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P R O C E E D I N G S

MR. KOTZ: We just wanted to get a little information from you. To start off with, what was the first interaction you had with Bernard Madoff's firm? How did you hear about it?

[redacted] [redacted] or --?

MR. KOTZ: I guess start [redacted], or maybe if there is just something briefly.

Law Enforcement

[redacted] There is this room with probably 10 to 12, 14 people like me. There might have been fund to funds, there might have been distributors, I do not know. Bernie comes in at the end of the table and just talks for like an hour, sort

of mentioning the split strike strategy, but not really. More talking about market making and business and how stocks are traded and at what price. At that point I was already cynical about the whole thing but I did not ask intrusive questions.

MS. STEIBER: Why were you cynical?

[redacted] The returns were impossible. Absolutely impossible in my opinion. No financial strategy could produce those sort of returns. So then he finishes and then they gave everyone a tour of the trading floor, which is the electronic marketing trading floor so it is very quiet but interesting. They said, "Oh, yeah. The hedge funds run," -- blah, blah, blah "run up on that floor." They were not going to take us to a different floor. They were showing the door. [redacted]

[redacted]

[redacted]

Assuming I was telling the truth, the institutional fund to funds exposure to Madoff was .22 percent. So the reason I am saying this is by and large I was like most institutional fund to funds managers. I understand it. It seems too good to be true. I am just going to stay away, which was my attitude. [redacted]

MR. KOTZ: As part of [redacted] you inquired about them again or had some interaction with them?

[redacted] Yes.

MR. KOTZ: So what happened then?

[redacted] How long do you want this to take?

MR. KOTZ: As long as it needs to take.

[redacted] I was fascinated. I mean, for me, anything that -- it is new and different. [redacted]

[redacted] I kind of pretty quickly figured out it was a Madoff feeder and I said this is going to be the most interesting thing I do all year, so I kind of elbowed out the line workers and jumped in myself. That is why I am talking, as opposed to other people.

MR. KOTZ: Why did you think it was a Madoff feeder?

[redacted] They must have said. I do not know. I presume when we talked to Maxam they said it was.

MR. KOTZ: Can you say because you had had that interaction with him previously?

[redacted] I think if you talk to the CIOs of corporate fund to funds that were not connected -- had no Madoff exposure a year ago they would have said it does not smell right, it is all weird. They would have actually, if they were in my shoes, be just as interested in looking at it.

MR. KOTZ: Because of the returns?

[redacted] It is so different from any other hedge fund. It is not -- I guess what I am trying to get across here is we are not the only people on the planet that said that this does not seem right. I think if you -- it is tough

to do now, but I think a lot of institutional fund managers said this does not smell good.

[redacted] We were asked to look into them and then shortly there after we had a separate client that was interested. So the two due diligences were run almost concurrently to each other.

[redacted] It was like May, June, August, and September.

MS. STEIBER: What was the second fund?

[redacted] Fairfield Century. And also this is tough because you guys are lawyers and follow a process. [redacted] I hate to say it, but we do not have to be objective for our business. Right off the bat we did not like these --

She is very methodical. She starts banging through it.

MR. KOTZ: What kind of questions?

[redacted] Basically what we get is an [redacted] of the company -- and we can give you these questions. We have a whole list of things. [redacted] We probably do not spend that much time on [redacted] because for us it is actually very difficult. We do not have access to SEC forms where we could actually go in and inspect various things. We find out if they have procedures and what they are, but we cannot actually verify them so that is whey we do not spend that much time on it. [redacted]

[redacted] And third parties.

[redacted] I am not sure if I mentioned third parties like an administrator.

[redacted] Again, this is all voluntary. You say you want to meet with them, they say okay, they could have said no.

[redacted] They could have, but we would have told them basically our clients --

[redacted] They see us as the gatekeepers and people want to be nice.

MR. KOTZ: Those are the standard things.

[redacted] Personal Privacy is asking them exactly these questions and they mention -- they must have mentioned at some point that all the money is in the brokerage account of Madoff Securities and I think we asked the question what type of brokerage account and they said cash and not a margin account. Then we said, "What goes on in the account?" They described the same thing that you are reading in the papers now. So Bernie follows a split strike strategy and a lot of time he is in Treasury Bills. He has got this wonderful feel for when to enter the market, when to get out, and which subset of the S&P 100 stocks to trade.

We probably asked about who the -- we must have asked about who the counter parties -- how they traded the S&P 100 options. I am pretty sure they said they are not exchange traded, they trade OTC. I asked who had counter parties and then Personal Privacy went on this something talking about well -- for example -- I am not going to be good on the

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details. I am sure I am wrong here. It used to be Merrill then it was UBS now it is JP Morgan -- something on that. By that point Personal Privacy and I are kicking each under the table.

MR. KOTZ: How come?

[redacted] And then the Maxam people said, "We see all the trades and the trades produce the returns," or something like that. And then we said, "How do you get all this?" They said they had total transparency. We said, "How do you get the transparency?" They said, blah, blah, blah. We said, "Can we see it?" We expected to see a computer screen and something, something, something. Someone comes in with this binder about this thick that had just zillions of trade tickets in this binder.

They may have had -- I forget if there was Tremont, Fairfield, or both -- they may have had someone from --

[redacted] It was Fairfield.

[redacted] So I see this binder of paper trade tickets and now we are really kicking each other because I have never in my life seen ticker trade tickets in this industry.

MS. STEIBER: What would you usually see? Just a print out of the electronic?

[redacted] You could get that, but typically people show you a system. So they will have their Morgan Stanley

account and you pull it up and it will have every single position, history of trades. Like if you open up your own Schwab account or Vanguard account it is electronic.

MR. KOTZ: So what does that say that there was not an electronic? This is unusual?

[redacted] This is part of the --

[redacted] It was unbelievably unusual.

[redacted] We asked how they got the trade tickets and they said they mail them to them.

[redacted] U.S. Mail. Not even FedEx, U.S. Mail.

[redacted] Which is unusual. It happens that people get these confirmations but usually you can see it electronic as it happening kind of deal. We are in the 21st Century.

MS. STEIBER: How does this work, though, because you are not dealing directly, you are dealing with the fund to funds, right?

[redacted] Yes.

MS. STEIBER: So you are dealing with them so how would they have gotten to his electronic system anyways? What would you have expected to see?

[redacted] I would have expected to see they take us to a computer -- Madoff was a broker dealer. So is Goldman Sachs, Morgan Stanley, Bank of America. So they would show us a computer screen and say here is our account at Madoff

and you would see all the positions. You would click on a tab and you could see the last 100 trades. Hedge fund managers have online access to their brokerage accounts.

MR. KOTZ: What did you think?

[redacted] It was highly unusual. We went in kind of just saying -- not really liking these people quite frankly. Saying this is really, really strange. So we were just nice.

MR. KOTZ: But the idea would be that either they are not, like you said, in the 21st Century and using true.

MR. KOTZ: So what does that mean?

[redacted] Well, brokers borrow money. You look at the broker dealers and they borrow huge amounts of money. [redacted] Instead of borrowing money in the capital markets they choose to borrow it this way. [redacted]

[redacted] what I tried to do -- with help by [redacted] an[redacted] They [redacted] the thought process as well. [redacted]

MR. KOTZ: You did this for both Maxam and Fairfield?

[redacted] I did it for [redacted] we took one additional step we did not do in [redacted]

MR. KOTZ: Is that in the report?

[redacted] Yes. Another thing about [redacted] that we had a problem with was the market recipe 100 options is nowhere near deep enough to trade $13 billion dollars. I thought there was $13 billion in all the feeder funds. The liquidity of listed S&P 100 options could not handle 1/20th of that size.

[redacted] Basically we think there was something like he opened up contracts with somewhere around I would say 8,000. I cannot quote the exact number.

[redacted] Maybe 90.

[redacted] It was somewhere around 8,000 and he needed like 188,000 contracts to execute.

[redacted] They said they trade OTC so I called a couple of friends who trade OTC and said, "What is liquidity like in S&P 100 options?" They said no. In the OTC market, what these traders told me, is liquidity is just as lousy as it is in the exchange-traded markets.

[redacted] I worked on the review too and frankly the thing on the OTC thing was if it was possible to do it. I think it did not make any sense.

[redacted] Just put those two together. The third piece is if Confidential Commercial Information [redacted] why on earth do all the feeder funds? Why not -- what the feeder guys say is Madoff makes money only from commissions. So Confidential Commercial Information [redacted] why wouldn't he collect hedge fund fees just by running a hedge fund and become a multi-billionaire as opposed to earning -- I think if he -- on commissions he would probably earn $200 million a year and running a fund he would probably earn $1 billion a year. There is a large difference. That was the third argument against Confidential Commercial Information [redacted]

MR. KOTZ: Did those questions come up at all? Did you ask them about that?

[redacted] We might have. That third question we probably asked.

MR. KOTZ: Do you know what the answer was?

[redacted] No. It was probably something like that is the way he does it. [redacted] Confidential Commercial Information [redacted] What he said was there were only 8 to 15 prop traders at the firm and he thought the amount of capital the prop traders controlled was anywhere from $800 million to $1.2 billion of trading in the market.

So that is nowhere near the size of the feeder funds. Then he started going on and on about how he thought said, "I'll send you the balance sheet and financials." A couple days later we get in the mail the -- what is it called?

[redacted] Statement of financial condition. It is basically just a balance sheet.

[redacted] It is probably some SEC thing.

[redacted] It is an SEC requirement for broker dealers.

[redacted] It was like a two-page balance sheet that

they have to give to trade companies. So we have the SIA --

[redacted] SFC.

[redacted] So we got the SFC and at the bottom -- the balance sheet was like $1.5 billion or whatever.

MR. KOTZ: Was that in line with where it should be given their size in the industry?

[redacted] At the bottom it is signed by Friehling and Horowitz. So for the Maxam report it was basically I got that. I ran over to [redacted]

[redacted] He came over to me and it immediately struck me that I do not know who Friehling and Horowitz is and I have been in this industry a long time. I have never seen them before in my entire existence and it is very, very, very rare that I run across an accountant that I have never seen in my years. Occasionally I run across an administrator or something else I have not seen, but an accountant is very, very rare.

The first thing I did was [redacted]

[redacted] Now these are kind of industry titans who are usually called on these kinds of things. They are familiar and go back 30 or 40 years in the industry and they would have heard of somebody like this. Nobody had ever heard of Friehling and Horowitz.

So then I started Googling them and looking them up and could not find very much at all. I did find some information about them. I found a home address, where his work address was, but that was about it.

[redacted] So that is all we did for [redacted] We figured out that none of us have ever heard of these people.

[redacted] So then --

[redacted] That was [redacted] That was all we did.

MR. KOTZ: [redacted]

[redacted] It took a while.

MR. KOTZ: A few weeks? A month?

[redacted] Well continuous time it was probably a week or a week and a half. A week maybe of continuous time. In our [redacted] report we just said no one on this planet has ever heard of this auditor.

MR. KOTZ: And that was the main reason?

[redacted] months later we looked for [redacted]

MR. KOTZ: Did you finalize the [redacted] report or were you still waiting?

Madoff -- it is all family. Everything seemed to be family. Well, what other business organization is very family oriented? Organized crime. So I convinced myself this whole thing was connected to a guy named Meyer Lansky. You know Meyer Lansky? So I read a book on Meyer Lansky and I kind of said Meyer was the man back in the 60s and 70s and Bernie started out in the mid-60s doing this -- started a securities firm.

They are both from a certain social, economic part of New York, which is really smart, Jewish immigrants, second generation. I became convinced, and it was partly you guys -- we knew from a Wall Street Journal article about this kind of thing being shut down in 1992. What the Journal article said was the court went in and found all the money and everybody got their money back and that was the end of it. We knew from Fairfield Greenwich -- they told us that

the SEC went in there in 2005. Plus between [redacted] I got from a friend of mine a copy of the Markopolos letter to the SEC.

So I put together the 1992 letter, the Markopolos letter, the 2005 visit, and I said, the money is probably there.

MR. KOTZ: This is after when you were drafting up --

[redacted] I came to the conclusion that the money is probably there because there have been people going in and out. I incorrectly deduced -- all you have to do is phone

DTCC and say how much of a total value of listed securities in Madoff Securities -- one phone call.

MS. STEIBER: Will you go back to that? This one phone call to the DTCC.

[redacted] What I presumed from these data points was somebody at the SEC must have checked with DTCC.

[redacted] There is actually a weakness in that is Madoff was saying -- he said he had $17 billion of assets or whatever he had. I am thinking if he has gone to the DTCC and had been saying he has $17 billion in assets but really he has $50 billion --

[redacted] We did not know about $50 billion then.

[redacted] The DTCC actually had a weakness in

it. He says he has 17 and he goes to the DTCC and says he has 17. It does not really matter. He could have gotten away with that.

MS. STEIBER: Explain that to me. I am really interested in that point because I think that is important.

[redacted] Personal Privacy [redacted] point is if you go in and you say show me your assets and show me what you are running and he says he is running $1 million. Then you go back to the -- he is a claiming broker but the cash has to be held at a federal bank. Basically what happens is you can call up --

[redacted] You can, not us.

[redacted] You guys could call up and ask how much money he actually has.

[redacted] Madoff Securities as a total entity, how much --

MS. STEIBER: That is what I am trying to get at.

Looking as a total entity and not necessarily as an advisory.

[redacted] Remember the feeder fund things -- he was not a money manager, he was an executing broker with full discretion.

MS. STEIBER: That is what he said but then all the other fronts of the firm was executing -- that is going to show up in the call; is that what you are saying?

[redacted] Madoff is strictly a broker dealer. He does not run a separate hedge fun.

MS. STEIBER: In 2006 he did register --

[redacted] He registered as an advisor but according to feeder fund managers the thing was still documented as a brokerage agreement. So he was still running.

[redacted] I think if you looked at Madoff Securities they are not necessarily all over the place, there is just one broker dealer. If you called up with the money DTCC, we believe -- we have never done this. They would say, yes, there is $17 billion in there. Since he controlled all his own records he could do whatever he wanted.

MS. STEIBER: He could have written down on the form $17 billion even though he had $50 billion investments.

[redacted] He could have claimed to have $50 billion to his clients but --

MR. KOTZ: At the time you assumed since the SEC came in 2005 that they had checked that out?

[redacted] It was unclear. I figured -- the analogy with the mob. My whole theory was Meyer Lansky was probably the richest man on the planet and he died a poor man in

Florida. Well that empire existed somewhere. I figured it was balance sheet for that organization and every time the SEC would come in they would just make sure that there was not money there. Everyone would say that everything was fine. I never expected a Ponzi scheme.

MR. KOTZ: How did you get the Markopolos

complaint?

Confidential Commercial Information [redacted] He was as big of a cynic as I was. He said that I had to see this thing so he gave me the Markopolos letter in confidence. I would assume that he knew Markopolos personally. I did not have that letter when we did the Maxam report but I did mention that letter in the Fairfield report saying that someone did go to the SEC with a whistleblower claim and the SEC did nothing about it. At that time we knew about the letter, which made me all the more think somehow the money is there, so -- that is how I kept coming back to the mob.

MS. STEIBER: Obviously you are a sophisticated team. When you look at the Markopolos letter did you analyze it step by step? You are very interested in this.

[redacted] How many times did you see the Markopolos letter?

[redacted] I honestly read it once. We had it but I did not re-read it. I thought -- I was convinced that I was right. That they were basically making money but it was

something nefarious that was making money, which I was totally wrong. It is different. I think he -- I am not really sure. I have not read the letter in so long. What I do remember is we approached it differently. We approached it as an investor, which gave us keys to certain doors. Whereas what I think he did was talk to everyone on the market, get a zillion opinions, and they agreed with his opinion and kind of synthesized them down. He wrote about rumors and other stuff, so he did a great job getting all the knowledge that was out there into one document and thinking it through himself.

MR. KOTZ: Did you find it to be somewhat persuasive?

[redacted] I will tell you this. I thought, there is now way in hell the SEC did not take a hard look at this thing. To me, it was -- Fairfield Greenwich was the ones also -- I got it through talking with my friends, but Fairfield Greenwich -- I do not think they mentioned the Markopolos letter but they definitely mentioned the SEC was there in 2005.

MR. KOTZ: Oh, yeah?

[redacted] Oh, yeah. Big time. As a result of the SEC visit Madoff registered as an investment advisor and I think they mentioned they started disclosing Madoff in their documents. But they definitely mentioned it to us.

MR. KOTZ: So it was mentioned in the sense of they got somewhat of a clean bill of health?

[redacted] Like they mentioned PWC. You know, people had been in there.

MS. STEIBER: When you were talking about -- you said that you had talked -- were you talking about the article by Michael Ocrant or the Journal one?

MR. KOTZ: Barons?

Law Enforcement [redacted]

MS. STEIBER: I was just wondering, were there other articles that you knew of?

[redacted] The only articles I knew of were the Barons and the Wall Street Journal from 1992.

[redacted] It is one of the first steps we ever do is run background checks. We had them run something on Maxam and Fairfield Greenwich and Madoff.

[redacted] They are the ones that had the Wall Street Journal article.

[redacted] That is how we found out about the Wall Street Journal article.

MR. KOTZ: Was there anything else in there that stuck?

[redacted] I would have to check.

Personal Privacy [redacted] It was a lot of crap.

[redacted] It is something we do on every single manager. We always ask for background checks.

[redacted] It is cheap. How much is it?

[redacted] Like $2,000. In the grand course of things --

[redacted] As you know most of these guys tend to have really, really deep histories.

[redacted] By and large Madoff -- if you go back to the time of sanctions and everything else there was regular non-reporting sanctions and stuff like that. Nothing from that time where it was like, wow.

MR. KOTZ: But the fact that there was a 2005 exam by the SEC and the fact that the Markopolos complaint existed and was seemly looked at by the SEC, that affected your thinking.

[redacted] That the money was there and being used for some bad purpose.

MR. KOTZ: Because you saw the red flags previously it affected your thinking -- in the end it affected your thinking to not go forward under a different theory. I guess my question is, from another perspective coming in, the fact that the SEC was there in 2005 and found only minor things and the fact that there was the Markopolos complaint out there and it seemed liked the SEC must have looked at it,

wouldn't that provide some assurances to people?

[redacted] I agree.

[redacted] As you mentioned even the feeder funds were telling us that. Fairfield Greenwich was telling us about the SEC was just in there and they did not find anything.

MS. STEIBER: Talking just from your experience, and of course this is just your opinion, where would you have expected -- are there certain steps that the SEC, that you would have expected, would have turned up any these red flags?

[redacted] I mean one of the things that strikes me is if you look at the statement of financial condition. I believe it was just so basic and there really was not a lot of meat there. There was no -- the customer calculations were not there.

[redacted] I think that is in the statement of financial condition.

[redacted] Twenty-twenty hindsight there are these accounting supplements where these accounting industry organizations --

[redacted] Totally Enron.

[redacted] We tried looking up Friehling and Horowitz and they were not listed as an auditor.

[redacted] Basically the accounting and

checking each other and we found out -- we did not know this at the time. There were no customer tables.

[redacted] There have been rumors for years. If you ask older people in the industry that have been around it is that his brother-in-law audits him. I heard that in 1998 as a rumor. I think a lot of people knew that rumor. To me it was that none of this stuff was secret. You did not need a rocket scientist to spot a lot of these potential issues.