Fw:

12/17/2004 7:14:19 PM

From: McCarthy, John A.
To: Swanson, Eric J. [SwansonE@sec.gov]

They shld receive nbbo at execution time---this is crazy email. U need to follow up.

Sent from my BlackBerry Wireless Handheld

-----Original Message-----
From: [redacted]
To: [redacted]; Colby, Robert LD [redacted]
CC: [redacted] McCarthy, John A. <McCarthyJA@sec.gov>; Gadziala, Mary Ann [redacted]

Sent: Fri Dec 17 16:32:58 2004
Subject: RE:

I spoke with [redacted] at Madoff. Andy Madoff subsequently called me to give us more information.

Madoff indicated that the problem that the firm experienced this morning was related to the delay in opening Pfizer this morning on the NYSE. Due to a huge order imbalance on the sell side, the stock did not open on the NYSE until 10:09:25 a.m. (Eastern) - it opened on the NYSE at 23.52, down 5.46 (18.84%) from yesterday's NYSE close.

Prior to the NYSE opening, Madoff received over 1300 orders that were guaranteed to receive the NYSE opening price. The firm's systems automatically give orders the NYSE opening price only if the firm receives the orders by 9:30 a.m. Orders received after 9:30 a.m. -- but before the NYSE open -- are still due the NYSE opening price, but these late orders have to be executed manually.

Of the 1300 orders received by the firm, approximately 90% were received before 9:30 a.m. and these orders were executed automatically at the proper NYSE opening price. The remaining orders had to be executed manually. Due to the volatility at the open, many of these late trades inadvertently received prices away from the NYSE opening price. As a result, the firm needed to cancel these trades and give customers new executions at the proper price. In order to do this, however, the firm reportedly had to cancel all of its 1300 trades and then re-execute all of the orders at the proper price. In 90% of the 1300 orders, therefore, the cancelled orders were re-executed at the same (correct) price that they had previously received. The remaining 10% received new execution prices that matched the NYSE opening price. All of these re-executions were reported to the tape as "sold sales" to reflect the fact that they were not indicative of current prices. All of these cancellations and sold sales were reported to the tape with an OTC market indication.

We also noticed on Bloomberg that there were about 150 sold sales reported by NSX. These were not related to Madoff's activity. Instead, the NSX indicates that these reports reflected "limit order protected" trades by Scott Trade. In these instances, the firm also guarantees the NYSE opening price. The firm does this by routing a matching proprietary order to the NYSE. When the NYSE executes this order, the firm turns around and does a trade with its customer at the same price. Because of the time lag in executing this matched trade with the customer (which may now be at a price outside of the current NBBO), these trades are also reported to the tape as sold sales.

[redacted]

-----Original Message-----
From: [redacted]
Sent: Friday, December 17, 2004 1:49 PM
To: Colby, Robert LD

Cc: [redacted] McCarthy, John A.; Gadziala, Mary Ann
Subject: RE:

Bob:
I spoke with StockWatch at the NYSE and Nasdaq. The NYSE indicates that the trade cancellations were coming from the OTC market. Nasdaq StockWatch indicates the cancellations were coming from Madoff. They report that Madoff experienced some sort of systems glitch that resulted in a large number of orders receiving inappropriate execution prices. The firm then cancelled these executions and subsequently effected the trades at correct prices. These trades were then