mr. Talarico, this is a
12 Confidentiality and Non-Disclosure Agreement since some of
13 the information here may be deemed non-public. You can take
14 a look at that and sign that.

15 Okay. Mr. Ostrow, if you're finished, we'll mark
16 this as Exhibit 1. This is the Notice of Rights.

17 (SEC Exhibit No. 1 was marked for
18 identification.)

19 BY MR. KOTZ:

20 Q It is right that this is your signature and date on
21 Exhibit 1?

22 A Correct.

23 Q Great. Okay.

24 MR. KOTZ: Thank you, Mr. Talarico. This we're
25 going to mark as Exhibit 2. This is the Confidentiality and
26 Non-Disclosure Agreement signed by Mr. Talarico and you

1 A On occasion. In some instances, there was one exam
2 where he was the direct supervisor on it because there was no
3 branch chief involved, in which case I did see him in the
4 field, whereas on my most recent exam, he didn't come out to
5 the field but we held meetings with him back in the office.

6 Q What about Robert Sollazzo, what is his position?

7 A He is the Associate Regional Director of the
8 Broker-Dealer Division at the New York Regional Office.

9 Q Okay. So is he Nee's supervisor?

10 A Correct.

11 Q Okay. So how much involvement on an exam would
12 Robert Sollazzo have?

13 A I've had some examinations where he's been heavily
14 involved and other exams where, you know, you might just hear
15 the name mentioned in a program update, you know, for a job
16 well done.

17 Q So there's some exams where Sollazzo would not be
18 onsite at all?

19 A Yeah. I don't think he's ever really come onsite
20 of any of my exams, but sometimes it's just a lot of
21 conference calls where to -- you know, Personal Privacy or to
22 other entities.

23 Q Now, when you conduct an exam, who is involved in
24 determining the focus of the exam?

25 A Well, currently, I guess myself as an examiner or
26 junior examiner would write up a scope memo and send that to

1 the branch chief or supervisor to approve or make changes.
2 Prior to that, it was probably just either this is a cause
3 exam, here's the reason why. If it's an oversight exam, you
4 know what to do, or if it's just a routine exam, you know, do
5 some pre-exam work and figure out a scope.

6 Q Okay. Does the assistant director play any role in
7 determining or approving the focus of a cause exam?

8 A The assistant director being John Nee in this case?

9 Q Yeah.

10 MR. TALARICO: John Nee was listed as an associate.

11 Is he an assistant? I mean, I'm --

12 THE WITNESS: I think I said assistant or
13 associate.

14 MR. KOTZ: I think Sollazzo was the associate and
15 Nee was the assistant.

16 MR. TALARICO: Okay, okay.

17 THE WITNESS: Yeah.

18 BY MR. KOTZ:

19 Q So I guess what I'm trying to figure out is you get
20 a complaint in and there has to be a determination made what
21 the focus of the exam is going to be. You said that the
22 staff accountant would prepare something, send it to the
23 branch chief, but who would make the final decision on what
24 the focus should be?

25 A Well, to just go back for one second --

26 Q Sure.

1 A -- the assignment memorandum is sent to the
2 examiner. So we don't decide what exams to do. Once we're
3 given an exam, we're either told what we're going there for,
4 whether it's for a cause or for an oversight or for just an
5 annual cycle or a cycle.

6 Once we're told what exam we'll be working on,
7 that's when you're usually provided more guidance as to what
8 you'll be looking at and then you draft a memo or a scope
9 based on that conversation with your supervisor or with the
10 associate.

11 Q All right. But the initial determination of the
12 focus of the exam is given to you prior to when you start?

13 A Correct. But it may be a one sentence form which
14 you have to then expand into, you know, a page worth of
15 notes.

16 Q Okay. And so then once you expand it into a page
17 worth of notes, who would have the final decision to approve
18 whether that page full of notes is exactly what you're going
19 to focus on in the exam?

20 A Only for the last year or so have I sent scope
21 memos and had them reviewed and have comments made. Prior to
22 a few years ago, it was really just -- I don't know if there
23 was a formal scope memo or just sort of as the exam
24 progressed, notes were taken and e-mails were exchanged.

25 Q Okay. Why don't we get into it in more detail? We
26 have a document.

1 All right. Let me start a little bit of a new
2 subject. When did you first hear of Bernie Madoff or Madoff
3 Securities?

4 A I'm sure I knew the name Bernie Madoff prior to
5 being assigned an examination of the Broker-Dealer Unit in
6 2005, whether just because he was a large market maker. If I
7 had -- if I had made a blue sheet request, you know, in years
8 past prior to that, I probably got a response back from
9 Bernard Madoff firm.

10 Q Okay. So you were aware that Bernie Madoff was a
11 large market maker. Did you have any other sense of his
12 reputation?

13 A Not really. I wouldn't say -- I didn't know as
14 much as when I started the examination and during
15 pre-examination I did learn more about him.

16 Q Okay. All right. Why don't we show you a
17 document? This is an e-mail from Peter Lamore to you, dated
18 3/30/2005, 11:55 a.m., and we're going to mark this as
19 Exhibit 3.

20 (SEC Exhibit No. 3 was marked for
21 identification.)

22 (The witness examined the document.)

23 BY MR. KOTZ:

24 Q Okay. Do you know why you would have sent this
25 e-mail, it looks like, to Peter Lamore, Paul Pocress --

26 A Pocress.

1 Q Pocress and then I guess yourself?

2 A Why would I have sent this e-mail to them?

3 Q Yeah.

4 A I believe either I had just started an examination
5 of Bernard Madoff or was about to and probably during
6 pre-exam work or from Factiva or some source found this
7 article. Paul Pocress because he's just the resident
8 examiner who knows an extreme amount of facts and details
9 about -- if you throw out any family name, he knows, you
10 know, where they own buildings, what their family owned, what
11 other businesses.

12 So I had probably told him at some point I'm
13 starting Bernard Madoff and he probably gave me some
14 background information and then, you know, I found this
15 article and just shared it with him.

16 Q Okay. And so this article refers to the Madoff
17 Dynasty. So as you were kind of learning about Bernard
18 Madoff, did you understand that he was kind of an important
19 figure in the industry?

20 A Glancing over this article, seeing that him and his
21 family are involved in multiple facets of the industry.

22 Q Okay. So it's fair to say that at the time that
23 you and the other folks on the exam started the exam, you
24 were aware that Bernie Madoff was an important figure in the
25 industry?

26 A Correct.

1 Q And Peter Lamore responds, "Ha. Thanks." Any idea
2 what -- why he wrote, "Ha?"

3 A No idea.

4 Q I'm going to show you another document. This is
5 dated 3/28/2005, 4:14 p.m., from you to Peter Lamore.

6 MR. KOTZ: We'll mark this as Exhibit 4.

7 (SEC Exhibit No. 4 was marked for
8 identification.)

9 MR. TALARICO: This right here?

10 THE WITNESS: The date of the last e-mail was?

11 MR. TALARICO: March 30th, 2005.

12 THE WITNESS: Okay.

13 MR. KOTZ: Yeah. So this is two days earlier.

14 (The witness examined the document.)

15 THE WITNESS: Okay.

16 BY MR. KOTZ:

17 Q Okay. And so Exhibit 4 is another document sent
18 around kind of for background before the exam?

19 A Looking at it, it says, "Background-Madoff" and
20 usually in pre-exam, I come across a bunch of articles and I
21 like to refer back to them later on or I just try to memorize
22 a lot of them. And I probably later on used this to dig
23 deeper into his London office. And I usually cite a lot of
24 firms when they don't file on their CRD with FINRA, if they
25 have outside business activities. So this is usually a good
26 start of how I find things like that.

1 Q Okay. So you were aware that Bernie Madoff served
2 as Chairman of the Board of Directors of the NASDAQ Stock
3 Market when you started the exam?

4 A That he had served or that he was serving?

5 Q Well, this article says he has served as Chairman
6 of the Board of Directors of the NASDAQ Market, Stock Market.

7 A Okay. Yes.

8 Q And you were aware that he was a founding member of
9 the Board of Directors of the International Securities
10 Clearing Corporation in London?

11 A From this article, yes.

12 Q Okay.

13 A I don't know if that has much relevance to my exam
14 in terms of what we were doing.

15 Q Okay. But you collected these documents as
16 background --

17 A Correct.

18 Q -- for the exam?

19 A Correct.

20 Q Okay. Have you ever met Bernie Madoff?

21 A Yes.

22 Q On how many occasions?

23 A For the two and a half months or so that I was
24 onsite conducting an examination of the books and records of
25 his broker-dealer.

26 Q How many times? Did you see him every day?

1 A I'd say almost every day, he was -- you know, I
2 usually have a contact person in the firm, like a compliance
3 examiner. He was the contact person for myself and Peter
4 throughout the 95 percent of the exam.

5 BY MS. STEIBER:

6 Q Was it unusual to have the CEO as the contact
7 person in an examination?

8 A Yes and no. There have been some exams where I've
9 never met the president of a firm and other exams where you
10 see them occasionally, they come in to see how things are
11 going, but this was unusual but, you know, we began to learn
12 that he was an unusual character.

13 BY MR. KOTZ:

14 Q But had you ever had another exam where the
15 president of the company was the main contact, the main
16 person you talked to during the entire onsite exam process?

17 A Probably been to a few two-or-three-person shops
18 where, in that case, someone might have dual hats and you
19 deal with that person. So there have been a few examples but
20 this was a very large firm, so it was a lot more unusual.

21 Q Okay. So have you ever had a case before with such
22 a large firm where the president was so involved as the
23 contact person?

24 A I would say no.

25 Q After the examination ended, have you ever -- did
26 you ever have any contact with Bernie Madoff after that?

1 A When you say examination ended, meaning the onsite
2 portion of the examination or the final processing of the
3 report?

4 Q Let's say the final processing of the report.

5 A I don't know if there was one call where he made
6 when he was overseas either stating that he received the copy
7 of the violation letter or if we were just letting him know
8 that we sent it or we held the exit interview on the phone
9 right before the report was processed. After that, I did not
10 have contact or see Bernard Madoff after that.

11 Q Okay. We'll talk about some of the specifics as we
12 go through the documents.

13 Were you aware of any other examinations or OCIE
14 involvements with Madoff, other than the exam we've been
15 talking about?

16 MR. TALARICO: When you say was he aware, do you
17 mean before the exam, during the exam, or after the exam?

18 BY MR. KOTZ:

19 Q Well, how about when the exam -- when you started
20 your exam, were you aware of any other exams going on?

21 A No.

22 Q Okay. At a certain point in time you'did learn --

23 A Yes.

24 Q -- that OCIE did another exam?

25 A Yes.

26 Q When was that?

1 A We had a meeting with Bernard Madoff and at some
2 point he had said, "You should be aware of this. We've been
3 in communication with OCIE and been going back and forth with
4 them." So myself and Peter, I think I researched it online
5 afterwards, saw it wasn't on NRSI, Name Relationship Search
6 Index, I believe, which is an internal system, so there was
7 no log of it there, and then I believe either -- I think John
8 Nee sent an e-mail to John McCarthy requesting information
9 related to this and then we became more aware of it.

10 All throughout the examination, Bernard Madoff
11 would drop the names of high-up people in the SEC and at
12 first, you know, he just -- he would always reference people
13 in OCIE and Broker-Dealers sometimes. So he knew a lot of
14 people. He even came in and told myself and Peter who the
15 next chairman of the SEC was going to be a few weeks prior to
16 us actually getting an e-mail at the SEC. So we were just
17 pretty amazed by that, as well, and just --

18 Q So the first time you heard about this Headquarters
19 exam was from Bernie Madoff?

20 A Correct. And then we verified it and got documents
21 and had conference calls.

22 BY MS. STEIBER:

23 Q Why do you think that he would always do all this
24 name dropping? Was it to, do you think, intimidate you or to
25 impress you?

26 A A combination of both. I mean, it didn't really

1 impress us. We just first thought he was throwing out a lot
2 of names and then came to realize he did know these people.
3 He did have conversations because we were skeptical at first.

4 BY MR. WILSON:

5 Q Were you aware of any other OCIE exams of Bernie
6 Madoff, other than the one you just mentioned?

7 MR. TALARICO: When?

8 MR. WILSON: At any time.

9 THE WITNESS: Not that I recall. I mean, I know of
10 this one where they were looking into the hedge fund
11 business, but -- and I -- no, I don't know if, during the
12 exam or after, when I was -- I think another examiner had did
13 an examination of Bernard Madoff back in the early '90s or
14 something or mid '90s. So I don't know when that came about.

15 BY MR. WILSON:

16 Q Okay. But you don't know any details about that?

17 A About that or about OCIE, no.

18 Q Okay.

19 BY MR. KOTZ:

20 Q Okay. If you could try to remember for us how you
21 first became involved in the 2005 cause exam of Madoff
22 Securities?

23 A How I got assigned to it, I'm not sure. I know
24 Peter was put on to the exam because he was a trader in a
25 previous -- a previous job. So they figured having someone
26 with industry experience on an exam where we'd be dealing

1 with, you know, algorithms, hedge fund or just algorithms in
2 general and trading since we were going to be drilling down
3 to see if the orders from the customer retail flow was being
4 used to influence the -- the hedge fund returns.

5 Q So who selected you? Who assigned you for the
6 Madoff exam?

7 A If you have to assignment memo, it would have on
8 there, I know John Nee was the assignee. I know Ethan's
9 father had passed away, so I don't know if there was ever a
10 thought of him being on the exam or not, but it was just
11 assigned to me from John, I guess, because he's Ethan's
12 direct supervisor and they wanted me to go out to the field.

13 Q So what was your role in the exam?

14 A I was the, I guess, senior examiner as well as, you
15 know, a mentor to Peter. I don't know how long he had been
16 there, but I remember him filling out like an annual
17 evaluation, junior evaluation form for one of the other staff
18 members during the course of the exam or right after. So I
19 helped him, you know, how to -- how to -- what I had done in
20 the past in terms of writing up stuff.

21 Q Okay.

22 BY MS. STEIBER:

23 Q So you were the lead on the exam? Is that the
24 technical term?

25 A During the exam portion, yes, I'd say I was the
26 lead. In terms of follow-up stuff, I wasn't really, you

1 know, involved as much, just secondhand.

2 Q And was there a branch chief on the team?

3 A There was no branch chief assigned to this exam.

4 Q Wasn't that unusual?

5 A Probably. I'm sure there are other instances, you
6 know. They're not going to stop the SEC for three or four
7 months while someone, you know, bereaves.

8 Q But in most exams you have that are cause exams, do
9 you have a branch chief on the matter?

10 A I would say 90 percent of the time, 95. Maybe one
11 other time I might have been assigned by a supervisor or even
12 one small exam, I think Bob Sollazzo worked closely with
13 because maybe Personal Privacy had been out or someone had been
14 out.

15 BY MR. KOTZ:

16 Q Were you aware of why the cause exam was being
17 initiated?

18 A Yes, it was three factors. There was a MarHedge
19 article written, I think in 2000-2001, regarding Bernie
20 Madoff and there was an article in Barron's by Erin Arvedlund
21 in 2001, I believe, related to the firm, and there was also
22 an IA exam done, I guess, with Investment Adviser #1
23 and I guess some e-mails or referrals or something was made
24 to Broker-Dealer and we used that, as well, basically just
25 e-mailed back and forth saying how does he get such great
26 returns.

1 Q And how was the determination made as to what the
2 focus of the exam would be?

3 A I would say we really used the Barron's article and
4 the MarHedge article as a starting point and just tried to
5 figure out, use that as an outline and just go along to see
6 if the customer order flow is being used, you know, if there
7 was some sort of black box algorithm that was picking off,
8 you know, large block trades and so that's where we started.

9 Q So you used those two more than the
10 e-mails? Investment Adviser #1

11 A The Investment Adviser #1 probably just was more recent than
12 those other two articles and sort of in the same -- same
13 genre.

14 Q Okay. So what was the focus of the 2005 cause exam
15 of Madoff Securities?

16 A To prove that he wasn't -- that Bernard Madoff
17 wasn't using profits or information, data mining, of the
18 customers of the broker-dealer to the benefit of a handful of
19 investment advisory or whatever it is that Bernard Madoff
20 referred to them as. We had a real difficult time dealing
21 with him.

22 Q And so that -- is that front running?

23 A Looking to see if he was front running, if there
24 was inside information or just, you know, you know, -- that's
25 it.

26 Q Okay. All right. I show you another document.

1 MR. KOTZ: We'll mark this as Exhibit 5. This is a
2 memo from Dorothy Eschwie to Robert Sollazzo and Richard Lee,
3 dated April 22nd, 2004, with some attachments.

4 (SEC Exhibit No. 5 was marked for
5 identification.)

6 (The witness examined the document.)

7 THE WITNESS: Where -- where was this produced from
8 or --

9 MS. STEIBER: These are from the workpapers.

10 THE WITNESS: Of the broker-dealer?

11 MS. STEIBER: That was produced by Nero.

12 MR. KOTZ: The workpapers for the exam.

13 THE WITNESS: For the Madoff exam?

14 MS. STEIBER: Yes.

15 MR. KOTZ: Yeah.

16 (The witness examined the document.)

17 THE WITNESS: Okay.

18 BY MR. KOTZ:

19 Q Do you recognize these documents? Exhibit 5?

20 A I know I recall the cover sheet. I'm not sure if I
21 recall seeing the second page. I guess I was there, but --
22 and I know the report contained -- our final report
23 contained, you know, excerpts from here. I'm not sure if I
24 had read this whole thing, if I had had a copy of it, you
25 know. You're saying it was in the workpapers.

26 Q Okay. But you mentioned before e-mails that were

1 point to make here is that not only are we unsure as to how
2 [Personal Privacy] makes money for us, we are even more unsure as to how [Personal Privacy]
3 makes money from us; i.e., why does he let us make so much
4 money? Why doesn't he capture that for himself?"

5 Do you recall that being something that you were
6 aware of at the time?

7 A Sure. Because that's -- that's an exact point
8 that's made in the 2001 Barron's article and the MarHedge
9 article. So that was another thing we were -- you know, we
10 asked Bernie in meetings why don't you make the 2 and 20 or
11 the common percentages from hedge funds, you know, and he
12 said he was just fine making the 4 cents per share which were
13 considered commission equivalents and these customers weren't
14 considered customers and it wasn't considered an investment
15 advisory.

16 Q Did you consider that unusual, that there was this
17 money kind of left on the table that he didn't collect?

18 A No, because I guess he had an explanation for that,
19 that he was fine with just making the 4 cents order flow
20 which 4 cents per share which worked out to be \$70 or \$80
21 million a year during 2001-2002.

22 Q Looking further down in this paragraph, it says,
23 "The point is that as we don't know why he does, what he does,
24 we have no idea if there are conflicts in his business that
25 could come to some regulator's attention. Throw in that his
26 brother-in-law's his auditor and his son is also high-up in

1 the organization, imagine that, and you have the risk of some
2 nasty allegations to freezing of accounts, et. cetera, et.
3 cetera."

4 Do you remember that being an issue that you looked
5 at in the exam?

6 A I know the first part of the sentence was written a
7 lot. So in terms of conflicts in his business that could
8 come to some regulator's attention, maybe just because that
9 went back and forth in our, you know, rough drafts to the
10 report, so I know that was a snippet taken.

11 In terms of, you know, from my e-mail about the
12 Madoff Dynasty, you know, we know to look for conflicts in
13 terms of, you know, everyone's family and everyone's related,
14 who's reviewing whose documents and the outside brokerage
15 statements.

16 Q Was that a concern, conflicts in his business, to
17 you as an examiner?

18 A It was a concern. It's always a concern that it
19 could be a problem, but we really didn't deal with anyone
20 else at the firm, other than Bernie, and we tried to, you
21 know, have conversations with Peter or have conversations
22 with Shana and, you know, usually were thwarted or once in a
23 blue moon we were able to send an e-mail out to Shana to
24 request an e-mail or something.

25 So we really just had the written supervisory
26 procedures to go with and, you know.

1 Q Did you think it was odd that you -- you said -- I
2 think you used the word "thwarted in efforts to talk to other
3 people, other than Bernie."

4 A Did we think it was odd? Yes, it was odd.

5 Q Okay. What about the issue of auditor
6 independence? During the exam, did you look into that?

7 A No, I don't believe we looked into that. I know we
8 had a copy of the annual audit of the broker-dealer, I
9 believe, in my files. That's it.

10 Q Okay. Further on in this same document that we're
11 talking about, it says, "It's high season on money managers
12 and Madoff's head would look pretty good above Eliot
13 Spitzer's mantle. I propose that unless we can figure out a
14 way to get comfortable with the regulatory risk in a hurry,
15 we get out."

16 Did you get the indication that at least the folks
17 in Investment Adviser #1 believed that Madoff may have been violating
18 the law?

19 A I can't -- I'm not comfortable commenting on that
20 paragraph because I don't recall reading this particular
21 e-mail. I know snippets of it. I know conversations with
22 Peter. I know -- you know, I don't know if it was just
23 paraphrased for me or --

24 Q Okay. If you look at the next page of Exhibit 5,
25 do you see where it says, and this is -- there's an asterisk
26 and underlines, do you see that, where it says, "We at

Investment Adviser #1

1 [REDACTED] have totally independent evidence that Madoff's
2 executions are highly unusual."

3 Do you know if you ever found out what that totally
4 independent evidence was?

5 A No, I don't believe so.

6 BY MS. STEIBER:

7 Q Did your supervisors, Nee or Sollazzo, ever suggest
8 that you contact [REDACTED] Investment Adviser #1 to gain additional information?

9 A No, I don't believe so. I did research on
10 [REDACTED] Investment Adviser #1 and [REDACTED] Personal Privacy, the head of it, and the whole
11 black box and just tried to really get up to speed and
12 understand algorithms as quick as I could at the start of
13 this exam to try to figure out the black box trading that
14 they were using there.

15 BY MR. KOTZ:

16 Q And in your research on [REDACTED] Investment Adviser #1 what did you
17 find about that company? Was it a credible company,
18 sophisticated company?

19 A Sophisticated, hired a lot of Ph.D.s in mathematics
20 from Stony Brook where I guess -- near where they're located,
21 but also extremely secretive, like Mr. Madoff.

22 Q But a credible source for allegations, would you
23 say, given their sophistication?

24 A I don't understand.

25 Q In other words, if you get an allegation from an
26 entity that says somebody's engaged in something improper,

1 wouldn't you look at where it comes from? Wouldn't you say
2 that since Investment Adviser #1 was such a sophisticated entity, an
3 allegation coming from them would be credible?

4 MR. TALARICO: Can I have a minute with him?

5 MR. KOTZ: Sure. You want to go off the record?

6 MR. TALARICO: Yeah.

7 (The witness conferred with counsel.)

8 MR. TALARICO: Mr. Ostrow has been shown Exhibit 5
9 and Exhibit 5 has a lot of notations and handwriting and we
10 don't know when these -- when these notations or handwriting
11 or underlining was done, was it done before the exam, was it
12 done after these done? These papers have been all over the
13 SEC, especially since Madoff got exposed, and very well these
14 things could have been underlined, you know, as a CYA measure
15 by someone else. We don't -- he's never seen these documents
16 in this form with these underlines.

17 THE WITNESS: That I recall. I don't recall seeing
18 the notes with stuff on it. Just snippets of it.

19 MR. KOTZ: Okay.

20 THE WITNESS: I mean, when -- when the memo came
21 out to hold all documents and conserve everything and stuff
22 and we started transferring stuff to a shared file, everyone
23 in the Commission was able to open up those files, oh, I'm
24 seeing your stuff being posted on the J Drive. There was no
25 sort of controls over it, just in general, like a going
26 forward thing for other exams.

1 BY MR. KOTZ:

2 Q Okay. You know that this is Lamore's handwriting
3 on the third page, right?

4 A Looking at it now and knowing what his handwriting
5 looks like, yes.

6 Q Okay. But you don't know who made these underlines
7 and this asterisk?

8 A I can't speculate who made them.

9 Q Okay. That's fine. Before the break, I had asked
10 you, I guess, about kind of the source. Given Investment Adviser #1
11 sophistication, would you consider information from them to
12 be credible?

13 A Not necessarily. You know, depending what the
14 source is, but people always provide tips. I've sat in
15 conference rooms and gotten tips from employees, you know,
16 who are about to quit or something and maybe it's just a
17 vendetta against the firm or something or just jealousy if
18 someone's earning 12 percent, why can't I?

19 BY MS. STEIBER:

20 Q In this case these are internal e-mails, though,
21 correct? They're e-mailing each other. So there's not --

22 BY MR. KOTZ:

23 Q And in fact, isn't it the case that they didn't --
24 Investment Adviser #1 didn't provide these e-mails to you? These
25 e-mails were discovered by the SEC in an exam?

26 A Exam, sure. So if it's something from an IA

1 examiner, take it serious, but still has to take it with a
2 grain of salt what the people are writing back and forth to
3 each other. But, you know, I don't think I zeroed in on that
4 particular sentence, if I had seen this e-mail, you know.

5 Q Okay.

6 A And we were there to see if the executions were
7 highly unusual ourselves. So that's what we were there to
8 verify.

9 Q Okay.

10 A The market making.

11 Q Okay. If we look at the next document, if you look
12 at -- do you see where it says Number 1 and then there's two
13 paragraphs down?

14 A Mm-hmm.

15 Q "By this measure, Madoff could do only 750 million,
16 that is with him doing 100 percent of the option volume in
17 this chosen strike with a generous 15 percent assumption.
18 Let's assume that he spreads it over three days, so we get to
19 2.1 billion, still far short of the target numbers."

20 Do you want to just kind of read the point in
21 Paragraph -- in Section 1 of this e-mail and just let me know
22 whether this is an issue that you recall or you looked at?

23 A Options in general we looked at and while if we
24 tried to figure out these kind of numbers, we were told by
25 Bernard Madoff during the exam that, I believe in January of
26 '04, the firm stopped using options. So once he tells us

1 that, it made me at least think do the outside funds, like
2 Kingate and FEMA, know that he's no longer using options, but
3 it sort of removed the question of could he do this on an
4 exchange where they don't trade that many options?

5 Q Did you do anything to verify that what Bernie was
6 telling you was correct?

7 MR. TALARICO: With respect to what? With respect
8 to options?

9 THE WITNESS: If he says he's not option trading
10 and we ask for option accounts and he doesn't provide them
11 because he says there is no option trading, that -- I mean,
12 there's not much more to verify --

13 MR. KOTZ: Okay.

14 THE WITNESS: -- and the statements just showed
15 securities on it.

16 BY MS. STEIBER:

17 Q Did you check with a fund to funds -- you had just
18 named a few -- to find out if they believed that Madoff was
19 trading options?

20 A No, we didn't check with them. We had -- myself
21 and, you know, we had wanted to check with them and --

22 Q And what happened?

23 A We sent an e-mail to John Nee, I guess, informing
24 him we were about to come back from the field, that we
25 thought it would be good to go there to look at their
26 marketing material, to look at their returns that they were

1 New York, and Fairfield Greenwich, either their New York
2 office or Connecticut office.

3 BY MR. KOTZ:

4 Q Okay. If you look at the bottom of this same page,
5 "Of course, all of our trades are with Madoff as the
6 principal, so or option positions are OTC with Madoff." It
7 goes to the next page. "So he can choose to use any strike,
8 any total volume he chooses, but the risk must be covered
9 somewhere if he's doing these trades at all. So we need an
10 OTC counterparty, not necessarily a bank, who's willing to do
11 the basket of the options, plus the underlying, with Madoff
12 at prices unfavorable for the OTC counterparty in 10 to 15
13 billion!!! Any suggestions who that might be? None of it
14 seems to add up."

15 Do you remember this issue at all?

16 A What was the name of the underlying -- was it HRH
17 or Heritage or something? I'm just trying to think because
18 when we got down to it with Bernie and finally got a list of
19 the 15 or 16 or 14 entities, I don't know if this particular
20 entity was one of the entities he gave us.

21 Q Okay. But what about the issue of the -- the point
22 here that you would need a counterparty who's willing to do
23 this, who didn't think that there would be a counterparty who
24 would be willing to do it because the prices would be
25 unfavorable to the counterparty in 10 to 15 billion? Was
26 that an issue that you guys looked at or do you recall that

1 issue?

2 A I don't recall that issue. I don't know if it was
3 done in London or prior to when he stopped doing it in 2004.
4 I'm not sure.

5 Q All right. Why don't we show you the next
6 document?

7 A Okay. Okay. This is an e-mail from Dorothy
8 Eschwie to Robert Sollazzo, 5/11/2004, 5:21 p.m.

9 MR. KOTZ: We're going to mark it as Exhibit 6.
10 (SEC Exhibit No. 6 was marked for
11 identification.)

12 (The witness examined the document.)

13 THE WITNESS: Okay.

14 BY MR. KOTZ:

15 Q Okay. Does it appear as if Sollazzo is responding
16 to the Madoff referral from Investment Adviser #1 [REDACTED]? Do you
17 think that this is that same matter?

18 A Was this -- this was -- is this taken from Robert
19 Sollazzo's e-mail or was this something provided in our box
20 of documents because this is a year earlier than our exam?

21 Q Right. Do you see where Sollazzo says, "We believe
22 this matter is worthy of an examination when resources
23 permit?" Were you aware that the information came in or the
24 decision was made to make -- to do an exam significant time
25 earlier but Sollazzo was waiting for resources?

26 A Probably as soon as I got the assignment memo,

1 whenever that was, maybe a week before I had heard about it,
2 you know, and sometimes we're asked to type up our own
3 assignment memo. In this case, I wasn't, but for Ethan, I've
4 done that before. I don't recall this, and I don't think I'd
5 seen that.

6 Q Okay.

7 A That's why, also, I'm sort of -- I don't know if --
8 you know, this was looked at back in '04 and then just
9 carried over into our exam.

10 Q Okay. It says, "Since the trading scheme appears
11 somewhat complex, we'll have to assign an experienced
12 examiner who has sophisticated knowledge of options. When
13 the time is right, we will strike."

14 Were you aware that Sollazzo waited essentially for
15 Lamore to start the exam because of Lamore's options
16 experience?

17 A No. I know he was put on the exam because of his
18 experience as a trader. So I didn't know it was being
19 like -- I didn't have an assignment memo with a TBA or
20 something, to be announced, and I waited a year or something.
21 I don't believe that happened.

22 Q And then in this same e-mail, Sollazzo says, "The
23 story, especially with consistent high returns earned over an
24 extended period, makes you wonder."

25 Was that something that was -- that you understood
26 to be a focus of the exam to explain the consistent high

1 returns earned over an extended period?

2 A Yes, based on the MarHedge article, references to
3 e-mails from Investment Adviser #1 and the Barron's article.

4 Q So in the exam, you looked at the issue of how
5 Madoff could obtain these consistent high returns earned over
6 an extended period?

7 A I would say we verified through trading data the
8 types being returned monthly and yearly. We then also looked
9 at, you know, trading desk and tried to correlate if, when he
10 put on a basket of stocks, if it had anything to do with the
11 order flow of the day and since these trades were done months
12 apart, you know, there were a lot of inconsistencies in terms
13 of data provided to us, why don't we see a trade on this day,
14 and he told -- Bernard Madoff would let us know, well, it was
15 a trade placed two months ago and it just happened to get
16 executed then.

17 So there was a lot of back and forth related to
18 that, but we tried to just verify the actual returns earned
19 by both the hedge fund and by the broker-dealer.

20 Q Okay. So you didn't kind of get to the bottom of
21 the question of how he was able to obtain consistent high
22 returns over -- earned over an extended period in the exam?

23 A Through the split strike conversion purportedly
24 that he was using and we looked at a few month sector and saw
25 that he was returning one-one and a half percent a month
26 which would come to the 12 percent and we, you know, used

1 spreadsheets and calculated from his side of the view as to
2 what was happening, but we wanted to go to, you know,
3 Fairfield Greenwich to then see if this the same returns
4 being reported to the investors on their end.

5 Q So by the end of the exam, you had satisfied
6 yourself as to the explanation of how Madoff was able to
7 obtain these consistent high returns earned over an extended
8 period?

9 A We satisfied ourselves at the end of the exam
10 knowing that he hadn't -- wasn't front running individual
11 customers and order flow. We still knew and felt that it was
12 highly suspicious and just odd and the whole story, there
13 were inconsistencies, so, you know, that were unsettling,
14 but, you know, there's only so much you can stress the point
15 to your supervisors and, you know, before you put on the next
16 exam and even -- even sitting in on testimony and stuff I
17 wanted to do, but again I was up in Albany, I was doing
18 another examination and I was just told you don't need to be
19 there, you know, Pete will be there, someone else will be
20 there and, you know, the year before I worked hand in hand
21 with Enforcement and, you know, found someone -- Madoff had a
22 sham \$400 million transaction just to get on the board of a
23 creditor's committee.

24 Q So toward the end of the exam work, after you had
25 established that you didn't believe there was front running,
26 you wanted to do more?

1 A I think throughout the exam we wanted to do more,
2 but there was a lot of questionable things in terms of -- and
3 just semantics in terms of the London office. Is it a
4 branch, is it an affiliate? You know, Bernard Madoff liked
5 to play with words. So, therefore, we'll deem it an
6 affiliate, so it doesn't have to fall under certain
7 regulation or, you know, the investment advisors, he wasn't
8 trading the money for them, he was just handling the trading
9 for them and directing them, based on his black box models.
10 So, you know, there was frustration throughout the whole
11 exam.

12 Q And so were there specific things that you or Peter
13 wanted to do with respect to the exam that you weren't able
14 to because of your supervisors, other than the one you
15 mentioned previously about going to the feeder fund?

16 A No. There were a few other issues, I mean, in
17 terms of we were looking at like closing cross data. We
18 spent a lot of the exam also just trying to get up to speed
19 and understand the types of vocabulary that the firm was
20 using for Robo and Godfather and all the different systems
21 they used to try to outsmart the system and pick off money
22 through proprietary trading.

23 So there was an issue where we felt that they had
24 an advantage of getting the NASDAQ closing and opening
25 information a few seconds before the rest of the market did
26 and since we knew in the back of our heads that he's very

1 involved with NASDAQ and Primex which was the trading system
2 and he would bring people in from Primex. They would work
3 there for a year or two and then they would go back to
4 Primex.

5 So we knew they had the capability of setting up
6 systems to exploit situations like that and in the end we had
7 conversations with the people at NASDAQ and they did verify
8 that, yes, it's possible that someone could have a slight
9 lead over someone else, but that was sort of it, and, you
10 know, we made NASDAQ aware of the situation.

11 Q Okay. I'm going to show you that next document. 5
12 and 6 back.

13 MR. KOTZ: All right. We're going to mark as
14 Exhibit 7 a series of e-mails from Investment Adviser #1 Portfolio
Manager to Personal Privacy
15 and others, dated Thursday, November 13th, 2003, with
16 numerous e-mails after that in a whole packet, as Exhibit 7.

17 I'd just ask that you take a look at them and let
18 me know if you recall ever seeing these e-mails.

19 (SEC Exhibit No. 7 was marked for
20 identification.)

21 (The witness examined the documents.)

22 THE WITNESS: Besides this first one or two that
23 were presented in Number 5, I don't believe I had seen any of
24 the other ones and also the other one you pointed out about
25 the cherry-picking stuff on the fourth page. So whatever was
26 previously presented to me in our files, but I don't remember

1 having this much detail about

Investment Adviser #1

2 BY MS. STEIBER:

3 Q Would the additional detail have been helpful in
4 your exam?

5 A I would say so.

6 (SEC Exhibit No. 8 was marked for
7 identification.)

8 BY MR. KOTZ:

9 Q Okay. I have another document for you. We'll mark
10 this as Exhibit 8. This is an e-mail from John Nee to you
11 and Peter Lamore, 12/22/2004, 3:17 p.m. It says, "FYI. Most
12 recent NASD Exam Report" and attached is an exam report.

13 A Okay.

14 Q Okay. Do you remember seeing this document?

15 A It was e-mailed to me.

16 Q Okay. But would it be common to look at a most
17 recent NASD report for an entity that you're doing an exam
18 of?

19 A Yeah. It would be part of the examination work.

20 Q Okay.

21 A I guess you have when the assignment memo was sent,
22 so I don't know if it was right before this or right after
23 this. I know we started the exam, I believe, in like March
24 of '04. March of '05. Sorry.

25 Q Okay. If you look at Page 12 of 26 to this
26 document, Exhibit 8, do you see where it says, "Internal

1 Audit?"

2 A Yes.

3 Q It says, "The staff responsible for conducting
4 internal audits have an appropriate degree of independence
5 for the departments and people they audit," and then it says,
6 "Response N/A," do you see that, and then the next page, "The
7 firm does not have an internal audit department."

8 Do you remember that, flagging that as an issue at
9 any point, that the Madoff firm didn't have an internal audit
10 department?

11 A Possibly not.

12 Q Okay.

13 A I know the NASD Exam Report, also, I don't think
14 had any reference to the hedge fund account. So we also
15 take, you know, these reports with a grain of salt.

16 Q Okay.

17 BY MS. STEIBER:

18 Q Why do you take NASD reports with a grain of salt?

19 MR. TALARICO: I'm sorry.

20 THE WITNESS: I just -- you know, even on like a
21 current exam, you know, going through FINRA workpapers and
22 reviewing them and seeing that like stuff just sometimes is
23 missing there, sometimes you get stuff from the firm and
24 sometimes the firm has a way of going back and forth with
25 attorneys, knocking stuff off the final exam report, but
26 things that I might feel that shouldn't have been knocked off

1 or was an issue.

2 So in that sense, I guess sometimes there are
3 oversights.

4 Q Do you think FINRA has these oversight because
5 they're too closely affiliated with the industry since it's
6 an SRO?

7 A Possibly industry, but, I mean, I've seen it on
8 every exam -- not every exam but on a lot of exams where
9 there's just, you know, a lot of my exams have strong
10 oversight comments, I would say, of things that are either
11 completely missed. So --

12 Q Is it --

13 A -- not necessarily Madoff family-related but just
14 in general, I guess. I don't know if that's
15 industry-related.

16 Q Is it possibly examiner incompetence?

17 A Possibly, but more so maybe that it's a check box
18 system and they don't think outside the box and even though
19 sometimes we think outside the box, sometimes we're stopped
20 from thinking outside the box and I might have been one of
21 the first examiners in the office to do an e-mail review and
22 supervisor and I sort of got in trouble for doing it but
23 later was told you did a good job, you know, and that became
24 routine where everyone did it. So sometimes you go against
25 the grain but it pays off.

26 BY MR. KOTZ:

1 Q But something in an NASD report like this, "The
2 firm does not have an internal audit department," so you
3 would think that maybe that was incorrect and they did have
4 an internal audit department or you would --

5 A I would say that since our focus was mostly to see
6 in terms of the order flow and front running and things like
7 that, we didn't really do a financial review. So we really
8 focused on the things we were looking at, spent a lot of time
9 analyzing tick by tick trades of stocks to make sure
10 customers weren't being harmed. So, you know, I know on my
11 next exam or two exams after that, a huge focus of my exam
12 was internal audit and what they were doing and were they
13 seeing everything properly --

14 Q Okay.

15 A -- and had someone working on the exam who was
16 extremely well-versed in internal audit.

17 Q But that wasn't a focus in the Madoff exam?

18 A On this exam? No.

19 Q Okay. We're going to show you the next document,
20 Exhibit 9. This is an e-mail from Peter Lamore to you, dated
21 3/17/2005, 10:32 a.m., and at the bottom of the page, in an
22 e-mail from Peter to you, as well, it refers to Focus
23 Reports.

24 (SEC Exhibit No. 9 was marked for
25 identification.)

26 BY MR. KOTZ:

1 BY MS. STEIBER:

2 Q Okay. What are they?

3 A These appear to just be annual audited reports as
4 opposed to like -- when I think focus, I think the monthly
5 and the capital computation for the monthly report filed with
6 FINRA.

7 Q Do you know if you looked at these documents?

8 A For Bernard Madoff Investment Securities, I'm sure
9 I looked at and that would have been one if the items we
10 requested, plus we have a file room in the office that has
11 annual audit reports sent to our office. So whether we got
12 it from them, the firm, we can get it from a number of
13 sources.

14 For the Cohmad one, I don't believe we would have
15 gotten it from the firm. We either got it in our office or
16 online, Edgar or something.

17 BY MR. KOTZ:

18 Q But you do think you -- you looked at them?

19 A Either myself or Peter might have looked at it
20 since he's saying -- he makes mention of -- or did I make
21 mention that -- that they received no compensation. So I
22 don't know if I found that on the Internet or I'm not sure
23 which one of us saw that.

24 BY MS. STEIBER:

25 Q If you notice on Page 6 of the Cohmad Securities
26 Annual Audited Report, on Note 5, it states that "The company

1 provides brokerage services to an entity owned by a minority
2 shareholder of the company for which it received fees
3 totaling over \$10 million for the year-ended June 30th, 2003.
4 The company shares office space and equipment with this
5 entity for which the company paid approximately \$79,000. The
6 company also reimbursed the entity for certain general and
7 administrative expenses incurred on behalf of the company in
8 the amount of approximately \$15,000."

9 Do you know if this related party transaction
10 refers to Madoff Securities?

11 A Possibly. I know we did have conversations with
12 Bernard Madoff specifically about Cohmad where he went into
13 like an hour story about Sonny Cohn and all the people behind
14 it and they were just family, friends, and he was letting
15 them have space and then we asked, because we saw checks
16 being paid to Cohmad Securities, it was like a 100,000 a
17 month or it totaled somewhat significant amount of money, but
18 he basically told us that Cohmad Securities was used to
19 provide advice on how Bernard Madoff's firm should handle
20 their government bonds and their securities and stuff and
21 whatever it was, I know we documented it, you know. Peter
22 had written some notes and we had a file and we provided it
23 to the staff that went out to Cohmad Securities in December
24 of 2008.

25 Q Okay. If you look through the Madoff Investment
26 Securities Annual Audited Report, do you see that that

1 related party transaction is not listed on the Madoff Audited
2 Report?

3 A Well, it's different time periods. The one is from
4 July or 07/1 of 2002 to '03 and the other one is from
5 November of '03 to October of '04. So --

6 Q If we --

7 A -- if we had a matching year to year or something,
8 possibly there'd be no mention of one versus the other. I
9 don't know.

10 Q So if you have -- have the Annual Audited Reports
11 for the same year and the related party transaction is not
12 also in the Madoff Securities Annual Audited Report, that
13 would be something notable for an examiner, correct?

14 A Yes, but at the same time I wasn't doing an
15 examination of Cohmad. It was really during pre-exam work
16 where I run a bunch of searches in google and see who else is
17 in the same building and, you know, so on the directory and
18 figured out that Cohmad is Cohn and Madoff.

19 So -- so if we took it any further, I don't know.
20 I mean, I'm sure we brought it to John's attention, the
21 Cohmad relationship, but after we got the story that he's
22 just helping them manage their bonds, you know, how much more
23 can you, you know, keep going?

24 Q Okay. Great. Thank you.

25 A I do often go into the notes of the annual audits
26 to try to get information that I wouldn't get otherwise with

1 the firm to try to tie it back, link it together.

2 (SEC Exhibit No. 12 was marked for
3 identification.)

4 MR. KOTZ: Okay. Next, we're going to mark as
5 Exhibit 12, this is an e-mail from you to John Nee and Peter
6 Lamore, 3/23/2005, 12:58 p.m.

7 (The witness examined the document.)

8 THE WITNESS: I think I did contact Personal Privacy at
9 some point.

10 BY MS. STEIBER:

11 Q Who is Personal Privacy?

12 A I don't know. I guess someone who worked in IA,
13 possibly. I don't know. But whoever it was, whoever made
14 the -- unless -- maybe I didn't talk to her.

15 Q Why -- why would you have contacted Personal Privacy, do
16 you think?

17 A Either to try -- we were probably either in the
18 field already and we were trying to get a copy of the report.
19 So I don't know if I called or -- maybe we did speak to her.
20 I'm not sure.

21 Q Do you think in an exam like this that's focused on
22 hedge fund trading, it would be helpful to have investment
23 advisor assistance?

24 A Yes, and at the same time I tried doing a lot of
25 the research myself to find out whether he should be
26 registered as an investment advisor then and brought that up

1 MR. KOTZ: The next document we're going to mark as
2 Exhibit 13 is an e-mail from Ostrow, you, to John Nee,
3 Thursday, March 24, 2005, 1:12 p.m., and attached is an
4 Initial Documentation Request List to Bernard L. Madoff
5 Investment Securities, dated April 1, 2005.

6 (SEC Exhibit No. 13 was marked for
7 identification.)

8 THE WITNESS: Mm-hmm.

9 BY MR. KOTZ:

10 Q It references in here, "John's corrections." Do
11 you recall any particular corrections that John Nee made?

12 A The specific corrections, no, but I most likely
13 brought them over a printed copy. He made a few maybe
14 grammatical corrections, maybe asked me to ask for something
15 specific and I went and made those corrections and this is
16 the e-mail.

17 Q Okay.

18 A Which, you know, sometimes even just looking in my
19 In Box of archived e-mails, when you look at a whole stream
20 of e-mails, sometimes it looks like it's an e-mail from me to
21 someone else but, you know, clearly it isn't, and I don't
22 know how they get jumbled like that. So it's even weird just
23 how I'd be writing to John saying here's the latest version
24 with John's corrections and why it wouldn't have been either
25 to Peter or from Peter or -- so sometimes things get lost in
26 translation there or get lost in the conversion.

1 Q Okay. Do you know on Page 3 of the attached
2 document request, there's references to "Anti-Money
3 Laundering Program?" Do you have any idea why those
4 questions would be asked?

5 A Page 4 or Page 3 of the request. Sorry.

6 Q Yeah.

7 A It's standard for us to ask for those documents. I
8 mean, I basically work off a template for each of my firms'
9 request lists and tweak it accordingly to the type of firm,
10 if it's a real estate firm or something, asking different
11 questions.

12 Q Okay. Do you know if at any point you went back to
13 the Investment Adviser #1 e-mails to determine how to define
14 what to put in the document request?

15 A No, I don't. I don't believe so.

16 Q Was there a request for trading data in the initial
17 document request?

18 A We asked for inventory positions in the Net Capital
19 and Financial Reporting, Number 8, Trade Date, Settlement
20 Date, Inventory, as of December 31st, 2004. So that would
21 have -- but not the specific customer transactions, that we
22 usually get into later. Some of it might show up on a Failed
23 to Deliver Report, Stock Borrowers, Stock Loan might have a
24 list of it, but these are just usually so we can tie into the
25 Focus Reports.

26 Q Okay. So generally, the specific type of customer

1 account statements wouldn't be requested in the initial
2 document request?

3 A Correct. And we were -- you know, we knew the
4 minute we started asking questions directly related to the
5 Barron's and the MarHedge article, it would get
6 confrontational and that's how it sort of was all leading up
7 to that one big meeting where we had with him and we
8 addressed all those points of that after having looked at all
9 the documents there.

10 So very rarely do we in the initial document
11 request come out with exactly what we know we're looking for,
12 trying to find, trying to figure it out as we go along.

13 Q Okay.

14 BY MS. STEIBER:

15 Q Why did you think it would be confrontational?

16 A Not related to the initial document request, but as
17 we were going, he just, you know, grew increasingly --
18 Bernard Madoff grew increasingly upset with the Exam staff or
19 the Exam Program and I know multiple times Peter would e-mail
20 back saying, you know, just talk to me, saying we shouldn't
21 be looking at e-mails, we shouldn't be doing this, and you
22 guys should know what time splicing is or slicing and what --
23 that we're talking with OCIE and, you know, so, you know, --

24 BY MR. KOTZ:

25 Q So there was a lot of pushback from Madoff on the
26 exam?

1 A Yes.

2 Q More than in other exams you've done?

3 A I mean, I've had people -- a lot of people lie and
4 stuff. So this was just really, you know, gray area, like he
5 tried to play with words.

6 Q But I'm talking about in terms of pushback saying
7 you shouldn't be doing this, giving you a hard time about
8 asking for information. I'm not talking about lying for a
9 second. I'm talking about general pushback.

10 A I've experienced it in other firms.

11 Q Okay.

12 A A minority, like maybe 30 percent of the exams, as
13 opposed to --

14 Q Okay. Have you ever experienced it to the extent
15 you experienced it with the Madoff exam?

16 A Possibly one or two other exams rival -- like come
17 close to that but maybe not to that level.

18 BY MS. STEIBER:

19 Q When you received this pushback from Madoff, did
20 you feel that, you know, need to push right back at -- at
21 Madoff?

22 A Sort of that we were stuck in the middle and just
23 being squeezed.

24 BY MR. KOTZ:

25 Q What do you mean stuck in the middle and being
26 squeezed?

1 A Maybe we would go back and tell John what -- relay
2 the information and ask to push further and just told to, you
3 know, relax or not and, you know, time to get out or, you
4 know, you've been out there long enough or things like that.

5 Q So John Nee discouraged you from pushing it further
6 when Bernie Madoff would pushback?

7 A Sometimes him, sometimes even Pete would say
8 let's -- let's wait and ask him this in the big meeting or I
9 would say let's hold off and not put it in writing yet
10 because he would get somewhat inflamed about it and even just
11 reading through, you know, maybe e-mails when even Peter or
12 Shana would respond to complaints to whoever it was, whatever
13 entity was writing in, the tone of language, you know, they
14 were all, you know, attorneys and just the way they
15 documented it and, you know, to make sure that there was
16 always a clean record-type of approach, but that really
17 didn't stop Pete and myself from pushing forward and trying
18 to prove that they weren't front running and all the things
19 alleged in the MarHedge article and Barron's article.

20 Q Okay. All right. Why don't we talk about the
21 articles?

22 MR. KOTZ: This we'll mark as Exhibit 14. This is
23 an e-mail from John Nee to you, 4/25/2005, 4:26 p.m.

24 (SEC Exhibit No. 14 was marked for
25 identification.)

26 BY MR. KOTZ:

1 Q And you can see on the second page, this is an
2 e-mail from you to John Nee and Peter Lamore, attaching the
3 Barron's article, and referencing "This is a very similar
4 article to the one we originally had read on Bernie and hedge
5 funds."

6 So that original article, that was the MarHedge
7 article?

8 A Yeah. I guess I'm surprised. I don't know if I
9 had found -- I didn't think I had found this article.

10 Q But you read this article by Erin Arvedlund?

11 A Yes.

12 Q Okay. And one of the things said in this article
13 is, "But what few on the Street know is that Bernie Madoff
14 also manages more than six billion for wealthy individuals.
15 That's enough to rank Madoff's operation among the world's
16 five largest hedge funds, according to a 2001 report in
17 MarHedge."

18 So you were aware that Madoff was managing that
19 much money and his operation was among the five largest hedge
20 funds?

21 A No, we really weren't aware of it, probably not at
22 that point, because up until that point, I know we had a
23 meeting, it's documented in our report, where, with him and
24 Peter and whoever else, we asked do you manage money? We
25 phrased it different ways and he told us, "No, we don't do
26 that here. We're not that kind of a business."

1 So it wasn't until some time in May, May 25th, I
2 believe, where he finally said, "Okay. There are four
3 accounts," and then it was 15 accounts and then it was 14,
4 and I think he tried staying below the 15 threshold or
5 whatever it was to require them to have to register as an
6 investment advisor.

7 Q So that was May 2005 you're talking about?

8 A Correct. May 2005, when --

9 Q When you found out that --

10 A Well, --

11 Q When he admitted to --

12 A -- we had seen it in articles and that's the point
13 we were trying to get at, asking for customer accounts and
14 customer statements, and he just kept on basically giving the
15 same generic run of all the different market makers out there
16 and saying these are our customers that we trade with on a
17 daily basis. He hadn't ever admitted up until that point,
18 until May, that he did have the six billion, but we knew
19 about it based on these articles, based on Investment Adviser #1 So
20 we were looking for it, and, you know, I was -- I was -- I'd
21 be in the office on Bloomberg, looking up split strike
22 conversion, find another entity that said to use that, and
23 then would relay that information to Pete and we'd say let's
24 wait and see if he gives it to us on the list that he
25 provides to us.

26 Q All right. So if you look at the next page of this

1 article, the middle of the page, there's a reference to
2 "still some on Wall Street remain skeptical about how Madoff
3 achieves such stunning double-digit returns using options
4 alone. Three option strategies from major investment banks
5 told Barron's they couldn't understand how Madoff churns out
6 such numbers using this strategy. As a former Madoff
7 investor, anybody who's a seasoned hedge fund investor knows
8 the split strike conversion is not the whole story. Taking
9 it at face value is a bit naive."

10 So you were aware at this time that there were
11 questions about how he could possibly achieve the returns he
12 achieved using the split strike conversion strategy?

13 A Right. Correct.

14 Q And what did you do in the exam to look into that
15 issue?

16 A Questioned Bernie about it and we were told that as
17 of, I believe, January of '04, they stopped using options and
18 that was pretty much our review period. All of 2004, you
19 know, at that time he didn't really want to go back much
20 farther than that because then it's no longer real time or
21 current data.

22 Q Who didn't want to go back?

23 A In general, I think the push in the office was
24 like, you know, just don't look at stuff that's too old or,
25 you know, --

26 Q Okay.

1 go to Fairfield Greenwich and ask specifically for marketing
2 material, see if they're putting on the option strategy. I
3 mean, it was pretty clearly laid out in that one e-mail to
4 John. I don't know if you have it.

5 Q We do. We'll get there, but do you know if -- if
6 Nee relayed some of these red flags to Sollazzo?

7 A I don't know. I can't speculate. I know we had
8 conversations or Bob got back to John Nee about Mike
9 Macchiaroli because we were having a hard time just trying
10 to -- you know, we know all these articles in Barron's and
11 MarHedge said he's so secretive, he won't tell a secret.
12 Well, we're the SEC and we want to know the secret, and, you
13 know, it stays confidential with us, and we want to get into
14 the black box.

15 So we had a real -- that was one big pushback, but
16 that was an instance where, I guess, John, we went to Bob and
17 Bob talked to Personal Privacy and Personal Privacy said it
18 falls under the books and records of the broker-dealer and
19 see it and, you know, gave a report that we should quote the
20 wording from to ask for that information, for the trading
21 directive and stuff.

22 BY MR. KOTZ:

23 Q So who's Personal Privacy ?

24 A I believe he's the head of -- I've forgot offhand
25 the exact office that he works in, but he's --

26 Q Senior level guy in the agency?

1 A Correct.

2 Q Okay. And so you made efforts to get more
3 information about the particular strategy from Bernie Madoff?

4 A Right.

5 Q And it went up to Personal Privacy and the decision
6 was made that you weren't allowed to --

7 A No. That we would be allowed to request to get
8 information related to the black box trading.

9 Q Okay. And did you make that request?

10 A I'm sure we did in some sort of roundabout way or
11 asked for more information. He gave us what he had when we
12 asked him for all correspondence between the investors and
13 everyone else for like a six-month period and there was not
14 one single piece of paper, you know. Just another red flag,
15 that Bernie tells us that Frank DiPascali has no e-mail. All
16 we could do was use Frank as a keyword in our e-mail search
17 to see if he does have an e-mail account or not.

18 Q So did you ever -- were you able to ever get the
19 information on the trading strategy that you wanted to get?

20 A I would say so, in terms of the -- if we were just
21 trying to figure out how the actual black box strategy
22 worked, most of it was Bernie's gut feeling, but the way he
23 explained it, which turns out to not really -- it's a real
24 strategy that exists out there, but he wasn't implementing it
25 and basically it just went into buy 35 to 50 stocks that
26 would mimic the S&P 100 while putting on a collar of options

1 and so that was the gist of it and we -- and we read -- I
2 think we had -- I think there was a more complex document
3 than the trading authorization directive that went
4 specifically into like percentages or how it would execute
5 and when it would be executed.

6 Q So the secrecy issue that's referenced in this
7 Barron's article was also a concern of yours?

8 A Sure.

9 Q Okay.

10 BY MS. STEIBER:

11 Q Were there certain areas of the firm that Madoff
12 never let you see?

13 A Well, we didn't take it a tour of the -- what's
14 behind Door Number 17 on the 17th Floor. We had gone on a
15 tour. I mean, the whole floor itself was a big glass
16 enclosure, so you could pretty much see the trading desk
17 sitting next to us. I mean, one day we stood over Mark
18 Madoff and he showed us how he does the trading and stuff.
19 So, you know, we pretty much saw everyone who was on the
20 floor we were sitting on.

21 Q That you were sitting on, but you were never
22 allowed to see the floor where the supposed investment
23 advisor business was taking place, correct?

24 A We had no idea.

25 MR. KOTZ: I'm sorry?

26 THE WITNESS: We had no idea. We knew the floor

1 existed. We didn't know that there were any customer
2 accounts or anything, you know, being done there or anything
3 like that, just that there was a back office, a few people
4 sitting there, not related to an investment advisory
5 business, because, according to Bernie, there was no
6 investment advisory business.

7 You could even see in one of the e-mails where the
8 concern when we wanted to get trading for some of these
9 entities, I specifically said in the e-mail, you know,
10 request it today, get it today and lock it up in the geek
11 bag, the locking wheel bag which now isn't even that secure,
12 I guess, but before the weekend because we didn't want to
13 give Bernie a chance to -- I believe what I was thinking was
14 we don't want to let him cherry-pick or get us the best
15 statement. We want just a raw statement right off the press
16 and take it.

17 BY MS. STEIBER:

18 Q Did you have trouble getting Madoff to produce
19 documents quickly?

20 A Sometimes speed was an issue. I know there was one
21 instance, I think, where they -- they probably came and took
22 something back. We sort of just -- we don't know if it was
23 deliberate or we just asked for whatever document it was
24 again. I believe it was the Annual Audit and we had to ask
25 them again for it because either Shana or someone came in and
26 took a stack of documents back from us and might have been

1 you know, it wasn't.

2 Q But were you at the time suspicious about Bernie
3 saying that he had this incredible gut feel?

4 A Yeah. We were suspicious the whole time, the whole
5 exam, after the exam.

6 Q So what were your suspicions when he -- he would
7 say this about the gut feel and his amazing timing?

8 A Pete and I would just both, you know, shake our
9 head or just in amazement or we would e-mail each other and,
10 you know, every time like he'd write it in a report or
11 something like that. We were able to get that into the
12 report, to say about the gut feel and stuff and, you know, so
13 in that sense, I know everything we did out there was well
14 documented in the report, what we looked at, who we talked
15 with, you know, and --

16 Q So you had these suspicions about the gut feel, but
17 you didn't really come to any conclusion about how he was
18 able to do it?

19 A I wouldn't say that we didn't come to a conclusion,
20 but we were able to rule out that he wasn't trading at the
21 same time that his market making side was trading, or prop
22 traders were trading. We were able to rule out -- you know,
23 we, of course -- when he handed us a statement for Fairfield
24 or Kingate or one of those entities, you know, we verified
25 that the prices and dates and -- all made sense on those
26 statements, you know.

1 But these are statements handed to us from the
2 president of the firm. Or, if we got them in electronic
3 format, you know, it's something that's produced by their IT
4 department, and you know --

5 Q But it's fair to say that, even at the end of the
6 exam, you were still suspicious about how Madoff was able to
7 achieve those returns that he did?

8 A No, I wouldn't say suspicious about how he achieved
9 those returns, because we knew it wasn't being smoothed out
10 from market making, we knew it wasn't insider trading. We
11 knew -- you know, it was just questionable, still, as to the
12 gut feel.

13 And the biggest thing in my mind was just the --
14 not using options any more, when that was the whole -- you
15 know, 50 percent of the gist of it was having options as part
16 of the strategy. So how can you -- if anything, just who can
17 we cite and how can we cite it for misrepresentation of
18 marketing material, but at that time hedge funds weren't
19 registered.

20 It wasn't, you know, according to John, the focus
21 of the exam, and to just focus on, you know, proving these
22 other points.

23 Q Right --

24 BY MS. STEIBER:

25 Q Did Madoff also claim that he was doing all the
26 trading himself?

1 What does that mean, that Barclays clears for the
2 brokers in London, delivery in the U.S., and paying them?

3 A I don't want to speculate on what Peter is saying,
4 but basically that the London affiliate or branch of Madoff
5 Securities used Barclays to clear their trades.

6 Q Okay. And then it says, "Additionally, in the same
7 operating account, I came across some weird descriptions that
8 I asked Bernie to explain." Do you know what was weird about
9 those descriptions?

10 A No, you would have to ask Peter. I forgot. I
11 mean, if you showed me documents showing that 10.75 million
12 credit, I might be able to recall or remember.

13 (SEC Exhibit No. 18 was marked for
14 identification.)

15 BY MR. KOTZ:

16 Q Okay, I will show you another document marked as
17 SEC Exhibit No. 18. It is an e-mail from John to you and
18 Peter, 5/3/2005, 3:18 p.m. And attached is a document
19 request to Barclays dated May 3, 2005. So what do you recall
20 about this?

21 (The witness examined the document.)

22 THE WITNESS: That we were trying to verify that
23 some of those fund-to-funds did, in fact, have accounts as
24 Barclays, as per what Madoff had said.

25 BY MR. KOTZ:

26 Q And did you verify that?

1 A This letter was sent out, a response was returned.
2 What exactly the response says, you would have to look at it.
3 I mean, this was -- the letter was addressed to John Nee,
4 came back to John Nee.

5 Q Okay.

6 A And it came back probably after we were back in
7 from the field, but I don't know what --

8 Q So you don't know whether you were able to verify
9 what you were looking for in this --

10 A I believe after -- when I was putting the boxes
11 together, and seeing that letter back from Barclays, I
12 believe it said, "This is the U.S. version, and you would
13 have to contact London," or something. But, "He did open an
14 account here," but it had just recently been opened, or
15 something to that effect.

16 You would have to look at specifically what she
17 said in the letter. But it didn't deny that there were
18 accounts there, but just that they were, you know -- contact
19 them, or something, I don't know. I don't know what the
20 follow-up was.

21 Q It didn't provide the trading -- it says, "All
22 trading done by or on behalf of any of the following." That
23 letter didn't provide that trading?

24 A Yes, I believe Barclays Capital, Inc. is the U.S.
25 broker-dealer.

26 MR. KOTZ: Okay, and they were just referring --

1 okay. Mark this as SEC Exhibit No. 19. This is a letter
2 from Erin Ashley Mansfield, director of compliance, to John
3 Nee, May 16, 2005.

4 (SEC Exhibit No. 19 was marked for
5 identification.)

6 MR. KOTZ: You see in here it says, "No relevant
7 transaction activity occurred during the period March 1, 2005
8 through March 31, 2005. There were no other customer
9 relationships identified at Barclays Capital for the other
10 names provided in your inquiry letter."

11 (The witness examined the document.)

12 BY MS. STEIBER:

13 Q Do you recall discussing this letter with Nee?

14 A I don't recall. If you check in the e-mails, if --
15 there is possibly an e-mail after May 16th where I state that
16 there should be trading activity in March some time. And
17 basically Bernie explained it that, "Well, the trade was
18 entered in January, so therefore it's just being executed in
19 March, and that's why it's not on our dated CD."

20 And I said, "Is that just semantics, also," to
21 John, and I don't know what the outcome was, but you know,
22 once again, I guess other red flags that the accounts were
23 just opened, and there were no trades for the other entities,
24 but you know, Bernie had a story for everything, and --

25 BY MR. KOTZ:

26 Q But that particular story that Bernie gave for this

1 matter, it didn't convince you that the matter was resolved?

2 A Just, once again, I had never seen something like
3 that, where a trade can be entered, not executed until two
4 months later because of a black box where a trade is just
5 sitting, and it just -- it didn't seem right, and we relayed
6 those concerns, and you know -- but we did take the next
7 step, or John, he took the next step, and wrote to Barclays.
8 And this was the response back.

9 MR. KOTZ: Okay.

10 BY MS. STEIBER:

11 Q And did you contact the Barclays UK affiliate?

12 A I don't know. I didn't. The last sentence,
13 though, that "A prime brokerage and trading relationship with
14 a Madoff-affiliated entity exists with our UK affiliate,
15 Barclays Capital Securities," that, once again, tied into my
16 concerns that the UK London office of Madoff should be
17 registered, and should be an entity that should be listed on
18 wherever -- but once again, that wasn't really -- you know,
19 John said that wasn't the -- eye on the prize, and we can't
20 really do much about telling them to register.

21 But stuff we were seeing, in terms of letterhead
22 and things referencing London, and them shutting down the --
23 like when they would -- like, if London was open but the U.S.
24 had a holiday, the offices here in New York were doing the --
25 making sure the systems were still up and running.

26 So, it just seemed like they were more interrelated

1 than just trading a little bit of Bernie's money off to the
2 side.

3 Q Right. So you would have expected that the London
4 office would have records, just like the U.S. office would
5 have records, right?

6 A Right. I mean, we were getting the trade data from
7 Bernie, which then was told to us that, "These are being
8 cleared through London, through Barclays," you know, so --
9 but he was -- then he said, "These are the statements that
10 the clients get," the ones he presented to us. So we were
11 just going to an outside source to try to verify that.

12 Q And you tried to go to an outside source, and you
13 were unable -- I mean, and you received a letter back that
14 said, "We have no records of trading with Madoff." At that
15 point did you ever discuss with John Nee seeking records in
16 the UK, and did John Nee say that you couldn't do that?

17 A I don't recall if we wanted to seek documents. It
18 was more so make Bernie acknowledge that the London office is
19 an affiliate versus branch, or branch versus affiliate. And
20 there were even e-mails back and forth internally at Madoff
21 between Shana and Peter, whoever it was, with an e-mail
22 about, I think, New York stock exchange regulators going to
23 see a branch office of a firm that -- they weren't afraid to
24 go and examine there. So it just made me think that it
25 should have been brought under the umbrella of the
26 broker-dealer.

1 Q But -- and you remember thinking that, and you
2 discussed it with John Nee, and he said, "That's not our
3 focus?"

4 A In the e-mail he wrote back specifically saying the
5 London thing is not our -- like, it's a tertiary, at best,
6 and the IA business also is not as -- you know, our focus
7 right now.

8 Q Okay.

9 A But even a letter like that, like -- we probably
10 pushed hard to write a letter to Barclays, and he did send
11 the letter. So, I mean -- and the response we got back tied
12 in with the responses that Bernie was giving us, so --

13 (SEC Exhibit No. 20 was marked for
14 identification.)

15 BY MR. KOTZ:

16 Q Okay, the next one is SEC Exhibit No. 20. This may
17 be that request that you mentioned. This is an e-mail from
18 Peter to you, 5/3/2005, 3:47 p.m., and it forward an e-mail
19 from Peter to John saying, "I would like to get the e-mail
20 trading data that we have requested, in addition to the
21 Barclays information from your request before we confront
22 him."

23 I'm sorry. Yes, actually, if you look -- why don't
24 we go all the way down to the bottom, so we can --

25 A So he sent the request, and then he forwarded it to

1 me and Peter.

2 Q Now, Peter says in here, "No problem. I'm ready to
3 call his bluff on his refusal to admit the money management
4 side of the business. So your document request is perfect
5 timing." Do you know what that was all about, calling his
6 bluff?

7 A Because up until that point, he had just kept
8 telling us that he doesn't run any money, or doesn't have any
9 of these investment advisory relationships.

10 Q And you found that that wasn't true?

11 A Coming down to semantics, he just considered
12 himself as not really managing the money, just -- these
13 people told him how much money they were going to give him,
14 and he was going to implement his strategy. So they were
15 basically using his system, or, you know --

16 Q And then in Peter's e-mail to John Nee at the top
17 it says, "I would like to get the e-mail trading data that we
18 have requested, in addition to Barclays information from your
19 request before we confront him. Also, I think it would be a
20 good idea to be ready to speak with the funds as soon as
21 possible after he denies his involvement with them." What do
22 you remember about that?

23 A Well, just that we're gearing up for the big
24 sit-down on May 24th, May 25th, whenever it took place, to
25 basically -- we knew, based on the articles, he was running

1 the \$7 billion. We asked for all customer accounts at the
2 firm, don't see \$7 billion. Where is it?

3 And it wasn't until that meeting that we then --
4 finally he came out and started naming four of the entities,
5 five of the entities. We knew there were maybe 8 or 9
6 entities, closer to 15. We didn't know if he was just trying
7 to keep it below the threshold for registering.

8 So, we knew it was going to, like, be -- basically,
9 he will be able to tell you better what was going through his
10 mind, because you know --

11 Q Okay. So, essentially, you had information from
12 the articles that contradicted what Bernie was telling you.

13 A Mm-hmm.

14 Q Is that right?

15 A Correct.

16 Q Okay. And then, you wanted to get kind of verified
17 information in your hands before you confronted him with this
18 statement that you knew that the information he was giving
19 you was not accurate.

20 A Correct.

21 Q Okay. And so, the information that you were going
22 to get to confront him with were the Barclays information,
23 and to speak to the funds. Is that right?

24 A To speak to the funds after he once again --

25 Q To get --

1 follow-up -- like I don't --

2 Q Did you ever figure out why this guy got such --
3 this compliance guy got such a high salary?

4 A Why high and then low and then high again? Or why
5 high in general?

6 Q Yes. Either one.

7 A I wouldn't -- \$400,000. It could be a little high,
8 but you know, maybe \$300,000 is more in line. But I
9 believe -- we might have asked, and -- I don't recall,
10 exactly. I think -- I don't know if he was out for part of
11 the year in 2004. I don't recall --

12 Q Okay. What about this thing --

13 A I don't remember.

14 Q -- "Any more info on the OCC options account?"
15 What is that about?

16 A I'm not sure if you have statements about OCC
17 option accounts, or if that would have been the account where
18 the option part of the split conversion would have been in,
19 but I don't remember --

20 Q What is OCC?

21 A Not sure. It might have just been an internal
22 designation to their options --

23 BY MS. STEIBER:

24 Q And then you say, "I sent an e-mail to

Personal Privacy

25 [REDACTED]"

1 A [Personal Privacy] yes.

2 Q Do you know why you would have sent an e-mail to
3 him?

4 A I think I just finished an exam for him. He's
5 another branch chief, like [Personal Privacy] And since I said he was
6 probably looking for the STARS completion sheet -- that's the
7 sheet we fill out at the end of an examination, so --

8 BY MR. KOTZ:

9 Q And what is the STARS?

10 A STARS?

11 Q Yes.

12 A It's statistics tracking analysis reporting system,
13 or something, that the administration staff punches in what
14 the results are that then get filed down to OC, I believe.

15 Q And it has in that system the audits that are done,
16 or examinations that are done?

17 A Possibly, but I don't think it would be a system
18 that we would use, necessarily. Sometimes I have called an
19 administrator -- or not an administrator, administrative
20 assistant, and said, "Can you look up an exam number," or,
21 "When is the last time a firm was done?" But I think there
22 is another system that's used for that.

23 But this -- none of -- those two sentences or three
24 sentences don't have to do with Madoff, just had to do
25 with -- I probably received a voice mail and you know, or

1 something, and trying to follow up with Jeff.

2 Q Okay.

3 A And you could probably find in my e-mail the exact
4 e-mail I sent to Personal Privacy, if I did, in fact, send it,
5 because in that e-mail I probably said, "I'm working on
6 Madoff stuff, by the way."

7 Q Okay. Well, now we don't have to talk to Personal Privacy

8 [REDACTED]

9 A I'm sure he will be glad.

10 MR. TALARICO: I'm sure he will be glad. He's a
11 very nervous guy.

12 MR. KOTZ: I'm glad that we don't have to speak to
13 him.

14 Okay, the next document we're going to mark as SEC
15 Exhibit No. 22, which is from you to Peter Lamore, dated
16 5/18/2005, 10:24 a.m.

17 (SEC Exhibit No. 22 was marked for
18 identification.)

19 BY MR. KOTZ:

20 Q Okay, "Swing by Donna Smith's desk, consumer
21 affairs, and pick up a complaint she received. She sits by
22 Sandy, Richard Lee, and Personal Privacy. It's a customer
23 complaining about a trade done through Fidelity which, in
24 turn, was routed through Madoff. The date was 3/21/2005. I
25 guess we can always just have the firm run off all the trades

1 in TWX that day, although it could be a lot. Thanks." Do
2 you remember this at all?

3 A Yes, of course. I mean, we were so focused and in
4 the zone on this exam that anything we can get our hands on
5 related to Madoff that might tie in somehow to any sort of
6 complaint, or any sort of issue, we acted on immediately.

7 So, here is someone who is working the consumer
8 affairs desk, gets a call about Madoff, looks on a list, sees
9 that someone happens to be at that firm and tells us about
10 it. We picked it up that day. We requested the data. It
11 was basically someone just saying, "I have an account at
12 Fidelity, I bought Time Warner, and I got gypped \$.10 or
13 \$.15," or whatever per share on Time Warner, whatever the
14 exact complaint was.

15 So, we looked at it, you know. I believe we
16 requested the trading data for that day, or we asked the firm
17 about it, whatever it was. But we were, you know, definitely
18 on point in terms of, you know -- the detailed review we did
19 related to the three stocks where we did cite the firm for.
20 You know, it took a lot of time and a lot of just converting
21 data and using Access and Excel and --

22 BY MS. STEIBER:

23 Q Do you recall if this complaint was resolved?

24 A I don't know if -- when you say "resolved" --

25 Q Did you determine if the complaint that had been

1 sent in to consumer affairs was -- you know, you resolve it?
2 Did you figure out if it was correct or not?

3 A I mean, this wasn't one of the major -- like I know
4 we acted on and looked into it. It should be in the work
5 papers, or it should be there, in terms of -- you know, at
6 the same time I know Donna Smith usually would send a letter
7 to the firm saying, "This customer complained. Write back
8 within 30 days." So, in that sense, you know --

9 Q So you think you would have documented resolution
10 of the complaint, or your findings from the complaint?

11 A Documented? Possibly not, but looked into, yes.
12 And if it would have been something, it would have been
13 documented. Usually exceptions are the ones that go into the
14 report, and things like that.

15 Like if we had found a problem at Time Warner, it
16 would have been mentioned right along OITN and the other, you
17 know, EGHT stock.

18 Q Would you have gone back to Donna Smith to let her
19 know how this complaint was resolved, or your findings?

20 A No, that's probably a weakness of the SEC, in
21 general, just in terms of -- you know, sometimes tips or
22 complaints come in, but what is the way to handle it
23 afterwards? You know, it was great that we got it while we
24 were there on site.

25 But, I mean, it wasn't something to the point where

1 we thought we needed to contact the customer who was writing
2 in, or it was something that -- you know, the nature of it
3 was not as severe, or just -- I don't recall. If you have a
4 copy of the Time Warner complaint, I will look at it. But we
5 should have it. I'm sure Pete picked it up and brought it
6 out. And I know we either asked for that day, or we might
7 have sat down and looked over his shoulder and looked at the
8 trades that day. I don't know what exactly happened to
9 resolve that.

10 MR. KOTZ: All right, I will show you the next
11 document that will be marked as SEC Exhibit No. 23.

12 (SEC Exhibit No. 23 was marked for
13 identification.)

14 MR. KOTZ: And this is an e-mail from Peter to you
15 and John Nee dated 5/23/2005, 10:56 a.m. There is a
16 reference to an article that was forwarded. And it says in
17 here, "Key issue here is the statement regarding the status
18 of foreign affiliates."

19 BY MS. STEIBER:

20 Q Was this the e-mail you referred to earlier?

21 A Yes.

22 Q Could you just describe the contents?

23 A An e-mail from Andy Madoff to Shana Madoff and
24 Peter Madoff, forwarding an article from Institutional
25 Investor from June 22, 2004, which talks about the New York

1 Stock Exchange conducting inspections of overseas
2 broker-dealer branches.

3 And I believe there is mention in there about the
4 difference between affiliates and branches, possibly. Yes.
5 "It will be conducted at foreign branches of a U.S.-based
6 member firm, but not foreign affiliates of those firms."

7 BY MR. KOTZ:

8 Q So there was an internal issue there about whether
9 those branches are affiliates?

10 A I wouldn't say it was an internal issue. It was
11 more just the family members e-mailing it around, and then
12 just Peter Madoff sending an e-mail to Andrew and Shana and
13 Alan, talking about the key issue being the status of foreign
14 affiliates. So I don't know what they were thinking.

15 Q And why was it relevant for your exam?

16 A I believe around that time Pete and I were of the
17 mind set that London should come under the umbrella of the
18 broker-dealer, and don't refer to it as an affiliate, but not
19 have it registered or -- you know, and we tried doing
20 research and find out how we could get them to register, or
21 how to cite them, and it just wasn't easy.

22 Q And so, what was the reaction from John Nee about
23 this issue that you raise?

24 A I believe he just said it's not -- it's tertiary,
25 at best, or you know, not the top of the list. "Keep your

1 eye on the prize."

2 MR. KOTZ: Okay. The next document, mark it as SEC
3 Exhibit No. 24.

4 (SEC Exhibit No. 24 was marked for
5 identification.)

6 MR. KOTZ: This is an e-mail from you to Peter
7 Lamore dated Tuesday, May 24, 2005, 11:57 a.m.

8 (The witness examined the document.)

9 BY MR. KOTZ:

10 Q Do you remember there were attachments to this
11 e-mail?

12 A Mm-hmm.

13 Q What are these attachments?

14 (The witness examined the document.)

15 THE WITNESS: I believe OPG refers to "opening," as
16 in the opening bell, or the opening stock trades.

17 BY MR. KOTZ:

18 Q So, are these audit trail and execution data?

19 A Yes, I believe so.

20 Q Okay. And the execution times of these
21 transactions are during standard U.S. trading hours. Is that
22 right?

23 A Yes, it looks like, I think, military time: 1555
24 would be 3:55.

25 Q Does this data reflect any trades executed during

1 explaining our mission."

2 You had mentioned that earlier. What exactly did
3 he say?

4 A What exactly did Bernie say? Because I wasn't in
5 that meeting.

6 Q Oh, okay.

7 A He says -- I was supposed to be in the meeting, and
8 then he just started going off, and then -- but he offered to
9 repeat it for me when I got out there, for Bernie. Bernie
10 would repeat it, but he was just summarizing his discussion.

11 Q Right. And did Bernie repeat it for you?

12 A I don't believe he necessarily went into time
13 slicing and reviewing e-mails. But -- whatever it was. But
14 in terms of the MIS system and ROBO, he did go over it, or
15 someone else came in and explained it. So we did, you know,
16 have --

17 Q Okay.

18 A -- more of a sit-down with him.

19 Q And then, at the end of this e-mail, Peter says,
20 "Anyway, I look forward to speaking with him regarding the
21 hedge fund issue which he has opportunistically failed to
22 mention to us."

23 A Yes. I mean, we're out there for two months, and
24 you know, he is -- in our mind, he has been lying to us the
25 whole time, saying he doesn't run this \$7 billion, or has

1 made no mention of it.

2 And it comes down to semantics of, "Well, I'm just
3 managing the money, I'm not collecting 2 percent, I'm only
4 getting \$.04." And the frustration of, you know, how do we
5 get this from him, and -- you know, and at the same time, we
6 have to wind up our exam pretty soon, and yet we still don't
7 feel comfortable knowing even the basics about the technology
8 group's systems, and how they work, because --

9 Q Why --

10 A -- we're just trying to figure out the language
11 that they use.

12 Q Why did you have to wind up your exam pretty soon?

13 A Why exactly right then? Just -- I mean, when we
14 first fill out an assignment memo, or when the assignment
15 memo is given to us, it usually has a time frame. And if it
16 says five weeks, the minute you're out there five weeks and a
17 day, or even around four weeks, you're told, "Start wrapping
18 up," or, "How are things going," and they want you out,
19 because they know that -- unfortunately it comes down to,
20 sometimes, numbers, and quantity, not quality, and --

21 Q So when you say they want you out, who is "they?"

22 A I guess your supervisor gets pressure from his
23 supervisor who gets pressure from their supervisor, which is
24 Bob, and then, ultimately, maybe he is getting pressure from
25 OCIE to churn out certain numbers.

1 Q So was that -- at any point in this particular
2 matter where you had talked about -- or gave the impression
3 that you wanted to stay longer, and it was told to you, "You
4 know, our time period is almost up?"

5 A Not necessarily to stay longer there, because we
6 were pretty much just banging our heads against the wall with
7 Bernie and not getting anywhere, and having a hard time
8 deciphering whether it's 13 customers, 14 customers.

9 So, once we got back, then we wanted to continue
10 on, at least in the sense of going to Fairfield Greenwich and
11 following up and seeing where it would go from there.

12 Q And you were told that the exam has got to be
13 wrapped up?

14 A The on-site portion of the exam came back -- I
15 think there is an e-mail where we say, you know, "We will be
16 back in the office next Monday or Tuesday," and you know, "We
17 will take it from there," and I think we sent out another
18 request or something to the firm, and then I was on my next
19 exam a few months later, a month or so later, whenever it
20 was.

21 Q So, you understood that, you know, this exam had to
22 be wrapped up and you had to move on to the next one?

23 A Correct. I might have even started my next exam
24 while it was being wrapped up, because I just remember John
25 sending final versions of the exam back and forth at the end

Pages 81 through 82 redacted for the following reasons:

Law Enforcement

1 who was so known for technology wouldn't have any e-mails?

2 A Not necessarily strange, but just -- you know, he
3 probably didn't. I mean, I don't know if they ever found
4 e-mails for him, but he probably didn't, and he just had
5 other people technology savvy working for him. And his
6 brother wrote a lot of the programs, and he just surrounded
7 himself with smarter people, I guess, if you will.

8 And he had people from, you know, Primex coming in
9 and running the systems, and working on the algorithms, and
10 the --

11 Q So you had the impression from Bernie that he
12 himself wasn't that technologically savvy?

13 A Correct. I mean, there was times where he would
14 have to -- based on Peter's e-mail, "He's running out and
15 asking a question, he's running out and asking a question."
16 But anything he could fluff over with a two-hour story, he
17 would try to get away with that. And you know --

18 MR. KOTZ: Okay. Okay. Want to break? It's up to
19 you.

20 THE WITNESS: Maybe a bathroom break in a half-hour
21 or so.

22 MR. KOTZ: Okay, just let me know.

23 THE WITNESS: Okay.

24 MR. KOTZ: Going to move to the next exhibit.

25 We're going to mark this SEC Exhibit No. 27.

1 at this e-mail, you don't see any attachment, you don't see
2 any sort of paper clip signifying it. So that was sort of
3 what we were coming up against with Shana's e-mails, in that
4 she deleted it, where it specifically said, "Deleted," a
5 file, and we asked them to retrieve that file. So sometimes
6 it just -- you know, you don't see it.

7 So, whatever it was, we asked for a few attachments
8 that they hadn't provided, and I believe they did print out
9 certain attachments for us, the firm.

10 (The witness examined the document.)

11 THE WITNESS: Are we just on this second paragraph?

12 BY MR. KOTZ:

13 Q Yes. Well, I guess --

14 A What's the question?

15 Q "He was somewhat vague regarding the actual
16 execution and clearance of trades." Do you remember that?
17 In what way was Bernie Madoff vague regarding the actual
18 execution and clearance of trades?

19 A I don't think I was in that meeting, and that's in
20 the e-mail from Peter to John.

21 Q Okay. But it -- John says to Peter, with a copy to
22 you, "In talking to William," so that's you.

23 A So I believe I was in the office and ran into John
24 in the hall. And then --

25 Q Do you remember the issue of trying to find out

1 more about the actual execution and clearance of the trades,
2 what information you were trying to get?

3 A I'm sure we asked the questions during that meeting
4 that the rough draft write-up is included, but probably in a
5 vague answer that didn't satisfy John's. And I'm sure we
6 continued on to ask those questions.

7 Q Did Bernie Madoff have a habit of providing kind of
8 vague answers to your questions?

9 A I would say so. Vague or misleading, extremely
10 misleading.

11 Q Okay.

12 BY MS. STEIBER:

13 Q Did you feel like you tried to ask him a pointed
14 question, and he would tell you a story in return?

15 A Yes, yes, definitely.

16 BY MR. KOTZ:

17 Q And he would never actually answer the question?

18 A Correct.

19 Q Okay.

20 A Or, there were times when he did answer a question,
21 but it was just a lie, you know, going back to Cohmad
22 Securities, when we said, "Why do you pay them 100,000,"
23 whatever it is, "a month," he said, "To manage our government
24 bonds and stuff, to help us structure our own broker-dealer's
25 portfolio," which we also thought was strange, because here

1 is someone supposedly managing \$7 billion, someone with a
2 market making side, and he is having this other firm instruct
3 him on how to handle, you know, \$800 million worth of
4 government bonds. It seemed odd.

5 So, he -- but he gave us an answer. He said he's
6 an old friend, "We give him space there, this is what he is
7 doing." You know, you try to take people's words for it, and
8 you -- you know, we thought it might be a good idea to do a
9 follow-up exam one day, and that's it.

10 Q All right --

11 BY MS. STEIBER:

12 Q Do you think in the exam program they take the word
13 of the registrant too often?

14 A As opposed to verifying without outside source
15 documents?

16 Q Right, right.

17 A In the past? Yes. I mean, I have seen recent
18 e-mails come out saying, "We're going to start going to
19 outside sources." So --

20 MR. KOTZ: Okay. I will show you the next
21 document. This is an e-mail from Bob Sollazzo to John Nee,
22 5/26/2005, 3:56 p.m. I'm going to mark this as SEC Exhibit
23 No. 28.

24 (SEC Exhibit No. 28 was marked for
25 identification.)

1 BY MR. KOTZ:

2 Q And in this e-mail, Bob says, "Bernie is fessing
3 up. I could only access part of the memo, but it sounds like
4 we may have something to review: directed executions. You
5 wonder what his benefit beyond commissions." Do you know
6 what he was fessing up to?

7 A Well, I mean, this is an e-mail I didn't have,
8 because this is Bob Sollazzo to John Nee, so I don't want to
9 speculate. But, based on the rough draft write-up that Peter
10 gave to John, which John gave to Sollazzo it was that finally
11 he was acknowledging the fact that he does have a handful of
12 investment advisory clients.

13 Q Okay. And then it says, "You wonder what is his
14 benefit beyond commissions." Do you know what that issue is
15 referring to?

16 A Once again, I believe in the rough draft write-up
17 that's sent around it talks about Bernie saying he's happy
18 with just the \$.04 commission. But I guess I don't know what
19 Bob is wondering, in terms of, you know --

20 Q Perhaps why he --

21 A Why only just commission, when he could be
22 registering as an investment advisory, and you know, all the
23 allegations that Barron's and --

24 Q Right.

25 A Why not take it all from himself?

1 Q Okay, I will show the next document.

2 A Okay.

3 MR. KOTZ: Mark it as SEC Exhibit No. 29.

4 (SEC Exhibit No. 29 was marked for
5 identification.)

6 BY MR. KOTZ:

7 Q This is from Eric Swanson to John Nee dated
8 5/26/2005, 3:57 p.m. This is what we -- we talked about this
9 a little bit before, in terms of you finding out from Bernie
10 that there was this other exam going on at headquarters.

11 How much information did you get from the folks in
12 headquarters about what they had done?

13 A What they had done? Not much information. I know
14 we ultimately got the trading data they were looking at, some
15 information, but basically just -- I remember on the call --
16 I don't know who said it, someone from OCIE basically, "He's
17 a very powerful person, Bernie, and you know, just remember
18 that."

19 Q Someone from OCIE?

20 A Yes --

21 Q From headquarters?

22 A It was either -- I think John McCarthy and Eric
23 Swanson were on the phone call. I don't know if Mark -- one
24 other person might have been on the call when they were down
25 there. But basically, just, "He is a very well-connected,

1 powerful person."

2 Q So, one of those three people said that, either
3 McCarthy, Donohue, or Eric Swanson?

4 A Unless there was an additional person in the room.
5 But we definitely heard that, some version of it, and that
6 was that.

7 Q So you think it was one of those three people?

8 A Yes.

9 Q But you don't know which one of the three?

10 A I don't.

11 Q And what was the context in which that was stated?

12 A Well, the attachment of the letter, the MarHedge
13 article, and all the allegations, and what we were looking
14 into. And basically, this is we're communicating with them
15 after we just had this big sit-down, and he finally came out
16 saying, "All right, there is 4 or 5 customers, maybe there is
17 15."

18 So, I guess we were digging into the heart of this
19 \$16 billion, \$20 billion operation, and on that call, that's
20 where it was, you know --

21 Q Who else was on that call from New York?

22 A John Nee. I believe Pete. I don't know if he was
23 in the field, or if he called in. But I think we were all
24 sitting in a room, a conference room. I don't think Bob
25 Sollazzo was on it. I'm not sure.

1 Q And do you know if the folks from headquarters who
2 worked on the exam indicated to you that they came to any
3 conclusion about their exam?

4 A I believe it was still an ongoing type of
5 investigation, or whatever, inquiry, whatever it was
6 considered. I know Pete had written to me saying, "How could
7 we have missed this?" You know, "Sorry," or whatever. And I
8 looked on the internal system, and it wasn't logged as any
9 sort of an inquiry or any sort of an open matter under
10 investigation or anything.

11 So, I said, you know, "Don't worry, don't lose
12 sleep over it. You didn't miss it, but now we're following
13 up on it."

14 Q But what about an exam? Would an exam be on NRSI?

15 A Just the regular broker-dealer exam? No, but we
16 would check the J drive, and search the name Madoff and see
17 the last report that was issued, because sometimes we use
18 that as the starting template for our next report.

19 BY MS. STEIBER:

20 Q But what about the STARS system? Aren't
21 examinations put into the STARS system?

22 A They are.

23 BY MR. KOTZ:

24 Q Did you check that?

25 A I'm not as familiar with the STARS system, to look

1 for that. And if it's not a -- I mean, during our initial
2 interview we ask, "Are you currently involved in any SRO
3 investigations, correspondence, state regulators." So, at
4 that point, you probably have our green book, our initial
5 interview. And most likely we checked off no, because he
6 didn't mention at that point.

7 It first came out during that meeting where he
8 said, "I'm talking with all these people down in OCIE. You
9 should know this already by now."

10 BY MS. STEIBER:

11 Q So that's the first you learned that there was an
12 ongoing headquarters examination, was from Bernie Madoff?

13 A That we should have known of that, correct, yes.

14 BY MR. KOTZ:

15 Q And so, you had that conversation with the team who
16 worked on the headquarters exam. How long was that
17 conversation?

18 A I don't recall.

19 Q Was it several hours, though, do you think, or --

20 A I don't believe several hours, no.

21 Q Okay. Perhaps less than an hour?

22 A I don't recall.

23 Q Okay. And did you have any follow-up conversations
24 with them about what they had done?

25 A Me, personally? I don't believe so. I don't know

1 if John or anyone else --

2 Q Did you find the information that headquarters had
3 obtained, or work that headquarters had done in their exam,
4 useful in connection with your exam?

5 A No, not really. I don't recall exactly what data
6 they were looking at, or what they were given. It looked
7 similar to our data. We had a different time period. We
8 just went with the stuff that we had. And I know it was just
9 two boxes in Pete's office.

10 And I believe they might have looked at it when the
11 next case opened up in November, the attorneys, because I
12 remember an e-mail where it said -- like, he said, "All my
13 boxes are there," you could look at what OCIE gave him, what
14 everyone --

15 Q So the entirety of Washington headquarters' exam
16 was in two boxes?

17 A I'm not 100 percent sure if it was 2 boxes. But I
18 believe it was two boxes, or close to. I don't know if there
19 was any electronic data. I know there was a lot of time
20 spent setting up a drive for us to get access to the
21 documents, and I believe the documents were just trading
22 data. I don't know what it was, but I know we went back and
23 forth.

24 Like, we probably spent two weeks on the exam just
25 trying to get access. We spent a lot of time trying to get

1 e-mails downloaded. There was a lot of things that slow us
2 down out in the field that either increase technological --
3 technology budgets could increase. Maybe if we didn't have
4 e-mail, we would spend a lot more time -- or have quicker
5 ways of doing things.

6 (SEC Exhibit No. 30 was marked for
7 identification.)

8 BY MR. KOTZ:

9 Q Okay, I will show you another document. This might
10 refresh your recollection, a letter from Jacqueline Wood to
11 John Nee. And it does, in fact, say, "We are forwarding two
12 boxes of documents."

13 A Yes, and this is -- I think we had already come
14 back from the field already. So June 9, 2005 --

15 Q So by the time you got the boxes of documents --

16 A Yes.

17 Q -- they weren't really useful?

18 A You know, I'm sure I probably thumbed through it,
19 and I'm sure Peter went through it. And then I don't know if
20 the attorneys went through it later on, but --

21 Q But in terms of your cause exam --

22 A Yes, we were pretty much -- I mean, the report was
23 probably -- you probably saw the report being sent back and
24 forth. Possibly. It didn't get filed until the end of
25 August, so I don't want to say there wasn't time where Pete

1 might have sat down and looked through a lot of this in more
2 detail, but basically it correlated with the kind of stuff
3 that we were being provided from Bernie.

4 MR. KOTZ: Okay. I will show you the next
5 document. Mark this as SEC Exhibit No. 31.

6 (SEC Exhibit No. 31 was marked for
7 identification.)

8 BY MR. KOTZ:

9 Q This is an e-mail from [REDACTED] to Mavis
10 Kelly, dated Wednesday, May 21, 2003, 5:47 p.m. Have you
11 ever seen this document?

12 (The witness examined the document.)

13 THE WITNESS: I don't believe I ever saw the
14 e-mail, or some of these first attachments or pages. I know
15 the -- Michael --

16 MR. KOTZ: Right.

17 THE WITNESS: -- article I know very well. But I
18 think I had only seen it on Factiva. I never actually -- I
19 think I tried to find it in MarHedge, but I never found it.

20 And then, there was a Power Point presentation that
21 I know I found on Google at one point, searching for a
22 conversion or something. So I had seen one or two things on
23 the Internet that made reference to the split strike
24 conversion that looked similar to this. I don't know if this
25 was it, but --

1 BY MR. KOTZ:

2 Q All right. But in terms of this format of SEC
3 Exhibit No. 31, the e-mail from [REDACTED] to Mavis Kelly with
4 attachments, this you don't believe you saw?

5 A I don't believe I saw it.

6 Q I mean, this was in the work papers.

7 A From OCIE or --

8 Q This was in --

9 A This was electronic, or was it --

10 Q I think this was a document in the work papers.

11 MS. STEIBER: Yes.

12 THE WITNESS: A document in the work paper from
13 OCIE, or --

14 MR. KOTZ: In the papers --

15 THE WITNESS: Our two boxes for the broker-dealer?

16 MS. STEIBER: Right. If you look at the prior
17 page -- sorry, the last line, where it says work papers from
18 Mavis, that is one of the work papers from Mavis. There were
19 also some notes that were in the work papers.

20 THE WITNESS: Okay.

21 MS. STEIBER: From -- that were produced. And as
22 you see, it says Mavis Kelly.

23 THE WITNESS: Okay, yes. I don't know if I had
24 seen it, unless -- if this was paper like this -- unless
25 Peter forwarded it to me or something like -- if you show me

1 an e-mail that shows that this was forwarded to me, then I
2 guess I saw it.

3 But going through everything in these boxes, I
4 don't know -- John Nee got them. I don't know how long they
5 sat in his office. I don't really remember doing much with
6 OCIE's work papers.

7 MS. STEIBER: Okay.

8 MR. KOTZ: Okay.

9 THE WITNESS: Other than seeing the two boxes, and
10 looking at some of the trading data from -- I just remember
11 big stacks, and we looked through it.

12 BY MS. STEIBER:

13 Q Do you recall in the phone call if you discussed
14 what initiated their exam?

15 A Their exam?

16 Q Did they say anything about being suspicious? I
17 mean, sorry, a complaint about Madoff's suspicious trading?

18 A I don't recall that. I don't recall. They might
19 have mentioned it on the call.

20 Q You -- they definitely didn't draw it to your
21 attention?

22 A I don't believe -- it's number nine on there --

23 Q Okay --

24 A -- more important. But no, I don't -- I mean on
25 the phone call I don't remember what we talked about, other

1 than us telling -- basically, just saying, "We want to v
2 that Bernie is telling the truth, and that he is really
3 contact with you guys." Yes, that's it.

4 BY MR. KOTZ:

5 Q So you didn't get a tremendous amount of
6 information from them about what they had done on that call?

7 A On the call, right. And when was the call? It was
8 in the end of May or something, May 26th? Like the day after
9 our meeting, or May 27th?

10 Q Yes.

11 A So I guess --

12 Q So you don't --

13 A -- two weeks later, I don't -- I mean --

14 Q You don't recall getting a lot of information from
15 them on that call about their exam?

16 A No, because, I mean, we kept asking Bernie, "Give
17 us copies of your correspondence with OCIE, their request
18 list," stuff like that. He wasn't providing it. That's why
19 we basically -- I believe John requested them to send
20 everything as well, because we just weren't getting it from
21 him.

22 And that's documented in the e-mails that, you
23 know, we're still waiting for it, still waiting for it.

24 Q Okay. So it was more of a sense of trying to
25 confirm that Bernie was telling you the truth than getting

1 MR. KOTZ: Sure.

2 MS. STEIBER: Sure.

3 THE WITNESS: Do you guys have the original
4 assignment memo? Like just the date, so I can put it in
5 reference when I was assigned the exam, or -- or if it was
6 decided a year earlier that one day I would be doing it, or,
7 you know --

8 MS. STEIBER: The original assignment --

9 MR. TALARICO: I'm going to have to step out.

10 MR. KOTZ: Okay. All right. Why don't we -- if
11 it's okay, then we will keep going.

12 THE WITNESS: Yes.

13 MR. KOTZ: So the next document we're going to mark
14 as SEC Exhibit No. 32, and this is an e-mail from Peter
15 Lamore to you, 5/27/2005 9:06 a.m. And it's several pages of
16 an e-mail string.

17 (SEC Exhibit No. 32 was marked for
18 identification.)

19 BY MR. KOTZ:

20 Q And if you look at the third page of this e-mail
21 string, there is a reference -- you, e-mailing Peter
22 Lamore -- saying, "Maybe we should put in motion a written
23 request for," and then there is a variety of things.

24 And then you say, "Maybe verbally you can ask again
25 if he has any of the correspondence he sent to Washington a

1 year-and-a-half ago." Do you remember that?

2 A Sure. Based on the meeting we had with him, where
3 he referenced it, we said, "Can you give us a copy of it?"
4 And then, the next day, "Can you verbally ask him for the
5 follow-up?"

6 Q And so did you verbally ask him for the follow-up,
7 do you think?

8 A Did Peter? Yes, because I think there is
9 references of it even in the beginning of June. We also say,
10 "Did we get this from Bernie?"

11 Q But he never provided it to you?

12 A I don't believe he did. If we have anything in
13 there, maybe it was one cover letter or something, or the
14 initial request. But I don't believe so.

15 Q Did he give you any reason why he wasn't going to
16 provide it to you?

17 A No.

18 Q Okay. And then if you see, following on, now on
19 the second page of the e-mail, Peter responds, "Okay, I will
20 write this request. Asked him again about correspondence.
21 He said there was none, of course. I am currently trying to
22 match the trading authorization directors with the account
23 information, separate docs, and I don't think we have
24 everything. I will address any missing docs, as well."

25 First, generally, would Bernie claim there wasn't

1 documents? Is that what this is a reference to, "I asked him
2 about correspondence, and he said there was none, of course?"

3 A Well, for two months we were told there were no
4 investment advisories and no hedge funds that he was managing
5 money for. So, the fact that there was no correspondence
6 related to anything, it wasn't surprising that he just didn't
7 give us stuff.

8 Q So were there missing documents, in general, in the
9 cause exam of Madoff, documents he didn't provide, or
10 documents --

11 A In that sense, documents he didn't provide. And
12 then, when he gave the trading -- we were going to wait for
13 him to give us the trading authorization directives to then
14 make sure he was giving us for the ones that we knew from
15 Investment Adviser #1 from MarHedge, from Barron's, from Bloomberg, all
16 the different sources, to see if -- why those weren't
17 provided, as well.

18 Q And so you -- he said you were going to do that?

19 A Yes, I think he said he was writing the request, he
20 asked for the trading authorizations. Let's see. It's
21 probably in other e-mails, but we -- and in our spreadsheets
22 on our electronic files of -- all these trading
23 authorizations, which are only signed by Bernie, which, once
24 again, is odd, that, you know, it wouldn't counter-signed.

25 Q Right. And then you respond back to Peter, "Even

1 as you hand the request to him you can say, 'If some of the
2 questions don't apply, you can write -- just write n/a on it
3 and give us a copy.' Questions like Barclays at the UK
4 office might not apply, according to Bernie."

5 What did he mean by that, that that might not
6 apply?

7 A What did I mean by that?

8 Q Well -- yes, right. You say, "Questions like
9 Barclays at the UK office might not apply, according to
10 Bernie."

11 A Basically, I just thought better let's put it in
12 writing, and then, if he wants to tell us there is nothing
13 related to it, let him use his handwriting, write it on it,
14 and give it back to us, so we have a record that he told us
15 it doesn't apply.

16 Q And is that what you did, do you think?

17 A If you look through other e-mails, or if you look
18 at our work papers, you should find the written request
19 related to those six points, at least, and whether he signed
20 off on it or not. You would have to double-check.

21 But I know we went back and forth about issues like
22 this. And the fact that we don't have the correspondence,
23 most likely, in the files is because he never gave it to us,
24 just what they sent us, OCIE.

25 Q Okay. And then on the first page of this same

1 e-mail, SEC Exhibit No. 32, you say to Peter Lamore, "I think
2 that just means that the model looks at, let's say, the price
3 of 1 particular stock 200 times throughout the day.

4 Actually, I believe the model runs 200 different tests on
5 each stock. We want to drill down deeper and know the
6 if/then type statements."

7 Do you know what this is referring to, and --

8 A Yes.

9 Q Did you drill down deeper, and do this analysis?

10 A I believe he gave us some sort of -- in the trading
11 directive, it talks about how the model works. And these, I
12 believe, are some documents that came about after we had a
13 conversation with -- trying to find out more information
14 about the black box.

15 So, basically, we didn't want to just know how it
16 prices the basket 200 times throughout the day. We wanted to
17 know, like, "if/then: so if the price drops to a certain
18 parameter, then the computer or something is going to buy X
19 amount of that stock." We wanted to know exactly all the
20 parameters that the system was looking at: correlation,
21 delta, all the things that the hedge funds should have been
22 interested in, and then part of their due diligence.

23 Q But --

24 A Because it was a secretive system. Nobody knew,
25 and we were trying to figure that out.

1 A He -- I would say it started to trickle in. We
2 probably got half of the trading authorization directives.
3 Maybe we got a few more additionally, afterwards. It would
4 be in the spreadsheets.

5 Q And so, then after you got that information and
6 those statements, did you go back and ask these questions
7 that you have in this e-mail?

8 A I don't know. I would have to -- in the report, I
9 don't think we would leave an open question like that. So if
10 in the report it says -- we probably just verbally asked him,
11 and it came back to, again, that Barclays was being used as
12 the clearing agent, clearing the trades for London on behalf
13 of these 16 hedge funds, and that's how it all worked.

14 Q In the e-mail right below, Peter sends an e-mail to
15 you Friday, May 27, 2005 at 10:28 a.m. He says, "One of the
16 brokers Bernie mentioned was Commerce Bank, which I believe
17 they either built or were going to build a technology
18 platform for."

19 Do you remember if you ever contacted Commerce
20 Bank?

21 A I don't know about Commerce Bank. I know there was
22 an entity, MOM, or something -- Mothers Overseas -- I forgot
23 what it stood for, but they were going to license this MA2.06
24 system and Bernie basically told us it never -- like there
25 were technical issues, and they never launched it, and they

1 didn't issue their system to another entity.

2 I don't know if that had to do with Commerce Bank.
3 But it was just an example of an e-mail where we saw that
4 they were going to license out their algorithm. And I
5 believe Peter Madoff or one of the two sons said something to
6 the effect, like -- the language in this said basically, "You
7 can't disclose to the media that you have our system." So we
8 just thought that was odd, and it also contradicted with
9 something.

10 So, I do not think I answered your question, sorry.

11 Q Do you recall whether you contacted Commerce Bank?

12 A Commerce Bank, no. We didn't contact Commerce
13 Bank.

14 MR. KOTZ: Okay, on to the next document. Okay,
15 the next document I'm going to mark as SEC Exhibit No. 34,
16 and this is an e-mail from you to Peter Lamore, 5/27/2005,
17 2:13 p.m.

18 (SEC Exhibit No. 34 was marked for
19 identification.)

20 BY MR. KOTZ:

21 Q And in this e-mail, Peter says to you first, "Hey,
22 he said he's not familiar with Auriga International, although
23 they could be an investor through one of the feeder funds."

24 And you respond, "That's weird, because Bloomberg
25 reports Auriga has a discretionary account with B. Madoff.

1 Maybe it was a few years ago, or it could be a feeder fund."

2 So you said it was weird. Why was it weird?

3 A Well, without looking at the attached list that's
4 referenced in the first e-mail, which would have been the 12
5 or 13 entities, and seeing that Auriga wasn't on there --
6 because I think there was another e-mail where I referenced
7 to Peter to see if Auriga is on there, because I looked on
8 Bloomberg and there was the information I found, and we could
9 Bernie that's where we found it because, you know, it is
10 not -- it's common knowledge, the Bloomberg system, I'm sure
11 he had one --

12 Q So what was this list that Auriga was not on?

13 A I believe the list is just a list that Peter or
14 Peter and myself put together showing who had signed a
15 trading authorization to use Bernie's model MA2.06. That's
16 it. So on there you would see Kingate, Sentry, Fairfield --

17 Q So you found it odd that Auriga was on the list,
18 but Bernie never heard of Auriga?

19 A It was odd. I mean, it's possible that Bloomberg
20 has outdated information, and maybe at one point Auriga was
21 with Bernie and now it was no longer. But --

22 MS. STEIBER: Can I show you a list as SEC Exhibit
23 No. 35?

24 THE WITNESS: Sure.

25 (SEC Exhibit No. 35 was marked for

1 identification.)

2 BY MS. STEIBER:

3 Q Is this the list of funds that Bernie produced to
4 you?

5 (The witness examined the document.)

6 MS. STEIBER: And we retrieved this from the work
7 papers.

8 THE WITNESS: I don't remember having names of
9 people. Because I know there was a reference where, like --
10 I know the trading directives weren't signed. So this could
11 be a different list or spreadsheet than -- I don't know if
12 that was the one attached to it. Is that the one attached to
13 this e-mail, do you know? Is SEC Exhibit No. 35 the one
14 referenced in SEC Exhibit No. 33 or SEC Exhibit No. 34?

15 MS. STEIBER: I don't think that we have the
16 attached spreadsheet.

17 THE WITNESS: All right. So I don't want to
18 speculate as to whether this is the attachment that I'm
19 saying that's weird, because it could have just been the one
20 that we put together where Bernie handed us saying, "Here are
21 all the people who use it, and here is my signature saying
22 that they're using it," and --

23 BY MS. STEIBER:

24 Q Do you recall that there were discrepancies between
25 the names that Bernie gave you and the names that you had

1 seen in various articles and on Bloomberg?

2 A Bloomberg, yes, in terms of Auriga.

3 Q What about --

4 A Yes.

5 Q What about -- did you notice any discrepancies
6 between the names that he had given OCIE in the headquarters,
7 and the names he had given the exam team?

8 A I don't recall what names we discussed with OCIE,
9 or what -- I don't recall what was in the documents from
10 OCIE.

11 Q You don't recall comparing the two lists, the
12 documents?

13 A I'm sure it was done, or I'm sure -- you know, the
14 biggest ones, in terms of Tremont, like we were trying to
15 focus on the biggest of -- the money ones. But, at the same
16 time, you know, I remember personally doing tons of research
17 on Kasigami and looking up these names and finding absolutely
18 nothing anywhere, in terms of Factiva or Lexis Nexis, or
19 anywhere. Couldn't find anything. Yes.

20 MR. KOTZ: Okay, we will go to the next document.
21 The document we're going to mark as SEC Exhibit No. 36. It's
22 an --

23 THE WITNESS: And, I mean, that last one clearly
24 showed we asked Bernie, "Where is Auriga on this," and he
25 gave us some excuse. And, you know, other than if we went to

1 Auriga then, and tried to contact them -- yes.

2 MR. KOTZ: The next document we're going to mark as
3 SEC Exhibit No. 36, this is an e-mail from Peter to you dated
4 5/27/2005 at 2:44 p.m.

5 (SEC Exhibit No. 36 was marked for
6 identification.)

7 BY MR. KOTZ:

8 Q If you see on the second page of this document, you
9 are sending an e-mail to Peter on Friday, May 27, 2005, 3:36
10 p.m. You say, "Wouldn't those account numbers you listed on
11 the spreadsheet correspond to the account at Barclays or the
12 Madoff account number? I can't believe this is the bank
13 account information for each of the 15 accounts. I can't
14 believe the Bank of America and HSBC both have account ranges
15 that start with 1FR."

16 Had you ever seen that before, where two different
17 banks had bank account information with account ranges that
18 start with the same numbers and letters?

19 A Have I ever seen it before? I can't recall if I've
20 seen something similar to that, or -- but if it was a prime
21 brokerage account, then those are Barclay-type account
22 numbers that then get allocated to Bank of America and HSBC.
23 If it's just like some sort of a pass-through, or who they
24 use for their clearing firm. It's possible, I guess.

25 Q Did you ever resolve the question of, you know,

1 what you're saying here, "I can't believe Bank of America and
2 HSBC both have account ranges that start with 1FR?"

3 A I'm sure we requested and got the -- printed out
4 statements for whatever entities it was, whether Bank of
5 America, HSBC, or whether it was Kingate Global or Tremont,
6 or wherever it was. We got all 15 entities for the whole
7 year, year-and-a-half, and they all started with that account
8 number. But, you know --

9 Q But you thought that that was --

10 A Strange.

11 Q Strange?

12 A Sure, it was strange.

13 Q And did you ever resolve why it wasn't strange?

14 A I don't know if we looked at stuff that OCIE had
15 also, and so it was the same numbers -- you know, here is
16 where I talk about locking up the stuff in the computer bag.
17 You know, so we had suspicions about pretty much everything
18 there, everything he said we wanted to try to figure out if
19 it existed or it didn't exist.

20 So, I can't recall -- I know we didn't send a
21 letter to Bank of America and say, "Would you have an account
22 1FR."

23 Q You can't recall how that issue was resolved?

24 A Well, we did what we would do on a normal exam if
25 they provided us a spreadsheet and we asked for the outside

1 statements, which were statements he printed up, and we
2 looked at it and compared it, and then if we had stuff
3 received by OCIE, we usually wouldn't go the next step the
4 same way an outside auditor doing the annual audit would
5 maybe send a request letter, even though -- we thought
6 everything was weird, so we would have been sending letters
7 out everywhere.

8 And at the same time, like we had been told, you
9 know, "You can't just go into Fairfield Greenwich and raise
10 red flags, and you know, have them lose business, because you
11 will be sued." But it didn't stop us from questioning
12 everything, and bring it up, and --

13 Q Right. Okay --

14 A Okay, I don't know if that other spreadsheet was
15 the one referenced here, because I recall trying to get names
16 of people as contacts at these places. So I guess that came
17 in at some point, but I don't know if that was from the
18 document related to OCIE, or if it was --

19 (SEC Exhibit No. 37 was marked for
20 identification.)

21 BY MR. KOTZ:

22 Q Okay, I will show you the next document, which is
23 SEC Exhibit No. 37. This is a string of e-mails, starting
24 with an e-mail from Peter to you, dated 6/1/2005 at 11:09
25 a.m.

1 Can you start on the last page of this string of
2 e-mails, SEC Exhibit No. 31? This says -- it's an e-mail
3 from Peter to you and John Nee, "Cliff Notes version of my
4 discussion with Bernie this morning. This is where Bernie is
5 saying his gut tells him when to enter and exit the market."

6 A Okay.

7 Q And here Peter says, "I asked him about monthly
8 performance stats of his model. He stated he doesn't track
9 it. I highly doubt this." Do you know why he highly doubted
10 that?

11 A Most people would probably want to brag if they
12 were earning 12 to 15 percent a year. And that's basically
13 what the Barron's and the MarHedge article said. And since
14 he wasn't giving us the data, we did take all the trading
15 data, we did try to calculate the returns. They did tie in
16 to 1.5 percent.

17 But, once again, we wanted to go to Fairfield
18 Greenwich, to see if the glossy material they're sending to
19 investors reflects the same 1.5 percent. It's a tie-in to
20 the exact same number that we were seeing. We wanted to
21 verify outside.

22 Q And what would have happened, do you think, if you
23 had done that?

24 A I can't speculate as to, you know, if the flag
25 would have been raised high enough, or if, you know -- I

1 don't know.

2 Q All right. If you look at --

3 A It's based on -- you know, current media news, it
4 seems like, Bernie was coaching Fairfield Greenwich anyway,
5 even before, when they came into the attorneys after this
6 exam ended. So the minute he would have gotten wind, you
7 know, odds are good, you know, we would have been led down
8 the same wrong path. Because it seems like a lot more people
9 were involved in this than just Bernie.

10 Q Okay. If you look at the third page of this e-mail
11 string, SEC Exhibit No. 37, you say to Peter Lamore and John
12 Nee, "Let me know if there are any transactions during the
13 time period we requested, and I will check to see if they are
14 on the database of orders entered."

15 Peter responds, "Hilarious nothing. Only
16 transactions on Feb 18 and March 15." Who was this in
17 reference to?

18 A Probably related to the request that we gave the
19 one where you asked about comparing the trading data for
20 customer -- during the day and the -- I don't know about --
21 FN1 maybe, or FN2. Like, once you saw the trades for one
22 account, it was the same replicated for all the accounts.
23 The only thing that really differed was whether it was \$3
24 billion, \$500 million, \$7 billion.

25 So, once we calculated the returns, we looked at

1 all the other accounts. But if we had requested FS1 or FS2
2 for that time period, that's what I would have had him
3 looking at, to compare.

4 And those transactions that happened on February
5 18th were some sort of, like, adjustment of shares. And it
6 probably was just because I think Textron, or whoever,
7 Texaco, had issued a dividend or something. So I guess it
8 messed up his model, or -- I don't know what Bernie did, but
9 it was just an odd -- another odd transaction. But he
10 explained it to basically be adjusting shares that -- things
11 that happened during that quarter, I guess whether it was
12 dividends paid or a stock split or something like that, he
13 would have to make some sort of adjustment to the customer
14 statements.

15 Q You mentioned earlier that Bernie at one point told
16 you who was going to be the next chairman of the SEC.

17 A Correct.

18 Q Who did he indicate?

19 A I believe it was Chris Cox at the time, when he
20 first came in. We learned at least two or three weeks before
21 the appointment of Chris Cox, before an e-mail in the SEC
22 saying, "We have a new chairman."

23 Q And did he indicate how he knew that?

24 A No. But by this point he had already pretty much
25 well established that he knew everyone in OCIE, and named

1 everyone, and already mentioned Lori Richards, had already
2 mentioned --

3 Q What did he say about him knowing Lori Richards?

4 A I just remember in the first day or two I think he
5 had started dropping those names. You know, so I think we
6 had either -- I don't know if he mentioned John or Bob or
7 just, you know -- or we just threw it in the back of our
8 heads, "He's saying everyone who is above us," and we didn't
9 know if it was true or not.

10 Then, as time went on, we found out about the OCIE
11 exam, and --

12 Q So what were the other names that he dropped, other
13 than Lori Richards? Eric Swanson?

14 A Specifically, I can't recall. I don't recall that.
15 I don't know if he mentioned his name, specifically.

16 Q Did he -- did Bernie Madoff ever tell you that he
17 was on the short list to be the next chairman?

18 A Yes, he did, I believe, yes.

19 Q What was the context of that?

20 A I'm not sure. I don't know if he was asked. I do
21 recall that now that you say that, yes.

22 Q And did you believe him, that that could be true?
23 I mean, he was pretty --

24 A In the beginning, when he was dropping all these
25 names, and then he said he was on the short list -- but then,

1 when he came in and told us who the next commissioner was, I
2 don't know if that's how he got wind of it, or -- I don't
3 know.

4 Q So, I mean, when you heard that he said he was on
5 the short list, you thought that could be true. He was
6 obviously very well known in the industry.

7 A Yes, I mean, we never verified and called anyone to
8 see --

9 Q Right.

10 A -- if he was on the list, which I guess, you know,
11 we could have done.

12 Q Okay.

13 A Unless he had the list.

14 Q What were the other things that he did like that to
15 kind of impress you? Anything else he said, that you can
16 recall?

17 A I don't -- first I will this other story. There
18 were tons of stories, hours and hours worth. A lot of
19 history, as well.

20 I will just summarize it, but one story he told us
21 is when his firm was moving, I think, to the lipstick
22 building. And he just -- he couldn't -- like his phobia of
23 moving, or something, and he basically just -- while all the
24 movers were coming and boxing up his stuff, he just curled up
25 on the couch and, like, huddled and just sat there for three

1 or four -- whatever, however long it was that it took them to
2 move the whole firm. He just couldn't handle it.

3 But, you know, the neatness and stuff, you could
4 definitely see in the offices, and that stuff that's in those
5 articles, it's true.

6 Q What about stuff about, you know, his connections,
7 or you know, he's so well known, that kind of thing? Did he
8 talk about --

9 A Not really. He didn't -- other than dropping names
10 of people at the SEC or wherever else it was, but he didn't
11 really mention anything else. You know, we learned about the
12 parties at his house and stuff through e-mails, you know,
13 like an annual employee party, and what not. And I think I
14 saw that Personal Privacy, the guy at NASDAQ who is now the
15 head of -- something.

16 But he -- I don't know if it was a pizza party, or
17 "Let's get Personal Privacy on the phone," or something. So it just
18 seemed like things were close, so that's why I didn't even
19 feel comfortable calling NASDAQ to ask about the closing
20 cross and the opening cross, you know, because it was too
21 clubby of a system, it seemed.

22 Q So you had the impression that Bernie had
23 connections with NASDAQ. So, to go to them --

24 A With the former chairman.

25 Q Right. Would not be useful?

1 A Yes, and I think we were maybe delayed in going to
2 them until we had all the e-mails we could find related to
3 it. Like myself and Pete -- but I know myself I did tons of
4 research on the closing cross, the opening cross, how it
5 works, how the feeds come in.

6 You know, I'm sure I spoke to Ellen Hersch about
7 it, and she might have sat in on that one call, or had some
8 notes about it. But, you know, we exhausted everything we
9 could do before we went to them to present our ideas to make
10 sure.

11 Q So, was there kind of this underlying concern that
12 if you accused or were seen to accuse Bernie of something, he
13 was so well known that there would be something coming back
14 at you?

15 A Not directly or indirectly. I mean, nothing major.
16 But just you can only push so much, or you know, since we
17 weren't really making much headway with all this other stuff,
18 let's push down this opening/closing cross-trade transaction,
19 yes.

20 Q So was there a concern about pushing too hard
21 without substantial evidence about Bernie, because he was so
22 well known?

23 A I guess hearing from OCIE that, you know, he is a
24 very well-connected and well -- powerful person, hearing
25 that, and hearing --

1 MR. TALARICO: Are you asking whether that's his
2 concern or the SEC's concern, or whether he knew that was the
3 SEC's concern?

4 MR. KOTZ: In general. In general.

5 MR. TALARICO: In general, meaning the SEC?

6 MR. KOTZ: Yes, I mean --

7 THE WITNESS: I wouldn't say the SEC, but --

8 MR. KOTZ: Well --

9 THE WITNESS: I mean, that -- I guess from OCIE, if
10 that's coming from them, that's their feeling. But you know,
11 it didn't -- it wouldn't stop me, necessarily, and I tried to
12 say, "Can I sit in on testimony," you know, "Can I do this?
13 Can I do that?" "No, don't worry. It's taken care of."

14 BY MR. KOTZ:

15 Q Who said that to you, "No, don't worry, it's taken
16 care of?"

17 A I know there were times where Peter would write,
18 saying, "All right, they're sending it out, Bernie is coming
19 in for testimony. It's going to be this day, so we'll see
20 you there," or something, and I'm like, "Okay, great, I will
21 tell my supervisor, I will tell this one," and then he would
22 clear it with the attorneys, and they would say, "No, just
23 one of you," you know?

24 Which -- I don't know if they took him because he
25 knew trading and he could understand what was going on, but I

1 think I had a pretty good grasp on it as well, and would have
2 been there, just as well, jumping up and down every time
3 Bernie told a lie.

4 Q So you wanted to be more involved in the
5 enforcement investigation, but the attorneys didn't want you
6 to be?

7 A I don't know if -- I don't know who -- I mean the
8 attorneys are the ones who said, "No, it's okay, one is
9 fine."

10 But, at the same time, from our own office, we
11 sometimes get push-back like not to help attorneys, and not
12 to spend time working on their stuff. I've gotten lots of
13 requests for, you know, "Can you look this up on Bloomberg
14 for us related to an enforcement case that you brought to
15 us?" And you know, you get in trouble sometimes. I wouldn't
16 say trouble, but you get told, you know, "Clear it first,"
17 or, "Don't help them."

18 And that comes back to the silo effect of, you
19 know, we've got to be out there getting numbers and doing
20 exams and --

21 MR. KOTZ: Okay.

22 BY MS. STEIBER:

23 Q Did Bernie ever say he knew any legislators or the
24 governor or, you know, a senator or --

25 A I can't recall. You know, he -- I forgot. He had

1 told us, like, someone had just been up there a few weeks
2 earlier in his office. I don't know -- I don't want to say
3 Chuck Schumer. I don't know who it was. There was someone
4 politically connected.

5 He was like, "Oh, if you would have been here a
6 week ago, So-and-So was here." So there were a few other
7 names dropped. But, once again, it didn't really phase us.
8 You know, "I met Chuck Schumer."

9 Q But did he give you the feeling that, "Hey, if I --
10 if you were to request documents for me, or push me too hard,
11 I have people that I can go to?"

12 A I don't know if that was directly stated or
13 indirectly. Maybe just by him dropping those names, he was
14 trying to give us the impression that, you know -- just even
15 by telling us who the commissioner was.

16 It's the impression we got that he was trying to
17 send to us, but we didn't let that stop us, because we're
18 impartial, and we try to do the best we can.

19 BY MR. KOTZ:

20 Q Was he very charismatic?

21 A Except for when he was angry with us.

22 BY MS. STEIBER:

23 Q You said he was charming?

24 A I guess, yes. It was -- you know, his stories and,
25 you know, a lot of history and a lot of, you know, "Back in

1 1970, when this started," or, "Before trading on the
2 exchanges," and you know.

3 But at the same time, in the back of our heads
4 we're thinking payment for order flow issues, and all these
5 other issues that, you know, had come up in the past. So we
6 tried to balance it.

7 BY MR. KOTZ:

8 Q So, when he was angry at you, what would he say?
9 What were those conversations like?

10 A Most of them happened, I think, when Pete was in
11 his three or four-hour conversations with him, and just what
12 I see in the e-mails back. He just got agitated, I guess,
13 when we would hand him a request, and he would see what's on
14 there.

15 You know, because maybe -- I don't know if he is
16 diagnosed with obsessive compulsive disorder, or what
17 diagnosis Bernie has, but he would have to get us most of the
18 responses, like, right away. Or, if there was something
19 outstanding -- but yet, when it came to the OCIE reports,
20 certain documents he didn't want to get us. But if there was
21 something that he could get us immediately, he made sure we
22 got it immediately.

23 Q So what would he be angry about, that you handed
24 him a document, or Peter handed him a document, and asked him
25 to do something?

1 A Yes, if it was a two-page request, or something.
2 Like, "Why e-mails? Why this? Why that?" You know, so --

3 Q All right. Why don't we continue?

4 (SEC Exhibit No. 38 was marked for
5 identification.)

6 BY MR. KOTZ:

7 Q Okay. Next document is marked as SEC Exhibit No.
8 38. This is an e-mail from John to Bob Sollazzo June 2,
9 2005, 10:04 a.m. and it forwards an e-mail from Peter to John
10 with a cc to you dated June 2, 2005, 10:03 p.m. -- a.m.,
11 sorry.

12 And in this e-mail, Pete says, "After reviewing the
13 Kingate account statements for January through April 2005,
14 paper version, I don't believe the retail customer order flow
15 information for Madoff's market making business has anything
16 to do with his hedge fund model."

17 "Essentially, he got long the S&P 100 for the hedge
18 funds January 20 through January 24, 2005, and sold the S&P
19 100, flattened out March 10 through March 13, 2005. There
20 was no activity in April of 2005. Granted, his purchase and
21 subsequent sale timing was excellent -- buy low and sell
22 high -- but held the basket for approximately six weeks.
23 Therefore, I don't believe that he is using any short-term
24 signals that would come from his retail order flow."

25 "I suspect he is extremely well connected to

1 But, once again, we didn't really see anything, and
2 we just showed that it wasn't his customer's orders from
3 Fidelity that were feeding him this information to put on the
4 basket, because there was no basket.

5 Q But you did kind of take note of his excellent
6 timing, always buying low and always selling high?

7 A Peter did there, and, yes, I probably agreed and
8 looked at the charts and whatever Peter printed out and
9 whatever I researched.

10 Q And then, on the second page is the -- what we
11 talked about previously, where Bob spoke to Personal Privacy
12 yesterday, and he agreed that documents associated with the
13 black box pile should be with the books and records
14 requirement, since the model is used in the conducting of the
15 firm's business.

16 A And this is in June already, so we're probably two
17 or three days shy of coming back from the field. And in
18 terms of when you said did we follow up on those Barclay
19 questions and the other questions, we were still trying to
20 just still get to the black box, three months later, and only
21 one week after finally officially being told that he was
22 running money for six or seven customers.

23 So, you can see how our hands were tied from the
24 whole -- beginning, and we're trying to gather the
25 information --

1 Q But at the same time you had the understanding that
2 you were going to be wrapping things up soon -- by that
3 point.

4 A Correct. We have to sort of tie our ends together
5 and come up with the -- you know, we had the violations of
6 the market making side, which we were able to work on in the
7 two or three-week -- or the two-month downtime that we were
8 waiting for Bernie to confess that he had these accounts
9 under his control.

10 MS. STEIBER: I know you had asked before to see
11 the assignment memo.

12 MR. KOTZ: Okay, so we're going to mark this as --

13 THE WITNESS: I mean was there any mention back in
14 April of 2004, when the Investment Adviser #1 e-mails came
15 out, and they talked about, "We need to have someone who is
16 well versed in options," like whoever that mystery person is,
17 let's pair them with -- like was there any --

18 MS. STEIBER: No --

19 THE WITNESS: Like when was the first mention of me
20 being assigned to this --

21 MR. KOTZ: No, all we saw was kind of waiting for
22 the person with the particular skills of Peter, and then
23 deciding on him. But we didn't see anything specifically
24 about, you know, you, per se.

25 THE WITNESS: And so was -- he decided well before

1 December 22, 2004, or --

2 MR. KOTZ: Well, from what we understand, the
3 complaint that precipitated it came in much before. And then
4 the decision was made to hold off to make sure, as resources
5 permit, that you would find somebody. And then I guess
6 Lamore was freed up, and then they decided to pair him with
7 you and start.

8 THE WITNESS: Got you.

9 MR. KOTZ: That's what our understanding is.

10 MS. STEIBER: And then, I agree, it didn't start
11 until March of 2005, when the exam work started.

12 THE WITNESS: Yes, I don't know if I was wrapping
13 up an exam in December and January and -- yes.

14 MR. KOTZ: Okay.

15 THE WITNESS: But that explains why, like, I didn't
16 really -- I guess I had access to their Investment Adviser #1
17 [REDACTED] stuff. But in terms of a year worth of that
18 folder, or files sitting on my desk, I didn't. I probably
19 just read it over, or read the summaries that Pete put
20 together, and stuff.

21 MR. KOTZ: Okay, go to the next document. Okay, I
22 will mark the next document as SEC Exhibit No. 39.

23 (SEC Exhibit No. 39 was marked for
24 identification.)

25 BY MR. KOTZ:

1 Q This is an e-mail from Peter to John Nee, 6/6/2005,
2 7:47 a.m. And it references a couple of e-mails that you
3 were involved in. See, on the first page of this, there is
4 an e-mail from you to Peter Lamore and John Nee Sunday, 7:31
5 p.m. You're working on the weekend?

6 A Yes.

7 Q "Attached is a spreadsheet showing total trades
8 done for each account in December 2004." And then, later on
9 it says, "For one customer a negative number appears in the
10 profit column. I believe this is a mistake, with the
11 conversion of data they gave us. On Thursday, as I was
12 walking out, they gave us a disk of text files that contained
13 the 15 months of customer statements. The data does not
14 appear as a customer statement, and I am going to ask the
15 firm to provide it in a usable format."

16 Do you know why you thought that the data did not
17 appear as a customer statement?

18 A It just didn't look like the one that you've seen
19 in the press now, where it's the heading of Bernard Madoff,
20 and it shows the positions. This was just raw data,
21 basically, that would be used to put on to a statement.

22 And I was probably doing this on a Sunday, because
23 we had just gotten this information a few days before, and we
24 had to wrap up the exam. And, you know, if we're going to
25 find anything, we have crunch time, in terms of a week before

1 the report is to be due. So I spend a lot of weekends
2 towards the end of exams, working with stuff, because firms
3 know how to hold off giving information. And there really
4 should be something that, you know, we should be able to do
5 when firms lie to us, you know more than just what happens
6 now.

7 Q Okay. And then, above that, on this document, SEC
8 Exhibit No. 39, Peter is saying to John, "Hey, John," and
9 then he says, "We still have not received the hedge fund
10 contact list, nor did the statements contain the addresses of
11 the 15 entities. We're going to ask them today for this
12 information."

13 A That's why the other document you showed me about
14 the addresses and the names and stuff, I don't know when that
15 came in, because what we were basically working on is, like,
16 a list of just those customers without the purchase amounts,
17 but it might have had the trading authorization date, and the
18 column for the date it was signed and stuff.

19 Q Did you ever get that hedge fund contact list?

20 A It looks like that was it. I don't know when that
21 came in, or how, or -- and possibly not. It's possible that
22 once we received it from OCIE, we had a list. But I think we
23 would have gotten it from him, as well. Something like that,
24 you know --

25 Q And, in the end, you didn't contact the individuals

1 on the list to confirm their relationship with Madoff and
2 trading --

3 A I don't believe we did, no.

4 Q And --

5 A I don't know if there were phone numbers that
6 were -- it was just addresses, mailing addresses to PO boxes
7 in the Bahamas or Liechtenstein.

8 MR. KOTZ: All right. The next document we're
9 going to mark as SEC Exhibit No. 40. This is an e-mail from
10 John Nee to you, dated June 7, 2005, 1:47 p.m.

11 (SEC Exhibit No. 40 was marked for
12 identification.)

13 BY MR. KOTZ:

14 Q And this is -- I think we may have referred to it
15 prior -- the e-mail, below that is from you to John Nee, cc
16 Peter Lamore, and then you cc'd yourself. Tuesday, June 7,
17 2005, 12:26 p.m. you say, "John, we have been reviewing all
18 the basket trades conducted by the 15 or so, using Bernie's
19 proprietary model. For all of 2004, Madoff executed close to
20 2 billion shares of stock, which represents a commission
21 equivalent of approximately \$82 million, \$.04 a share. It
22 appears, without this commission equivalent business derived
23 from the hedge funds, we estimate the firm would lose \$10
24 million to \$20 million per year. We intend to obtain an
25 expense break-down for October 2004 to December 2004, to get

1 a better understanding of the commission equivalent
2 business."

3 So, was it your understanding that the
4 broker-dealer side was losing money without the investment
5 advisor side?

6 A Yes.

7 Q Was that surprising to you?

8 A Yes, in the sense that you think here was this
9 large market making firm, and he hasn't admitted to having
10 any sort of accounts, but yet it makes up 80 or 90 percent,
11 or it is -- you know, if anything, the investment advisor is
12 smoothing out the earnings of the broker-dealer.

13 Q Right.

14 A So --

15 Q And then you say, "We are researching whether or
16 not Bernie should be registered as an investment manager,
17 advisor, due to his entire discretion in trading these
18 accounts. The other issue we have is with the London
19 affiliated office of Madoff, since the London affiliate is
20 the selling agent for the U.S. office through Barclays. We
21 will be researching whether the London office should be
22 deemed a branch, versus an affiliate."

23 And this is when John Nee responds, "Thanks for the
24 update. Be sure to keep your eyes on the prize. The branch
25 versus affiliate issue is a secondary/tertiary issue, at

1 best. I also don't think we get that far with the IA issue,
2 as broker-dealers can, as you know, act in an advisory
3 capacity."

4 So, in essence, John Nee was telling you here not
5 to continue to look at these issues, but to focus on the
6 front running aspect, is that right?

7 A If that's what the prize was. I don't know what
8 the prize was. But yes, to basically just stay focused on
9 verifying that the -- the front running issue, that it wasn't
10 happening, and that they weren't using --

11 Q So were you disappointed with this e-mail from John
12 Nee?

13 A Yes, I was.

14 MR. KOTZ: All right. Let's go to the next one,
15 SEC Exhibit No. 41. This is an e-mail from you to John Nee,
16 dated June 8, 2005, 8:43 a.m.

17 (SEC Exhibit No. 41 was marked for
18 identification.)

19 THE WITNESS: I laughed before when you read that.
20 I cc'd myself because I usually do that on exams. Because
21 then, when I come back into the firm, I can sort my e-mails
22 by myself, and I know the important stuff I sent to myself
23 and to everyone else, because it gets lost in our sent box.

24 BY MR. KOTZ:

25 Q If you look at the second page of this, there is an

1 be?

2 A Sometimes not aggressive, sometimes hard to find,
3 sometimes -- yes. Takes a while to get an answer or a
4 response.

5 And sometimes they -- you know, sometimes you get
6 led down the wrong road by them. You know, you could be
7 looking at one issue, and then all of a sudden you get a
8 blast of seven e-mails saying, "Hey, there is a new memo out,
9 you know, do this review as well." So all of a sudden you're
10 given two or three new reviews to do while you're trying to
11 stay focused on the -- you know, the eye on the prize, or
12 something.

13 Q Right.

14 A And you're distracted from it.

15 Q And do you feel sometimes where there is an
16 influential person like Madoff, supervisors may be reluctant
17 to push something too much because they're concerned about
18 some kind of reaction?

19 A Yes. I've seen it where, you know, maybe I've been
20 told, "Don't rock the boat so much there, because we have a
21 good relationship with them," and when we -- and not
22 Madoff-related, but you know, "where we need to make a
23 request for documents, they always gave it to us. So let's
24 try to go easy."

25 You know, and I don't go easy, and I push hard, and

1 I get pushback from staff members. But, you know, at the end
2 of the day it turns out, yes, it is an issue, or it should be
3 an issue.

4 (SEC Exhibit No. 42 was marked for
5 identification.)

6 BY MR. KOTZ:

7 Q All right. The next document, SEC Exhibit No. 42.
8 This is an e-mail from John to you and Peter Lamore,
9 6/16/2005.

10 This is the e-mail where, if you see below it, in
11 the e-mail from you to John Nee cc'ing Peter Lamore on
12 Wednesday, June 15, 2005, you say, "We would like to
13 visit" -- "We would still like to visit some of the hedge
14 funds. Example, Tremont in New York, and Fairfield in
15 Connecticut or New York."

16 And John replied that he didn't want you to do
17 that, is that right?

18 A He replied, "Let's meet" --

19 Q And what happened?

20 A -- "and go over it." But in the meeting -- we
21 didn't go to Fairfield or Tremont.

22 Q Did you bring up the issue of wanting to go to
23 Fairfield or Tremont in the meeting?

24 A Since we had sent it the night before, and we met
25 him the following morning, and -- I would say yes.

1 Q Okay. And --

2 A I'm sure we brought it up. Or he -- I don't know,
3 I mean, everything that went on in there, but we weren't
4 allowed to go.

5 Q Okay.

6 A I don't know if that's when I heard that the -- you
7 know, "If you're wrong," or you know, "You can't just go and
8 wave your arms at Tremont, if they have 8 billion with him."
9 I don't know if that was the meeting as to why we couldn't --

10 Q And that was said by John Nee.

11 A (Nodding.)

12 Q Yes?

13 A Yes.

14 Q Okay. Let's go to the next one --

15 A I mean, the second-to-last sentence about we had --
16 "We hope to have a draft list requested for the hedge funds."
17 I don't believe we -- that meeting the next morning sort of
18 put a kibosh to -- because I don't think there was any sort
19 of draft e-mail, other than we would have taken what was
20 written in there, in terms of the understanding of the
21 strategy used by the hedge funds, the marketing material, the
22 performance data. We would have broken that down into an
23 official request list.

24 MR. KOTZ: Okay, I will show you the next document.

25 We're going to mark the next document as --

1 MR. TALARICO: I bet you it's an e-mail.

2 MR. KOTZ: I bet you're right.

3 MR. TALARICO: From John Nee to -- some time in
4 June.

5 (Laughter.)

6 MR. KOTZ: Okay, well, close. The next document
7 we're going to mark as SEC Exhibit No. 43, it is an e-mail.
8 It is an e-mail from Peter Lamore to you, dated July 5, 2005,
9 11:03 a.m. And it attaches a one-page document.

10 (SEC Exhibit No. 43 was marked for
11 identification.)

12 BY MR. KOTZ:

13 Q What is this document?

14 A It looks like what would be a work summary control
15 sheet related to the audit of the broker-dealer, which we
16 then classified as section 1-9.

17 Q And it says in here, the annual audit was prepared
18 by the firm's independent auditors, Frieling and Horowitz.
19 Did you ever look into Frieling and Horowitz?

20 A No. And we saw payments going to them to pay for
21 the annual audits, and we saw the annual audits, so we saw
22 the name and stuff. But I can't recall if I googled their
23 name.

24 Q Okay. And did you recognize their name at the
25 time?

1 A No. I don't know if -- I don't believe the name
2 Frieling is mentioned in the other e-mail you showed me
3 related to -- I don't think the Investment Adviser #1 one or the one
4 where it was about the -- or the family dynasty?

5 Q Right.

6 A I don't know if that name was mentioned in there
7 now, thinking back.

8 MR. KOTZ: Okay. Okay, the next document. We will
9 mark the next exhibit as SEC Exhibit No. 44. This is also an
10 e-mail.

11 (SEC Exhibit No. 44 was marked for
12 identification.)

13 BY MR. KOTZ:

14 Q This is an e-mail from Peter Lamore to you, dated
15 7/5/2005, 8:34 a.m. And you say -- Peter says, "Attached is
16 a write-up of the two articles written about Madoff's hedge
17 fund business. When you have time, let me know what you
18 think."

19 So, this is also kind of a work paper. Is that
20 right?

21 A Work summary control sheet that -- the majority of
22 it would most likely be cut and pasted into the report,
23 itself. Or, it was written in the report and then it was cut
24 and pasted to make a work summary control sheet.

25 Q And this is -- was taken directly from the two

1 articles? It's just a summary of the articles?

2 A I haven't held them side by side. I think it's
3 mostly the -- some quotes from the articles, but then I
4 believe it's peppered with facts from the exam, or where
5 there were discrepancies, like where -- let's see, I'm sure
6 they are in there. This just might be the -- well, let's
7 see.

8 (The witness examined the document.)

9 THE WITNESS: It might just be mostly the article.

10 MR. KOTZ: Okay.

11 THE WITNESS: Do you have any questions about this
12 one?

13 MR. KOTZ: Why don't we go to SEC Exhibit No. 45?

14 (SEC Exhibit No. 45 was marked for
15 identification.)

16 BY MR. KOTZ:

17 Q That's an e-mail from Peter to you, Monday, July
18 25, 2005, 8:51 a.m. And this is an attached document, as
19 well. If you could, just tell me what this is. Supervisory
20 compliance procedures?

21 A Written supervisory procedures, yes. Basically
22 just has some background information about the firm, and who
23 would take over in case Bernie Madoff was absent, as the
24 alternate.

25 Q In looking at the issue of supervisory compliance

1 procedures, did you look at the issue of potential conflict
2 of interest? For example, that family members were in key
3 executive positions at the firm?

4 A I'm pretty sure we were looking for, like,
5 procedures, and we wanted to make sure that the people on the
6 trading desk weren't e-mailing stuff to other people in the
7 firm. So -- and we asked for outside brokerage accounts for
8 some of the employees, to make sure they weren't trading on
9 data -- so, in terms of -- so, family relations and stuff --
10 we knew from the beginning, by reading that Madoff dynasty,
11 that it's a family business.

12 Q Right.

13 A And there is nothing wrong with family businesses,
14 per se, but --

15 Q Okay. What about the lack of an independent
16 custodian? Was that an issue you looked at?

17 A Does it say that here?

18 Q I don't see it here.

19 A Well, we were told that he had no control over the
20 money, Bernie. He --

21 BY MS. STEIBER:

22 Q Who told you that?

23 A Bernie, himself. He would basically -- Tremont
24 would say, "Okay, you have 7 billion," but the money would
25 flow through to Barclays, and the trades were bought, and

1 like -- so he -- so we believed, or I believed, that the
2 money and the securities were being held at Barclays, or
3 cleared through Barclays in London, and then sent to the
4 respective entities listed, like, under Kingate, where it
5 said HSBC is custodian or Barclays -- whatever entity was
6 listed as the custodian, that's where we thought the ultimate
7 money and securities were being sent back and forth to.

8 Q But you never had any independent verification of
9 that, correct?

10 A Other than the letter to Barclays. And had we
11 contacted and went to Tremont or Kingate, or one of those
12 places, possibly, you know. But -- yes.

13 BY MR. KOTZ:

14 Q What about the lack of segregation of duties for
15 the investment advisory firm? Did you look into that?

16 A Considering they had no investment advisory
17 business until two months into the exam, and you know, we --
18 I don't know if we requested the procedures for the
19 investment advisory, but it wasn't a registered investment
20 advisor.

21 And that was the whole point I was trying to make,
22 is that why shouldn't they be, you know? They're running \$7
23 billion, \$8 billion, and they have -- we said 15, they said
24 14, first they said 4, so -- you know, it came down to
25 semantics again, but --

1 MR. KOTZ: Go on to the next document. Okay.
2 next document I'm going to mark as SEC Exhibit No. 46.

3 (SEC Exhibit No. 46 was marked for
4 identification.)

5 MR. KOTZ: This is an e-mail from Peter to you,
6 Thursday, July 28, 2005, 8:11 a.m.

7 MR. TALARICO: Can I get a copy? Thanks.

8 (The witness examined the document.)

9 BY MR. KOTZ:

10 Q This is a summary of the investment advisory
11 business?

12 A Correct. And it looks like there would have been
13 an attachment also of account information and allocated
14 capital with that e-mail.

15 Q And you used these in putting together the report,
16 these summaries?

17 A Could be vice versa. Maybe the template of the
18 report is filled in with the topics we want to talk about.
19 Maybe we write it into the report, and then we cut and paste
20 it into our control sheet.

21 Q So, at this point in time, you were starting to
22 prepare the report.

23 A Write. It's being written up and --

24 Q And so, you made the determination in this exam
25 that there was no evidence of front running activity, is that

1 right?

2 A Correct.

3 Q Okay. Was there any thought to looking at the fact
4 that -- Madoff was making these very consistent returns with
5 low volatility, or these other red flags, and the
6 determination was he wasn't front running. Was there any
7 thought given to looking at what the other possible
8 explanations could be for how he was able to achieve these
9 returns?

10 A Yes, there were probably some other ideas, in terms
11 of inside information or inside trading.

12 Q And was there any discussion of continuing the
13 exam, or refocusing the exam, now that you've ruled out front
14 running, to look at any other potential issues?

15 A By then we had already been there two-and-a-half
16 months, and that's the time we're given, and that's it. You
17 know, do me and Pete pass each other in the hall the month
18 after, three months later, and still shaking our heads about
19 Madoff? Sure, of course.

20 Q And why isn't it that you -- if you have an exam,
21 and you're supposed to be there for a certain period of time,
22 but you don't have all the questions answered, wouldn't you
23 just continue, and -- you know, continue with that before
24 starting on something new?

25 I mean, why is it kind of just understood that your

1 BY MR. KOTZ:

2 Q "Finally," because now you thought that now you
3 would get to the bottom of some of these unanswered
4 questions?

5 A Right. See if he is -- see why he is lying, or see
6 if he's consistent with the lies he told us.

7 Q But do you know if John Nee ever expressed any
8 concern that perhaps it would make the exam team look bad, or
9 the exam look bad, if enforcement then found out that there
10 were --

11 A Stuff we missed or something?

12 Q Stuff you missed.

13 A I don't know what John was thinking, but my thought
14 would be, "Hey, here is everything we can do to help," and,
15 you know, we're there to help, provided our supervisors let
16 us help.

17 Q Did Peter Lamore ever express anything, any concern
18 about missing anything? If you see in the e-mail he sends to
19 John Nee, he says, "I don't believe we missed anything."

20 A Yes, because for what we went in there to do, to
21 look at front running, we really didn't miss anything. It's
22 all the stuff that slowly trickled in, finding out about
23 OCIE, finding out about this and that, that was, you know,
24 what we were trying to keep unearthing. But --

25 Q Did you, at that time, read Harry Markopolos's

1 complaint?

2 A I read it in the e-mail that was forwarded to me
3 November 7th or November 8th or something.

4 Q Of 2005?

5 BY MS. STEIBER:

6 Q If you look at the second page of this e-mail,
7 where it says -- the paragraph starting "In a nutshell," if
8 you go about halfway into the paragraph it says, "The
9 informant believes that Madoff may be running one giant Ponzi
10 scheme and there are signs that it may be close to crashing
11 down on him."

12 When you heard that they had opened up the
13 enforcement exam did you -- or enforcement investigation --
14 did you hear that they were investigating Madoff for a
15 possible Ponzi scheme?

16 A I didn't see any of this but when I opened up the
17 Markopolos attachment it said "Ponzi" in the first or second
18 line, so that's when I first probably saw it. I didn't see
19 this.

20 BY MR. KOTZ:

21 Q So when you say that in your exam you looked at
22 front running, did you understand that now enforcement was
23 looking at a different issue, the issue of a Ponzi scheme?

24 A I don't know when I came to realize that they were
25 looking at a Ponzi scheme other than seeing those

1 allegations, but I know Peter and I talked about a lot of the
2 points in that and said, well, Markopolos didn't know they
3 were trading in London from two in the morning until nine in
4 the morning.

5 Q Right, but before we get to that, based on Harry
6 Markopolos' complaint did you understand that he was
7 suggesting that there may have been -- Madoff may have
8 engaged in a Ponzi scheme? Right? Isn't that --

9 A Am I reading, yes, correct.

10 Q -- okay. And in your examination you focused upon
11 front running, not whether he was engaged in a Ponzi scheme,
12 is that right?

13 A Not on the flow of money, correct, not on that.

14 Q All right. So if you look at Sollazzo's response
15 in this email to Bachenheimer cc John Nee Thursday, November
16 3rd, 5:38, he says, "These are basically some of the same
17 issues we investigated and I recognize at least one of the
18 hedge funds. Some of the comments are not new. I remember
19 looking at similar allegations back in the 90's of Madoff.
20 John Nee supervised the exam, but I can get you a copy of the
21 report."

22 Wasn't it the case that they were actually
23 different issues? I mean, wasn't the complaint that Harry
24 Markopolos brought forward relating to different issues than
25 the issues you looked at in the exam?

1 A Meaning by Bob saying, "I remember looking into
2 similar allegations?" Similar allegations in this current
3 email?

4 Q Doesn't Bob give the impression in this email about
5 you guys have already kind of looked at this issue and
6 there's nothing new here, when, in fact, you had focused on
7 front running and this was an allegation of a Ponzi scheme?

8 A Okay.

9 Q Isn't that right?

10 A Yes, that's what it looks like.

11 Q So the fact that you guys looked at it and didn't
12 miss anything, would it necessarily mean that there wasn't
13 plenty for the enforcement division to look at in terms of
14 the Ponzi scheme allegation, right?

15 A Correct, there would still be plenty of stuff to
16 look at because we felt like we left with some unanswered
17 ideas or thoughts.

18 Q Okay, and so you, personally, were happy that
19 enforcement was looking at this matter further?

20 A Correct.

21 Q Do you know if Sollazzo or Nee were happy that
22 enforcement was looking at this matter further?

23 A I don't know. Based on "Oh, no!" I'd say not so
24 happy.

25 BY MS. STEIBER:

1 Q Would it make them look bad if enforcement finds
2 something that their program didn't find?

3 A Would it make enforcement look bad?

4 Q Would it make OCIE look bad or the enforcement, in
5 the examination program, look bad to Sollazzo and Nee if --

6 A There was a Ponzi and we missed it?

7 Q -- right.

8 A Sure, I guess it could make them look bad, but, you
9 know, when you're dealing with three months of lies and stuff
10 and, you know, back to the 90's, I was in grade school and,
11 you know, that was never brought to my attention of anything
12 happening in the 90's until I read recent reports.

13 Q Right.

14 BY MR. KOTZ:

15 Q Okay. You don't know what those similar
16 allegations back in the 90's, what Sollazzo was referring to?

17 A There, then, no. Now that --

18 Q Sure. What it is?

19 A -- the thing in '92 maybe with Bienes and Avellino
20 or Avenus and \$40 million or \$400 million that was returned
21 or something, just by reading in the news.

22 Q Okay, let me go to the next document. We're going
23 to mark this as Exhibit 50. This is an email from Peter to
24 you dated 11/7/2005.

25 (SEC Exhibit No. 50 was marked for

1 Ponzi scheme, so that could have been a section that Peter
2 focused in on this guy, why he's doing it, at least this guy,
3 but you'd have to ask him.

4 Q Okay, but I mean from your perspective if the
5 author wanted to make money by uncovering the fraud, wouldn't
6 he have the same interest as you or the enforcement division
7 in trying to find the fraud?

8 A Wouldn't he have the same interest?

9 Q Yes, well, why would that be --

10 A He'd probably have a greater interest, I guess, you
11 know, economically. But I was sitting up in Albany in a
12 conference room and probably didn't have access to a printer
13 and didn't print out the full 19 pages and tear it apart
14 because Peter was looking through it. I looked at it and
15 helped out and gave comments where I could.

16 Q Did you ever speak to Harry Markopolos?

17 A No.

18 Q Do you know if Peter ever did?

19 A I don't know.

20 (SEC Exhibit No. 52 was marked for
21 identification.)

22 BY MR. KOTZ:

23 Q Okay, let's go to the next document. This we're
24 going to mark as Exhibit 52. This is your response back --
25 I'm sorry, this is John Nee's response back to Peter dated

1 11/10/2005 11:42 a.m., and at the top is an email from Peter
2 to John Nee 11/10/2005 11:51 a.m.

3 And John Nee, in this email, says, "there is still
4 a little mystery as to what Madoff does, but a Ponzi scheme
5 or directly hitting on an immediate customer order flow
6 doesn't likely from what we've seen." I assume he left out
7 the word 'appear.'

8 Was that your view, too, at that point that a Ponzi
9 scheme didn't appear likely from what you've seen?

10 A This is my first time reading this, this part, his
11 response. This just went back and forth to Pete. No, I
12 don't think I would have chimed in and said definitely not a
13 Ponzi scheme, but based on the documents we had and looking
14 at the broker dealer and us not seeing people requesting
15 money and getting paid money, how are we to believe
16 differently that, you know, people are getting money and
17 being received.

18 Q Right, but wouldn't it be more accurate to say that
19 you didn't look into the issue of a Ponzi scheme rather than
20 to say based on what you've seen it didn't appear likely to
21 be a Ponzi scheme?

22 A Yes.

23 Q Okay. I mean, what I'm getting at here is, do you
24 think that perhaps John or Bob Sollazzo sort of downplayed
25 the allegations in Harry Markopolos' complaint to

1 enforcement?

2 A It appears that way, but even then when enforcement
3 took the next step and started bringing people in and Peter
4 heard Bernie or Frank or whoever blatantly lying again,
5 there's only so much jumping up and down he can do and even
6 with me confirming what he's saying it didn't help any. It
7 was a slap on the wrist as opposed to doing something else.

8 Q But, I mean, in your view, based on Harry
9 Markopolos' complaint, there were matters in there, even
10 based on the information that you gleaned during your exam,
11 that should have been followed up on by the enforcement
12 division, is that right?

13 A Sure, by then it was out of broker dealer's hands.
14 Broker dealer's not going to go back out there a month later,
15 especially with enforcement being notified and all they would
16 do is contact the broker dealer side to say, hand us what you
17 have so far. We'll take it from there.

18 Q Was there any discussion of doing additional exam
19 work by the OCIE folks at that point?

20 A OCIE, I don't know. I wasn't really involved.

21 Q But nobody brought that to your attention, the idea
22 that perhaps now that Harry Markopolos filed his complaint
23 you, or you and Peter, might go back in?

24 A No, not to me.

25 (SEC Exhibit No. 53 was marked for

1 had with the enforcement lawyers, did they seem kind of
2 energized about investigating this matter?

3 A I didn't really talk to any of them. I talked on
4 maybe one phone call. I just got feedback from Pete.

5 Q And did Pete, in that feedback, ever indicate to
6 you whether they were energized about this investigation?

7 A I don't know about the beginning of the
8 investigation, but I know when he was extremely upset about
9 the fact that they weren't taking serious the fact that
10 everything was a lie. Like there were so many contradictions
11 to what Bernie said in testimony or Frank said to what we
12 were told on our exam.

13 Q And so how, according to Pete, did enforcement
14 lawyers respond to those points that Peter was making?

15 A I don't know, but I did see in one of the emails
16 from Simona or from them, where they put a memo related to a
17 call to Anjid someone or other from Fairfield Greenwich where
18 it had a lot of points in there and where it brought up the
19 contradictory statements based on Pete's knowledge of our
20 exam and from what the guy from Fairfield was saying.

21 So it's just based on the information that
22 Fairfield say that, oh, yeah, the options are done by Bernie
23 or something. But we knew that Bernie told us January of '04
24 they stopped. So that seemed to be a pretty good memo in the
25 sense that it addressed some of the differences.

1 Q Did Pete give you any indication why the
2 enforcement lawyers were not taking him seriously or why he
3 had to jump up and down?

4 A Can we go off?

5 Q Sure.

6 (A brief recess was taken.)

7 (SEC Exhibit No. 54 was marked for
8 identification.)

9 BY MR. KOTZ:

10 Q All right, why don't we show you this document,
11 Exhibit 54.

12 A Okay.

13 Q This is an email from Simona to Peter and Meaghan
14 Cheung. Above it is an email from Peter to Simona 11/17/2005
15 10:18 a.m. Below, as I indicated, is an email from Simona to
16 Peter Lamore, Meaghan Cheung; Wednesday 11/16/2005.

17 Were you aware of this issue about, "Meaghan, prior
18 to sending out this request maybe it would make sense to call
19 Fairfield's legal or compliance department to warn about the
20 request and also to give a head's up as to it's scope?" Were
21 you aware that that was talked about?

22 A No, I'm not on this email.

23 Q Okay. Do you have any idea why enforcement would
24 call Fairfield's legal or compliance department to warn them
25 about a request before sending it in an investigation?

1 and Peter's perspective you thought you should do more than
2 seek information from some of the hedge funds on a voluntary
3 basis, and if they don't work out don't do anything else?

4 A What was that, what me and Peter had thought at the
5 end of our exam?

6 Q Well, no, at this stage you guys had completed your
7 exam. Harry Markopolos issued his complaint. Enforcement
8 was looking into it. Isn't it fair to say that it wasn't
9 your and Peter's opinion that all you needed to do was seek
10 information from some of the hedge funds voluntarily and if
11 they didn't work out not do anything else?

12 A Yeah, especially not on a voluntary basis. You
13 know, make them hand over the documents, but once again, I'm
14 not on any of these emails. I didn't see these emails
15 between Calamari and Doria.

16 Q Okay.

17 MS. STEIBER: Can we just go off the record for
18 just a moment.

19 MR. KOTZ: Why don't we go off the record.

20 (A brief recess was taken.)

21 BY MR. KOTZ:

22 Q How many times did they take testimony, to your
23 knowledge, in the enforcement matter? Who did they take
24 testimony of?

25 A I know they took testimony of Frank DiPascoli. I

1 know they took Bernie Madoff. I don't know if they took
2 someone else from his office as well, and then I believe they
3 brought in one or two people from Fairfield Greenwich, a guy
4 Jeffrey something or other.

5 Q And Peter Lamore went to both Bernie and Frank
6 DiPascali's testimony?

7 A I believe he sat in on both and I know he gave me a
8 copy of Frank on my chair and I think I got a copy of
9 Bernie's afterwards

10 Q So what was your reaction when you saw Bernie's
11 transcript of his testimony?

12 A I think I had already been prepped in terms of all
13 the discrepancies that were in there so reading it was just,
14 you know, more disbelief.

15 Q And these were discrepancies between what Bernie
16 said under oath and what Bernie had told you?

17 A Correct.

18 Q And what was your reaction when you saw Frank
19 DiPascali's testimony?

20 A I think -- I don't know if Bernie had said that
21 there were like four or five customers who had maybe \$100
22 million under management with him. That was shocking
23 because, you know, we didn't know any of those customers. It
24 didn't come up on any of the broker/dealer records. They
25 didn't come up in the investment advisory 16 institutions.

1 So that was somewhat shocking and I believe I just did some
2 google searches and Factiva searches and forwarded the
3 information to Peter who I could find on the guy Personal Privacy or
4 something.

5 And then I guess in Frank's I think it came out
6 that there were a handful more individuals who had money with
7 Bernie as well, which, you know, was not anything we knew
8 about either.

9 Q So do you remember specifically what were the items
10 in Bernie Madoff's transcript or testimony that conflicted
11 with what he told you?

12 A I don't recall exactly. I haven't looked at a
13 transcript in four years, three years, whenever it was.

14 Q Okay. Did Peter Lamore indicate to you that he
15 made the enforcement attorneys aware of these discrepancies
16 between what Bernie Madoff said under oath and what he told
17 you in the exam?

18 A Under oath? Did he bring it up during the
19 testimony do you mean?

20 Q No, afterward.

21 A Yeah, I believe he told me what some of the
22 discrepancies were.

23 Q Do you know if Peter told the enforcement attorneys
24 that he heard the testimony of Bernie Madoff and it
25 conflicted with what Bernie had told him and you in the exam?

1 A I don't know, but I believe he did because I think
2 he told me. I was jumping up and down at the attorneys and
3 letting them know about all of the discrepancies.

4 Q And did Peter suggest anything specific to do with
5 regard to these discrepancies?

6 A I don't know. I don't know if he made any
7 suggestions to enforcement. That's not really our role as
8 examiners. I guess we can help out and try to make
9 suggestions, but that's really in their field or realm.

10 Q Did Peter ever indicate to you that the enforcement
11 attorneys weren't taking him seriously or weren't listening
12 to him?

13 A I don't know about not taking him seriously, but
14 the same way no one really took Markopolos seriously. It's
15 sort of the same way Peter felt to a same degree and me to
16 maybe a lesser degree just in terms of wanting to go to
17 Fairfield or whatever.

18 Q But did Peter indicate to you that enforcement
19 attorneys weren't listening to him as much as he would have
20 liked?

21 A Maybe on one or two occasions.

22 Q Okay. So at the point in time where Bernie Madoff
23 told you a variety of things in the exam, you and Peter, and
24 then there's testimony and Bernie Madoff contradicts himself,
25 do you know whether Peter, at that point, believed that

1 part of it and, you know, someone should try to find that. I
2 thought that was a pretty key email. If you don't have it I
3 could forward it to you guys probably.

4 BY MS. STEIBER:

5 Q It's nice to hear how it's relevant.

6 A Let me think if there's anything else that I
7 thought you might have showed me. I mean, I think we had --
8 we were going to ask for like if they had a group Comad email
9 address set up but, you know, someone from Comad Security was
10 also listed as the fire warden for the floor and stuff and so
11 things sort of made sense, but at the same time it didn't
12 always make sense.

13 Q Have you learned anything now about Comad
14 Securities that would have been relevant to your examination?

15 A Sure. They whole fact that they were feeding money
16 into these feeder funds or feeding money to Bernie that we
17 had no idea about, that could have been important and
18 relevant.

19 But based on the story that Bernie told us about,
20 you know, his family, friends would give him the space and
21 they help us manage our bonds, you know, he had bonds sitting
22 in his account and they were sitting there and we saw checks
23 monthly and you know it wasn't -- and the fact that it was
24 called Comad and he was one of the directors, I thought maybe
25 it should have been disclosed or something on a U4 or U5 or

1 something.

2 Q And were there any other emails to your supervisors
3 that we haven't touched on today in which you raised an issue
4 to them that maybe they didn't act on?

5 A No, I'd say the biggest issues were the going to
6 see the funds themselves and also the London affiliates and
7 registering as an investment advisor. Those are big points.
8 It's like a double-edged sword in the office where if you say
9 to someone, hey, in terms of foreign affiliates what can be
10 done; oh, I'm not sure or not much.

11 If you then -- you don't want to go around your
12 supervisor and ask maybe the attorney in the office or ask
13 someone else in the office because then you're sort of going
14 against what they said or doubting what they say. So if
15 there was some way that you could do that and instead of
16 everyone just get praised for it instead of, you know,
17 getting shot down for it that would be a good thing.

18 BY MR. KOTZ:

19 Q But did that office of international affairs,
20 wouldn't that be an office within the SEC that might have be
21 able to help with issues involving overseas entities?

22 A Possibly.

23 Q Was there any thought to ask them for assistance?

24 A No, I think we might have looked into the FSA and
25 verified that the London affiliated was registered with the

1 FSA, or at least that's what it was told and that's what was
2 on the letterheads and stuff, but I mean even making a long
3 distance call or something is something that might be frowned
4 upon or you need all these documents and stuff to say you're
5 calling customers. You know, it's a lot of red tape to
6 sometimes get stuff done.

7 If any one of us could have just picked up the
8 phone and called Fairfield or something and caught them off
9 guard and asked a question, you know, fax me a statement from
10 Bernie Madoff now, that could have maybe stopped it. Not us
11 faxing over a request list to them, giving them time to work
12 on an answer.

13 That was the urgency of saying, have Bernie print
14 out a statement now and let's lock it up because we don't
15 want him picking out the statement he wants to show us. I've
16 gone to firms where they're like, I'll give you the print out
17 I just handed to FINRA. Here's this; which now we do have
18 because that's part of the FINRA oversight.

19 MR. KOTZ: Okay. I think that's all we have.
20 We're going to go off the record.

21 (Whereupon, at 3:55 p.m., the examination was
22 concluded.)

23 * * * * *

24

25