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09 CV 7085

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

- against -

FRANK DIPASCALI, JR.,

Defendant.

__ Civ. ___

COMPLAINT

Plaintiff Securities and Exchange Commission ("Commission"), for its Complaint against defendant Frank DiPascali, Jr. ("DiPascali" or the "Defendant"), alleges:

SUMMARY

1. For decades, DiPascali helped Bernard L. Madoff ("Madoff") conduct a massive securities and advisory fraud at Bernard L. Madoff Investment Securities LLC ("BMIS") that victimized thousands of investors before it collapsed, causing more than $64 billion in investor losses.

2. A BMIS employee since 1975, DiPascali rose to become a key Madoff lieutenant responsible for overseeing the bulk of the day-to-day operations of the unprecedented fraud that was run out of the 17th floor at BMIS' offices.

3. DiPascali oversaw the mechanics of an entirely fictitious investment strategy, known as the "split-strike conversion," that BMIS claimed to be pursuing on behalf of its clients. DiPascali helped Madoff structure and record non-existent trades that were reflected on millions of pages of customer confirmations and account statements distributed each year. Not one of the trades purportedly executed as part of this strategy ever occurred.

4. DiPascali also played a critical role in helping Madoff avoid detection of his scheme. DiPascali designed, developed and oversaw a wide and varying array of fictitious books and records — all prepared to conceal the scheme from investors, auditors and regulators.

VIOLATIONS

5. By virtue of the conduct alleged herein, Defendant directly or indirectly, singly or in concert, has engaged in acts, practices, schemes and courses of business that violated Section 17(a) of the Securities Act of 1933 (the "Securities Act") [15 U.S.C. § 77q(a)]; violated and aided and abetted violations of Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act") [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5]; and aided and abetted violations of Sections 206(1) and 206(2) of the Investment Advisers Act of 1940 (the "Advisers Act") [15 U.S.C. §§ 80b-6(1) and (2)], Sections 15(c) and 17(a) of the Exchange Act [15 U.S.C. §§ 78o(c) and 78q(a)], and Rules 10b-3 and 17a-3 thereunder [17 C.F.R. §§ 240.10b-3 and 240.17a-

3], and Section 204 of the Advisers Act [15 U.S.C. § 80b-4] and Rule 204-2 thereunder [17 C.F.R. § 275.204-2].

NATURE OF THE PROCEEDINGS AND RELIEF SOUGHT

6. The Commission brings this action pursuant to the authority conferred upon it by Section 20(b) of the Securities Act [15 U.S.C. § 77t(b)], Section 21(d)(1) of the Exchange Act [15 U.S.C. § 78u(d)(1)], and Section 209(d) of the Advisers Act [15 U.S.C. § 80b-9(d)], seeking to restrain and enjoin permanently Defendant from engaging in the acts, practices and courses of business alleged herein.

7. In addition to the injunctive relief recited above, the Commission seeks: (i) a final judgment ordering Defendant to disgorge his ill-gotten gains with prejudgment interest thereon; (ii) a final judgment ordering Defendant to pay civil penalties pursuant to Section 20(d) of the Securities Act [15 U.S.C. § 77t(d)], Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)(3)], and Section 209(e) of the Advisers Act [15 U.S.C. § 80b-9(d)]; and (iii) such other relief as the Court deems just and appropriate.

JURISDICTION AND VENUE

8. This Court has jurisdiction over this action pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)], Sections 21(e) and 27 of the Exchange Act [15 U.S.C. §§ 78u(e) and 78aa], and Section 214 of the Advisers Act [15 U.S.C. § 80b-14].

9. Venue is proper in the Southern District of New York pursuant to 28 U.S.C. § 1391. The Defendant, directly and indirectly, has made use of the means and instrumentalities of interstate commerce, or of the mails and wires, in connection with the transactions, acts, practices and courses of business alleged herein. A substantial part of the events comprising Defendant's fraudulent activities giving rise to the Commission's

claims occurred in the Southern District of New York, and Defendant committed his fraudulent activities while working in a business office in this District.

THE DEFENDANT

10. **DiPascali**, age 52, resides in Bridgewater, New Jersey. DiPascali began working at BMIS in 1975 at the age of 19. After many years as a research clerk and then a trader, DiPascali was put in charge (by Madoff) of the build-out and computer installation in BMIS' new office space in the Lipstick Building at 885 Third Avenue in New York City in the mid-1980s. Later, at Madoff's direction, DiPascali became involved in, and eventually oversaw, the day-to-day operations of the bulk of BMIS' multi-billion dollar fraudulent scheme.

RELEVANT INDIVIDUALS AND ENTITIES

11. **Madoff**, age 71, was, until recently, a resident of New York City and the sole owner of BMIS. Until December 11, 2008, Madoff, a former chairman of the board of directors of the NASDAQ stock market, oversaw and controlled the fraudulent investment adviser business at BMIS as well as the overall finances of BMIS. Madoff was charged civilly and criminally for his role in a multi-billion dollar Ponzi scheme. See S.E.C. v. Bernard L. Madoff and Bernard L. Madoff Investment Securities LLC, No. 08-CV-10791 (S.D.N.Y.) (LLS) (the "Civil Action"); United States v. Bernard L. Madoff, No. 09 Cr. 213 (S.D.N.Y.) (DC) (the "Criminal Action"). On February 9, 2009, in the Civil Action, the District Court, with Madoff's consent, entered a partial judgment in the Commission's case against Madoff. On March 12, 2009, Madoff pleaded guilty to eleven felony counts in the Criminal Action. In his allocution, Madoff admitted that he orchestrated the massive Ponzi scheme that is the subject of the present charges. On June

29, 2009, Madoff was sentenced to 150 years in prison and ordered to forfeit his assets. Madoff is currently incarcerated in a federal prison in North Carolina.

12. **BMIS** registered with the Commission as a broker-dealer in 1960 and as an investment adviser in September 2006. BMIS used to occupy floors 17-19 of the Lipstick Building in Manhattan, New York City. BMIS purportedly engaged in three different operations: investment adviser services; market-making services; and proprietary trading. BMIS is currently under the control of a trustee appointed pursuant to the Securities Investor Protection Act of 1970 (15 U.S.C. § 78aaa et seq.).

FACTS

I. Background

A. The Advisory Business During the Early Years

13. BMIS managed investor accounts as far back as the 1960s, although the firm was ostensibly focused on market-making. For the most part, the early investors were individuals, mostly Madoff's family and friends, including some high net-worth individuals. The purported investing strategies for these accounts were primarily convertible arbitrage and stock-picking, and the accounts consistently posted double digit returns.

14. Over time, this advisory business expanded and various accountants and financial advisors began soliciting individual investors around the country and providing the money they raised to BMIS. These "feeders" sometimes issued to investors promissory notes that guaranteed high rates of return (e.g., 19%) and then invested the proceeds with BMIS at higher rates promised by Madoff (e.g., 21%), seeking to pocket the difference for themselves. Unlike the friends and family accounts, Madoff and BMIS

did not deal directly with these individual investors. Instead, Madoff dealt with the feeders and set up aggregate, pooled accounts at BMIS for each feeder, leaving it to the feeder to deal with the individual investors, issue statements to such investors, and make distribution payments to them.

B. DiPascali's Early Career

15. DiPascali joined BMIS in 1975, at the age of 19, when BMIS was a small OTC market-maker with approximately a dozen employees. A college dropout, DiPascali was introduced to BMIS by his neighbor and friend, a longtime BMIS employee who first joined in 1968. Initially, DiPascali did not work on any of the investor accounts. He first worked as a research clerk for Madoff's brother, who was an executive at BMIS, and later as a trader for Madoff. In the mid-1980s, Madoff put DiPascali in charge of overseeing the build-out of BMIS' new midtown Manhattan office space in the Lipstick Building at 885 Third Avenue, including installation of its technology platform.

16. DiPascali's stature at BMIS grew with the success of the buildout and the technology installation in the new offices. Madoff soon began turning to DiPascali for assistance with a range of special projects. During this period, in addition to assisting Madoff with special projects, DiPascali began to develop expertise in trading options.

17. In the years following BMIS' move to 885 Third Avenue, DiPascali became more involved in BMIS' advisory business, pitching in when asked to help with issues that arose with the various investor accounts at BMIS (i.e., family, friends and feeder accounts). At least as early as the 1980s, DiPascali (together with other employees

of BMIS) helped to fabricate various backdated and fictitious trades, often involving options, and to record them in investor account records for the purpose of generating phantom returns, hedges or tax events in those investors' accounts. DiPascali and others continued to help fabricate trades for this original group of accounts until the end of the fraudulent scheme in December 2008.

C. Avellino & Bienes

18. In 1992, the Commission brought charges against some of these feeders[1] for unlawfully offering securities (promissory notes) in unregistered transactions. One of the feeders then charged by the Commission was Avellino & Bienes ("A&B"), and the judge presiding in the action against A&B appointed a receiver to administer the affairs of A&B.

19. Since A&B's funds were purportedly held at BMIS, the receiver demanded that BMIS liquidate A&B's accounts and produce account records substantiating the values and trading in the accounts.

20. Madoff scrambled to secure adequate funds to meet the receiver's redemption request and to fabricate credible account records to corroborate the purported trading in the accounts. DiPascali was instrumental in fabricating after-the-fact records for the A&B accounts that appeared to substantiate profitable trading in the accounts. Upon BMIS' payment of the full amount of the purported value of these investment accounts — more than $300 million — the receiver distributed this money to thousands of A&B investors.

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[1] See SEC v. Avellino & Bienes et al., No. 92-CV-8314 (S.D.N.Y.); and SEC v. Telfran Assoc. et al., No. 92-CV-8564 (S.D.N.Y.), both of which were filed in November 1992.

II. The Split-Strike Conversion

21. The A&B case marked the beginning of a new chapter in the Madoff fraud. Following the liquidation of the A&B accounts, many of the investors reimbursed by the receiver in the A&B case came right back to BMIS. This time, they came as direct investors with BMIS, rather than the A&B feeder.

22. The size and volume of these accounts placed a great administrative burden on BMIS' small advisory account staff. Compared to the limited number of investor accounts BMIS had previously maintained, Madoff now had many hundreds of accounts.

23. To handle the volume, Madoff needed a more efficient and less labor intensive method of generating phony trade confirmations and account statements. Previously, BMIS had manually entered fictitious, backdated trades on an account-by-account basis. Madoff also needed an investment strategy that could credibly explain how he supposedly achieved specific target rates of return across hundreds of different accounts. DiPascali was instrumental in addressing both of these challenges.

A. The Strategy

24. Beginning around the time that A&B investors opened accounts at BMIS, and continuing through December 2008, Madoff told most of BMIS' investors that he managed their accounts pursuant to the split-strike conversion strategy. In fact, Madoff's entire split-strike conversion strategy was a longstanding fraud. Every trade,

every order ticket, every account statement, every confirmation and all other relevant records were fictitious.[2]

25. Because of the size of the accounts, Madoff concluded that the "strategy" had to focus on large cap stocks so that no questions would arise about the volume of purported trading they were supposedly engaging in.

26. The strategy entailed purchasing a subset of the stocks (which they called a "basket") comprising the S&P 100 index ("S&P 100"), the performance of which was presumed to correlate very closely with the performance of the overall index. The purported goal was to time the market by purchasing the basket before a run-up in the S&P 100 and selling the basket after the index increased. When Madoff sold off a basket and was not "in the market," he purportedly invested the money in U.S. Treasuries and money market funds while awaiting the next trading opportunity.

27. DiPascali used his knowledge and experience with options to help Madoff develop a fictitious hedging strategy for the new accounts. To hedge the downside risk of the phantom position, Madoff and DiPascali "purchased" fictitious put options on the S&P 100, which were supposedly funded by the "sale" of call options on the S&P 100. This now-infamous strategy has been described as a split-strike conversion. And, to be clear, none of the trading under this strategy ever actually occurred. The entire exercise was a fantasy.

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[2] A number of preexisting friends and family accounts did not migrate to the new split-strike conversion strategy. These friends and family accounts continued to be handled on an account-by-account basis through December 2008, with DiPascali and others helping to select and create backdated and phony trades to fabricate returns.

B. **The Mechanics**

28. Under DiPascali's oversight, BMIS' programmers organized the new accounts on a single IBM AS/400 computer. The accounts were set up so that one set of "trades" could be entered on an aggregate basis for all the accounts, and the computer would automatically allocate the fictitious trades, pro rata, to the various individual accounts. Once Madoff and DiPascali identified a basket trade that achieved the fictitious targeted return, the trade was proportionally replicated in each account automatically. The system then generated separate trade confirmations and account statements for each account based on its pro rata share of the purported trading and carried forward the account holdings from month-to-month.

29. Several times a year, Madoff told DiPascali that he wanted to "get into the market." At that point, DiPascali was responsible for constructing a weighted basket of approximately 35-50 of the S&P 100 stocks that was designed to correlate to the performance of the overall S&P 100 index. DiPascali then asked his staff to compile historical price (high, low, open and close) and volume data from Bloomberg for each of the stocks.

30. With the benefit of hindsight, DiPascali picked advantageous historical prices, often near the lows, to create the appearance of a profit once the purported trade was booked. DiPascali did the same for the options, virtually guaranteeing that the purported trading would appear to be profitable. However, Madoff grew concerned that showing positive returns every month would be suspicious — particularly following two press stories, published in May 2001, that raised questions about the unerring consistency

of his returns. To make the strategy and returns more credible, Madoff occasionally instructed DiPascali to enter phony basket trades designed to lose money.

31. Madoff instructed DiPascali to generate a credible annual return for the strategy, between 10 and 17%, although in the later years of the fraud the returns shifted towards the lower end of the range. Indeed, Madoff essentially promised some investors that they would enjoy a particular rate of return. To achieve these phantom returns, DiPascali closely monitored the basket and consulted with Madoff to ensure that the gains were appropriate — not too high or too low. Then, after several weeks of holding the positions, Madoff directed DiPascali to sell off the basket and book a modest profit, averaging a return in the fraud's later years of about 1% per month. Since no actual purchase or sale took place, DiPascali could examine the historical prices of the securities comprising the basket and pick such date and pricing for the "sale" of the basket as was needed to achieve the targeted rate of return.

32. Madoff had promised certain investors a higher rate of return than what the bulk of the split-strike conversion accounts were supposedly generating. To achieve these higher promised returns, Madoff instructed DiPascali to execute an extra round of fictitious trades in a subset of investor accounts each December to boost their performance even higher.

33. Madoff did not have real-time access to the positions, performance or value of the basket. Madoff had to call DiPascali (or others on DiPascali's staff) for updates, which he did several times a day.

34. Once Madoff decided to do a "basket trade," DiPascali (or his staff) provided key punch operators with the relevant pricing information and they then entered

the data into the AS/400. The system then generated and printed hundreds of thousands of pages of confirmations (a separate one for each stock, for each account), which BMIS then mailed out to each investor. Millions of pages of paper and hundreds of hours of BMIS employee time were expended on these mailings each year.

35. DiPascali and the advisory accounts staff were eventually moved to the 17th floor of 885 Third Avenue to support this massive undertaking.

36. Certain practices were followed to ensure that the bogus trading appeared credible. For example, since the reported trades never happened and the prices were not real, there was no third-party confirmation process to eliminate the risk of potentially conspicuous errors, such as recording trades at prices or in volumes that did not exist in the market on the trade date appearing in investor account records. To reduce the risk of such anomalies, DiPascali introduced various controls, including a procedure whereby members of his staff attempted to check all trades to ensure that the reported prices were within the high-low range for the day.

37. In addition, because of the size of some of the BMIS accounts (some of the fund-of-funds accounts were in the billions of dollars), DiPascali and Madoff were concerned that it would look suspicious if they went into the market all at once, in a single day. To address this, DiPascali and Madoff decided that only accounts with balances of $20 million or less (the "regs," for the thousands of regular investors) would fully enter or exit the market in a single day. For the accounts with over $20 million in assets (the "pros," for the couple of hundred larger investors, including most professional investors), the move into or out of the market might only encompass a portion of the total account or might be spread over a few days.

38. During the earlier years of the split-strike conversion, DiPascali's lookback reached back several days. However, as the investors became more sophisticated, particularly the fund-of-fund investors, Madoff and DiPascali had to provide confirmations to investors closer in time to the purported trading. As time went on, the "lookback" could only extend back a day or so before the confirmations had to be sent out.

39. Despite this limitation, DiPascali found enough flexibility, particularly in the pricing and timing for the phantom S&P 100 options, to generate the appearance of consistently positive annual returns.

40. DiPascali understood that the purported trading for these options accounts was fictitious. He knew that none of these securities was ever purchased. He knew that the transaction prices did not reflect actual transactions, but were picked after-the-fact to generate fictitious returns. He knew that there were no trade confirmations or account documentation coming from anywhere outside of BMIS that reflected the purported trading being shown in the client accounts.

41. DiPascali knew that BMIS' entire split-strike conversion strategy and tens of billions of dollars of purported trading in the investor accounts were a sham.

C. Lies to Investors

42. Notwithstanding his knowledge that the strategy was a fiction, DiPascali maintained the façade to investors.

43. Year after year, he directed that millions of pages of false account statements and trade confirmations be prepared and distributed to thousands of investors.

He knew that the holdings, the transactions, and the returns on those accounts were false and he lied to investors about it.

44. In addition to the massive mailings of fraudulent trading and account records, DiPascali spoke to investors about their advisory accounts at BMIS and lied directly to them about their accounts. He lied about the trades and account values; he lied about the strategy and purported controls; he lied about BMIS' proxy voting policies and its custody of assets. Everything about the BMIS advisory accounts was a lie because the securities did not exist.

D. The Money

45. DiPascali knew that when investors sent in funds to BMIS for investment, the funds were deposited or wired into a bank account at JPMorgan Chase (the "703 Account"). He also knew that this account was not in any way reflected on the books and records (including the ledger) of BMIS' broker-dealer operation.

46. DiPascali knew that investors' redemptions were funded by this same 703 Account and that there was no affiliated trading account to which these funds were ever sent or received.

47. The 703 Account was nothing more than a slush fund. Every day, members of DiPascali's staff prepared for Madoff reports showing how much investor money was deposited and withdrawn from the 703 Account. Any excess cash in the account was transferred to an affiliated JPMorgan Chase account and a handful of other accounts and used to purchase U.S. Treasuries and other short-term paper until the money was needed to fund investor redemptions, BMIS' broker-dealer operations, or some other personal need of Madoff's.

48. By the summer of 2008, the value of this affiliated account exceeded $5.5 billion. Following the market collapse in September 2008, however, investor redemptions spiked dramatically, requiring Madoff to distribute to investors more than $6 billion in the final three months of the fraud.

49. DiPascali and Madoff also misappropriated funds from the 703 Account to enrich themselves.

50. Beginning in or about 2002, DiPascali set up an account at BMIS for himself. DiPascali named the account after his fishing yacht, Dorothy Jo. Although DiPascali made no capital contributions to the account and had no positive balance in the account, DiPascali withdrew over $5 million from the account between 2002 and 2008 to fund his personal expenses, including the purchase of a new boat.

51. DiPascali's withdrawals were funded directly from money deposited by investors with BMIS. Investor money in the 703 Account was being used to fund the overall operations of BMIS, and, therefore, contributing to the over $2 million in salary and bonus that DiPascali received from BMIS each year.

52. In the final days of the fraud, the money available to meet investor redemptions had dwindled to a few hundred million dollars. DiPascali and Madoff discussed using the remaining funds to liquidate the accounts of family and friends of the firm, including employees, rather than honor redemption requests by BMIS' larger institutional investors.

53. To that end, DiPascali reviewed BMIS investor lists and identified which accounts should be liquidated. With Madoff's approval, he then instructed that checks be prepared to liquidate those accounts. These checks, totaling more than $150 million,

were then prepared. However, Madoff was arrested and the checks were seized before they could be distributed.

E. The Cover-Up

54. Over the course of this extended and far-reaching fraud, BMIS was subject to scrutiny by a number of different constituent groups, including investors, auditors, regulators and journalists. Madoff communicated through words or actions to DiPascali his fear of detection. At Madoff's direction, a significant portion of DiPascali's time and effort (as well as the time and effort of other BMIS employees) was dedicated to anticipating and preparing for such inquiries and audits — in particular, SEC examinations in 2004 and 2005 and an SEC investigation in 2006.

(1) Falsified Books and Records

55. One reason the fraud was not detected for so long was DiPascali's considerable success in overseeing the creation of large quantities of false books and records that corroborated the fictitious trading.

56. In addition to allocating trades and generating trade confirmations and account statements, the AS/400 computer system housed and automatically generated books and records reflecting the phantom trading in the advisory accounts.

57. This computer and the books and records it generated were separate and distinct from the books and records for BMIS' market-making and proprietary trading operation, which in the later years used a different computer system.

58. Because no actual trading took place in the advisory accounts, the books and records generated by the AS/400 were incomplete and Madoff was concerned that they would raise doubts in the eyes of a regulator or auditor. For example, trade blotters

and order tickets could not be generated by the AS/400 with credible execution times, counterparties or executing brokers.

59. In addition, the stock record for the advisory accounts did not reflect any real holdings and would not match the records held in BMIS' name at Depository Trust Corporation ("DTC"), which is the central securities depository in the United States.

60. Madoff and DiPascali, together with other BMIS employees, addressed these issues in a number of ways, often varying the approach depending on who was reviewing the records. Following are some examples of the methods they employed to avoid detection of the scheme during third party inquiries and examinations:

(a) Special Accounts. Although great effort was made to conceal the existence of advisory accounts to the fullest extent possible, some audits and regulatory inquiries required an acknowledgment that the business existed and the production of books and records to substantiate the activity in those accounts. However, Madoff was careful to avoid ever disclosing the scope and magnitude of the accounts, hiding the fact that there were several thousand accounts with aggregate values in excess of $50 billion. Accordingly, DiPascali helped Madoff devise a shifting subset of 10 to 25 accounts — the "special" accounts — which they deceptively presented as the universe of BMIS advisory accounts. DiPascali and others then prepared various fake books and records reflecting only this subset. This way, BMIS provided auditors and regulators with just enough information to make the phony books and records appear credible but not enough to appreciate the magnitude of the advisory business.

(b) Custody. Because securities were never purchased on behalf of investors, it was important to deflect inquiries into the custody of assets. One

deceptive tactic was to claim that the assets were not custodied at BMIS because BMIS only functioned as an executing broker on an RVP/DVP (receive-versus-payment and delivery-versus-payment) basis. To substantiate this story, Madoff directed DiPascali and others to prepare alternate account statements and records for the special accounts. The alternate account statements excluded certain purported transactions and information that were inconsistent with an RVP/DVP arrangement. Madoff also directed DiPascali and others to change the titles for the special accounts to indicate that the assets were custodied elsewhere. For example, an account in the name of "John Doe" was changed to "European Bank for the benefit of John Doe" on the fictitious set of account statements and trade reports given to auditors or regulators. In this way, the assets were purportedly custodied at European Bank and there would be no reason to ask DTC for records reflecting BMIS holdings since the stock was held in street name at European Bank, not BMIS. Madoff even ordered that old, superseded BMIS stationary and letterhead be maintained indefinitely in case he had to fabricate records going back further in time.

(c) **DTC Reports**. For some investors and auditors, BMIS purported to hold custody of the advisory account assets. To address due diligence custody audits, Madoff directed DiPascali and others to create fake DTC reports. DiPascali and others spent substantial time and effort ensuring that these reports mimicked the layout, print font and paper-type of actual DTC reports. Madoff and DiPascali then made these fake DTC reports available to auditors for review. One investor was even shown the report onscreen at a computer terminal at BMIS and told that the computer was receiving a live feed from DTC.

(d) **Shifting Counterparties**. The advisory account records on

the AS/400 did not reflect any counterparty information (because none existed). To respond to inquiries from regulators and auditors, however, DiPascali had to create credible trade blotters for the BMIS advisory business that included counterparty information. Including counterparties, however, created a risk of detection because the regulator or auditor might approach the counterparty for its corresponding records and compare the two. This risk was particularly acute for option trades because Madoff and DiPascali, when pressed about the volume or pricing of option positions, would explain that the option trading was not done on any exchange but directly with counterparties over-the-counter. To alleviate this risk, DiPascali, at Madoff's direction, created a list of counterparties that were unlikely to be approached for verification. On the one hand, when regulators and auditors in the U.S. asked for the information, DiPascali provided a list of European financial institutions. On the other hand, when auditors for European investors asked for the information, DiPascali provided names of U.S. dealers. In addition to providing the list of names, DiPascali directed that fake trade blotters be prepared for only the "special" accounts to reflect fictitious trading with the various counterparties on the relevant list. These records were provided to regulators and auditors.

(e) **Random Number Generator.** BMIS received specific requests from regulators for order execution information for the advisory accounts. Since billions of dollars of fictitious trades were generally keyed into the AS/400 at one time, DiPascali could not use the data as it existed on the AS/400 because the order time would not be credible. Instead, he developed a report that would appear to reflect actual trading, at variable intervals and in different increments. To generate the report, DiPascali and

others created and used a random number generator program to break up the massive trades into orders of variant sizes and prices and to randomly distribute the trades across different times. Furthermore, to avoid the possibility that the pricing at those intervals might not match the consolidated trading tape, DiPascali directed that the orders be "executed" during the early part of the day in Europe (the middle of the night in the U.S.). Madoff, DiPascali and others then represented that the single execution price reflected on the investor confirmations was an average price for trading purportedly done in the European market.

(2) Miscellaneous Other Ruses

61. In addition to the false books and records, DiPascali helped Madoff and BMIS engage in other subterfuges to avoid detection:

(a) Despite the mandatory registration requirement for investment advisers, Madoff failed to register BMIS with the Commission as an adviser for many years in order to avoid scrutiny of the phantom advisory business. Following a 2006 inquiry by Commission staff, BMIS did register with the Commission and filed a Form ADV; however, the ADV filing failed to reflect the full scope of the advisory business. Only the assets and identity of a small subset of "special" accounts (only 23) that DiPascali had constructed were reflected on the Form ADV, shielding the vast scope of the advisory business from view.

(b) In order to avoid scrutiny by sophisticated financial institutions that might notice something troubling about BMIS' account statements or trading activity, Madoff developed a practice, which DiPascali enforced, of closing down accounts for investors who worked at such institutions. When DiPascali learned that

BMIS received a request from a compliance department at a financial institution for an account statement of an employee (which many financial institutions do as a matter of policy), DiPascali would inform Madoff, who then directed that the account be closed.

(c) Concerned that Forms 13-F filed with the Commission by BMIS' fund-of-fund investors would expose the magnitude of the fictitious BMIS positions to the outside world, Madoff and DiPascali pretended to exit the split-strike conversion strategy and shift into U.S. Treasuries before the close of the quarterly reporting periods. In this way, they avoided having fictitious options and stock positions disclosed in public filings of its investors (or of BMIS).

(d) Madoff and DiPascali told regulators that BMIS executed the trades for the advisory accounts overseas and that it received a fee of four cents per share as compensation for these executions. To substantiate that story, Madoff transferred investor funds from the 703 Account to his London firm, Madoff Securities International Ltd., and then had those funds transferred back to the BMIS operating account for the market-making and proprietary trading part of the business. These circuitous transfers — which from 2005 to 2008 totaled approximately $250 million or more — made it appear from the books and records for the market-making side of the business that commissions revenue was being paid to BMIS from overseas. The transfers also provided convenient cover for Madoff to move assets of his advisory clients to his non-advisory businesses and ultimately to his own pocket. DiPascali was aware of and took part in discussions about these transfers and their purpose.

(e) Madoff was concerned that an investor, auditor or regulator might request to observe trading in the advisory accounts in real time at BMIS' offices.

To prepare for this possibility, Madoff instructed DiPascali to oversee a phantom computer trading platform that would appear to reflect real trading. In the event of a surprise visit from outsiders requesting to observe real time trading activity, one BMIS employee was to enter trades on a computer screen and another was to go into an office nearby that was equipped with a linked computer and play the role of a counterparty trader in Europe. At Madoff's direction, DiPascali and others tested this network periodically to ensure that it remained operational.

(f) During the Commission staff's 2006 investigation, DiPascali gave testimony that was fraught with false and misleading statements. He lied about the number of client accounts and about the extent of assets under management. He also testified that the trading was real and that he personally received and reviewed trade confirmations for the options trades, none of which was true.

FIRST CLAIM FOR RELIEF

Violations of Section 17(a)(1) of the Securities Act (Antifraud violations)

62. Paragraphs 1 through 61 are realleged and incorporated by reference as if set forth fully herein.

63. From at least the 1980s through December 11, 2008, the Defendant, in the offer and sale of securities, by the use of the means and instruments of transportation and communication in interstate commerce or by the use of the mails and/or wires, directly and indirectly, has employed devices, schemes and artifices to defraud.

64. The Defendant knew or was reckless in not knowing of the activities described above.

65. By reason of the activities herein described, the Defendant has violated

Section 17(a)(1) of the Securities Act [15 U.S.C. § 77q(a)(1)].

SECOND CLAIM FOR RELIEF

Violations of Section 17(a)(2) and 17(a)(3) of the Securities Act (Antifraud violations)

66. Paragraphs 1 through 61 are realleged and incorporated by reference as if set forth fully herein.

67. From at least the 1980s through December 11, 2008, the Defendant, in the offer and sale of securities, by the use of the means and instruments of transportation and communication in interstate commerce or by the use of the mails and/or wires, directly and indirectly, has obtained money and property by means of untrue statements of material fact or omissions to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, and has engaged in transactions, practices or courses of business which have operated as a fraud and deceit upon investors.

68. The Defendant knew, was reckless in not knowing, or should have known of the activities described above.

69. By reason of the activities herein described, the Defendant has violated Sections 17(a)(2) and 17(a)(3) of the Securities Act [15 U.S.C. §§ 77q(a)(2) and 77q(a)(3)].

THIRD CLAIM FOR RELIEF

Violations of, and Aiding and Abetting Violations of, Section 10(b) of the Exchange Act and Rule 10b-5 (Antifraud violations)

70. Paragraphs 1 through 61 are realleged and incorporated by reference as if set forth fully herein.

71. From at least the 1980s through December 11, 2008, the Defendant, in

connection with the purchase and sale of securities, directly and indirectly, by the use of the means and instrumentalities of interstate commerce or of the mails and/or wires, has employed devices, schemes and artifices to defraud; has made untrue statements of material fact and has omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and has engaged in acts, practices and courses of business which operated as a fraud and deceit upon investors.

72. By reason of the activities herein described, the Defendant has violated Section 10(b) of the Exchange Act [15 U.S.C. §§ 78j(b)] and Rule 10b-5 [17 C.F.R. § 240.10b-5] promulgated thereunder.

73. In addition, from at least the 1980s through December 11, 2008, Madoff and BMIS, in connection with the purchase and sale of securities, directly and indirectly, by the use of the means and instrumentalities of interstate commerce or of the mails and/or wires, have employed devices, schemes and artifices to defraud; have made untrue statements of material fact and have omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and have engaged in acts, practices and courses of business which operated as a fraud and deceit upon investors.

74. By reason of the foregoing, and pursuant to Section 20(e) of the Exchange Act [15 U.S.C. § 78t(e)], the Defendant has aided and abetted Madoff's and BMIS' violations of Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5(a), (b) and (c) promulgated thereunder [17 C.F.R. §§ 240.10b-5(a), (b) and (c)]. Specifically, the Defendant knowingly provided substantial assistance to Madoff and

BMIS in committing such violations.

FOURTH CLAIM FOR RELIEF

Aiding and Abetting Violations of Sections 206(1) and 206(2) of the Advisers Act (Fraud upon Advisory Clients and Breach of Fiduciary Duty by Investment Adviser)

75. Paragraphs 1 through 61 are realleged and incorporated by reference as if set forth fully herein.

76. Madoff and BMIS at all relevant times were investment advisers within the meaning of Section 202(11) of the Advisers Act [15 U.S.C. § 80b-2(11)].

77. Madoff and BMIS directly or indirectly, singly or in concert, knowingly or recklessly, through the use of the mails or any means or instrumentality of interstate commerce, while acting as investment advisers within the meaning of Section 202(11) of the Advisers Act [15 U.S.C. § 80b-2(11)]: (a) have employed devices, schemes, and artifices to defraud any client or prospective client; or (b) have engaged in acts, practices, or courses of business which operate as a fraud or deceit upon any client or prospective client.

78. As described in the paragraphs above, Madoff and BMIS violated Sections 206(1) and 206(2) of the Advisers Act [15 U.S.C. §§ 80b-6(1), (2)].

79. By reason of the activities described herein, and pursuant to Section 209(d) of the Advisers Act [15 U.S.C. § 80b-9(d)], the Defendant has aided and abetted Madoff's and BMIS' violations of Sections 206(1) and 206(2) of the Advisers Act [15 U.S.C. §§ 80b-6(1) and 80b-6(2)]. Specifically, the Defendant knowingly provided substantial assistance to Madoff and BMIS in committing such violations.

FIFTH CLAIM FOR RELIEF

Aiding and Abetting Violations of Section 15(c) of the Exchange Act and Rule 10b-3 (Fraud Upon Customers by Broker-Dealer)

80. Paragraphs 1 through 61 are realleged and incorporated by reference as if set forth fully herein.

81. BMIS is a broker within the meaning of Section 3(a)(4) of the Exchange Act [15 U.S.C. § 78c(a)(4)].

82. From at least the 1980s through December 11, 2008, BMIS, while a broker, by engaging in the conduct described above, made use of the mails or means or instrumentalities of interstate commerce to effect transactions in, or to induce or attempt to induce the purchase or sale of securities (other than commercial paper, bankers' acceptances or commercial bills) otherwise than on a national securities exchange of which BMIS was a member, by means of manipulative, deceptive, or other fraudulent devices or contrivances.

83. BMIS' manipulative, deceptive, and fraudulent devices or contrivances included representations to customers that securities transactions occurred, and securities were held, in their accounts when no such transactions occurred and no such securities were held in customers' accounts.

84. Defendant knew these statements were false.

85. By reason of the activities described herein, and pursuant to Section 20(e) of the Exchange Act [15 U.S.C. § 78t(e)], Defendant has aided and abetted BMIS' violations of Section 15(c) of the Exchange Act [15 U.S.C. § 78o(c)] and Rule 10b-3

thereunder [17 C.F.R. § 240.10b-3]. Specifically, Defendant knowingly provided substantial assistance to BMIS in committing such violations.

SIXTH CLAIM FOR RELIEF

Aiding and Abetting Violations of Section 17(a) of the Exchange Act and Rule 17a-3 (Broker-Dealer Books and Records Violations)

86. Paragraphs 1 through 61 are realleged and incorporated by reference as if set forth fully herein.

87. As a registered broker-dealer, BMIS was required to make and keep certain books and records current and accurate pursuant to Section 17(a) of the Exchange Act [15 U.S.C. § 78q(a)] and Rule 17a-3 thereunder [17 C.F.R. § 240.17a-3].

88. As set forth above, BMIS failed to make and keep certain books and records current and accurate. BMIS, among other things, manufactured and maintained account statements, ledgers, journals and other records reflecting fictitious securities holdings and fictitious securities transactions in investors' accounts.

89. As a result, BMIS violated Section 17(a) of the Exchange Act and Rule 17a-3 promulgated thereunder [15 U.S.C. § 78q(a) and 17 C.F.R. § 240.17a-3].

90. The Defendant knew that BMIS manufactured and maintained account statements, ledgers, journals and other records reflecting fictitious securities holdings and fictitious securities transactions in investors' accounts.

91. By reason of the foregoing, and pursuant to Section 20(e) of the Exchange Act [15 U.S.C. § 78t(e)], the Defendant aided and abetted the violations of Section 17(a) of the Exchange Act [15 U.S.C. § 78q(a)] and Rule 17a-3 thereunder [17 C.F.R. § 240.17a-3]. Specifically, Defendant knowingly provided substantial assistance to BMIS in committing such violations.

SEVENTH CLAIM FOR RELIEF

Aiding and abetting violations of Section 204 and Rule 204-2 of the Advisers Act (Adviser Books and Records Violations)

92. Paragraphs 1 through 61 are realleged and incorporated by reference as if set forth fully herein.

93. BMIS at all relevant times was an investment adviser within the meaning of Section 202(11) of the Advisers Act [15 U.S.C. § 80b-2(11)].

94. BMIS failed to make, maintain on its premises, or keep accurate, certain books and records required by law. For example, BMIS failed to make, maintain on its premises or keep accurate, books and records concerning its assets, liabilities, finances, client accounts, closed client accounts, and correspondence with clients. Among other things, BMIS manufactured and maintained account statements, ledgers, journals and other records reflecting fictitious securities holdings and fictitious securities transactions in investors' accounts.

95. The Defendant knew that BMIS manufactured and maintained account statements, ledgers, journals and other records reflecting fictitious securities holdings and fictitious securities transactions in investors' accounts.

96. By reason of the foregoing, BMIS violated Section 204 of the Advisers Act [15 U.S.C. § 80b-4], and Rule 204-2 thereunder [17 C.F.R. § 275.204-2], and the Defendant aided and abetted BMIS' violations. Specifically, Defendant knowingly provided substantial assistance to BMIS in committing such violations.

PRAYER FOR RELIEF

WHEREFORE, the Commission respectfully requests that the Court enter a final judgment against the Defendant granting the following relief:

I.

Finding that the Defendant violated the securities laws and rules promulgated thereunder as alleged herein.

II.

Permanently restraining and enjoining the Defendant, his agents, servants, employees and attorneys and all persons in active concert or participation with them who receive actual notice of the injunction by personal service or otherwise, and each of them, from committing future violations of Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)].

III.

Permanently restraining and enjoining the Defendant, his agents, servants, employees and attorneys and all persons in active concert or participation with them who receive actual notice of the injunction by personal service or otherwise, and each of them, from committing or aiding and abetting future violations of Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

IV.

Permanently restraining and enjoining the Defendant, his agents, servants, employees and attorneys and all persons in active concert or participation with them who receive actual notice of the injunction by personal service or otherwise, and each of them, from committing or aiding and abetting future violations of Sections 206(1) and 206(2) of the Advisers Act [15 U.S.C. §§ 80b-6(1) and (2)].

V.

Permanently restraining and enjoining the Defendant, his agents, servants, employees and attorneys and all persons in active concert or participation with them who receive actual notice of the injunction by personal service or otherwise, and each of them, from committing or aiding and abetting future violations of Section 15(c) of the Exchange Act [15 U.S.C. § 78o(c)] and Rule 10b-3 thereunder [17 C.F.R. § 240.10b-3].

VI.

Permanently restraining and enjoining the Defendant, his agents, servants, employees and attorneys and all persons in active concert or participation with them who receive actual notice of the injunction by personal service or otherwise, and each of them, from committing or aiding and abetting future violations of Section 17(a) of the Exchange Act [15 U.S.C. § 78q(a)] and Rule 17a-3 thereunder [17 C.F.R. § 240.17a-3].

VII.

Permanently restraining and enjoining the Defendant, his agents, servants, employees and attorneys and all persons in active concert or participation with them who receive actual notice of the injunction by personal service or otherwise, and each of them, from committing or aiding and abetting future violations of Section 204 of the Advisers Act [15 U.S.C. § 80b-4], and Rule 204-2 thereunder [17 C.F.R. § 275.204-2].

VIII.

Directing the Defendant to disgorge his ill-gotten gains, plus prejudgment interest thereon.

IX.

Directing the Defendant to pay civil money penalties pursuant to Section 20(d) of the Securities Act [15 U.S.C. § 77t(d)], Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)(3)], and Section 209(e) of the Advisers Act [15 U.S.C. § 80b-9].

X.

Granting such other and further relief as to this Court seems just and proper.

Dated: New York, New York
August 11, 2009

SECURITIES AND EXCHANGE COMMISSION

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