U.S. Securities and Exchange Commission

SEC Charges Key Madoff Lieutenant for Operating and Concealing Fraud Through Bogus Trades and Documents

FOR IMMEDIATE RELEASE
2009-182

Washington, D.C., Aug. 11, 2009 — The Securities and Exchange Commission today charged Bernard L. Madoff's chief financial officer, Frank DiPascali, with securities fraud for overseeing the mechanics of Madoff's entirely fictitious investment strategy and creating millions of phony documents and trading records to conceal the fraud from regulators and investors.

Additional Materials

- Litigation Release No. 21174
- SEC Complaint

According to the SEC's complaint, filed in U.S. District Court for the Southern District of New York, DiPascali helped generate bogus annual returns of 10 to 17 percent by fabricating backdated and fictitious trades that never occurred. The SEC further alleges that DiPascali helped Madoff cover up the fraud by preparing fake trade blotters, stock records, customer confirmations, Depository Trust Corporation (DTC) reports and other phantom books and records to substantiate the non-existent trading.

"DiPascali and Madoff ran an extraordinary and massive counterfeiting operation that concealed their fraud from investors and regulators alike," said Robert Khuzami, Director of the SEC's Division of Enforcement.

Without admitting or denying the allegations of the SEC's complaint, DiPascali has consented to a proposed partial judgment, which if entered by the court would impose a permanent injunction against DiPascali and leave the issues of disgorgement and a financial penalty to be decided at a later time.

The SEC alleges that DiPascali, who resides in Bridgewater, N.J., sustained Madoff's unprecedented fraud from at least the 1980s until the scheme's collapse, causing billions of dollars in investor losses. A specific computer was used to simulate phantom trading in advisory accounts, and to generate phony books and records reflecting that trading. This fake set of books and records was kept separate and distinct from the books and records for the market-making and proprietary trading operation at Bernard L. Madoff Investment Securities LLC (BMIS). When investors sent in funds to BMIS for investment, the funds were deposited or wired into a bank account at JPMorgan Chase that was not in any way reflected on the books and records (including the ledger) of the BMIS broker-dealer operation.

The SEC's complaint alleges that great effort was made to hide the fact that there were several thousand advisory accounts at BMIS, which would have required SEC registration. DiPascali helped Madoff devise a shifting subset of 10 to 25 accounts — known as the "special" accounts — which they deceptively presented as the universe of BMIS advisory accounts. DiPascali and others prepared fake books and records to provide regulators with information about only these special accounts in order to conceal the true size of the advisory business.

According to the SEC's complaint, DiPascali joined BMIS as a research clerk at age 19 after dropping out of college. Eventually, Madoff put DiPascali in charge of the bulk of day-to-day operations on the now-infamous 17th floor of BMIS. As Madoff consistently communicated his fear of detection to DiPascali, a significant portion of DiPascali's time and effort was dedicated to anticipating and preparing for regulatory inquiries — particularly SEC examinations in 2004 and 2005 and an SEC investigation in 2006.

The SEC's complaint alleges that DiPascali helped carry out Madoff's fictitious "split-strike conversion" strategy 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. None of the trades purportedly executed as part of this strategy ever occurred. In fact, the strategy was nothing more than fictitious trading by hindsight, supported by documents created after the fact based on actual historical data.

According to the SEC's complaint, DiPascali helped Madoff cover his tracks in numerous nefarious ways. For instance, when Madoff grew concerned that showing positive returns every month would be suspicious, he occasionally instructed DiPascali to enter phony trades designed to lose money in order to make their investment strategy and returns more credible. In order to avoid scrutiny by sophisticated financial institutions, they made a practice of closing down accounts of investors who worked at such institutions. Madoff and DiPascali even went so far as to develop 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 employee was to go into an office nearby and play the role of a counterparty trader in Europe.

The SEC further alleges that DiPascali misappropriated investor funds for personal gain, setting up an account at BMIS for himself in 2002 that he named after his fishing yacht, Dorothy Jo. DiPascali withdrew more than $5 million from the account between 2002 and 2008 to fund personal expenses, including the purchase of a new boat. DiPascali's withdrawals were funded directly from money deposited by investors with BMIS. Investor money being used to fund the overall operations of BMIS also contributed to the more than $2 million in salary and bonus that DiPascali received each year.

Today's charges mark the fifth enforcement action taken by the SEC related to the Madoff fraud. Previously, the Commission charged Madoff and BMIS, their auditors, certain solicitors, and certain feeder funds.

The Commission's complaint specifically alleges that DiPascali violated Section 17(a) of the Securities Act; violated, and aided and abetted violations of, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder; and aided and abetted violations of Sections 204, 206(1) and 206(2) of the Advisers Act and Rule 204-2 thereunder and Sections 15(c) and 17(a) of the Exchange Act and Rules 10b-3 and 17a-3 thereunder. Among other things, the SEC's complaint seeks financial penalties and a court order requiring DiPascali to disgorge his ill-gotten gains.

The Commission acknowledges the assistance of the U.S. Attorney's Office for the Southern District of New York and the Federal Bureau of Investigation. The Commission's investigation is continuing.

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