

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

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

 COPY

WITNESS: Number ~~27~~ 31  
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3rd Floor Conference Room  
Washington, D.C. 20549  
DATE: Monday, April 27, 2009

The above-entitled matter came on for hearing,  
pursuant to notice, at 9:45 a.m.

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EARANCES:

On behalf of the Securities and Exchange Commission:

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## C O N T E N T S

1			
2			
3	WITNESS:		EXAMINATION
4	John McCarthy		9
5			
6	EXHIBITS:	DESCRIPTION	IDENTIFIED
7	1	Non-Disclosure and Confidentiality	9
8		Agreement - McCarthy	
9	2	Appendix A, List of Examinations	
10		and Staff	26
11	3a	8/3/2000 Memo, Richards and McCarthy	29
12		to Walker and Cutler	
13	3b	12/20/2000 Letter, Richards to	29
14		S. Madoff Skoller	
15	3c	3/8/2001 Memo, McCarthy to Richardson	29
16	4	3/3/03 Memo with attachment	32
17	5	10/20/2002 E-mail OCIE Staff Attorney	33
18	6	8/27/03 E-mail, ██████████ to Daugherty	36
19	7	10/29/03 E-mail, McCarthy to Swanson	36
20		Entitled: Call Madoff Re: Fleet ASAP OCIE Staff Attorney	
21	8	11/10/03 Memo, ██████████ to Swanson	37
22	9	Barron's Article 5/7/01	42
23	10	12/11/03 E-mail, McCarthy to Swanson	48
24	11	5/21/03 E-mail with attachments,	49
25		██████████ to Kelly	

1	EXHIBITS:	DESCRIPTION	IDENTIFIED
2	12a	12/18/03 E-mail, McCarthy to Richards	51
3	12b	12/2003 Planning Memorandum	52
4	13	12/17/03 Draft Letter, Swanson	65
5		to NASD	
6	14	12/10/03 E-mail, Richards to	67
7		McCarthy	
8	15	12/18/03 E-mail, Richards to McCarthy	73
9	16	12/19/03 E-mail, Donohue to Daugherty	73
10	17	Madoff Document Request	76
11	18	1/6/04 E-mail, Swanson to P. Madoff	76
12	19	1/16/04 Letter, B. Madoff to Swanson	82
13	20	1/29/04 Notes from call with [REDACTED]	87
14		[REDACTED]	
15	21	2/4/04 Notes from Conference Call with	91
16		B. Madoff	
17	22	Handwritten notes	92
18	23	2/4/04 E-mail from Walker to Donohue	94
19		and Wood	
20	24	3/11/04 Memo from Richards, McCarthy,	94
21		Swanson, Donohue, and Daugherty to Gray	
22	25	Document Requests to B. Madoff, Drafts	95
23		1-10 and Final	
24	26	Draft Letter from Swanson to P. Madoff	96
25	27	3/11/04 Letter from B. Madoff to Swanson	97

1	EXHIBITS:	DESCRIPTION	IDENTIFIED
2	28	Madoff Investment Securities	98
3		Account Statements	
4	29	3/9/04 Letter, McCarthy to Firestone	103
5	30	4/6/04 E-mail, Walker to Sadowski	107
6	31	4/7/04 E-mail, Donohue to Walker	107
7	32	3/16/05 E-mail, Donohue to Swanson	110
8	33	2/28/06 E-mail, McCarthy to Swanson	117
9	34	2/28/06 E-mail, Nee to Swanson	117
10		CC: Lamore	
11	35	3/1/06 E-mail Exchange, McCarthy	118
12		and Swanson	
13	36	12/19/05 E-mail, Buchmueller to	120
14		McCarthy	
15	37	3/19/06 E-mail Exchange, S. Madoff	121
16		and McCarthy	
17	38	4/17/06 E-mail, S. Madoff to McCarthy	122
18	39	4/21/06 E-mail, Sadowski to McCarthy	123
19	40	4/6/06 E-mail Exchange, Sadowski and	128
20		McCarthy	
21	41	4/23/06 E-mail, Swanson to McCarthy	131
22	42	4/27/06 E-mail Exchange, McCarthy and	133
23		Swanson	
24			
25			

## P R O C E E D I N G S

1  
2 MR. KOTZ: On the record. Okay, we are on the  
3 record at 9:45 a.m. on April 27, 2009, United States  
4 Securities and Exchange Commission.

5 I'm going to swear you in, if that's all right?  
6 Could you please raise your right hand?  
7 Whereupon,

8 JOHN ANDREW MCCARTHY

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

11 MR. KOTZ: Okay. Could you state and spell your  
12 full name for the record?

13 THE WITNESS: John Andrew McCarthy, J-o-h-n  
14 A-n-d-r-e-w M-c-C-a-r-t-h-y.

15 MR. KOTZ: Okay. Mr. McCarthy, my name is David  
16 Kotz; I'm the Inspector General of the United States  
17 Securities and Exchange Commission. And I have my colleagues  
18 here, Heidi Steiber and Chris Wilson and you have your  
19 attorney here, Mr. Ty Cobb. This is an investigation by the  
20 Office of Inspector General, case number OIG-509.

21 I'm going to ask you certain questions and you'll  
22 have to provide answers under oath. The court reporter will  
23 record and later transcribe everything that is said.  
24 Therefore, please provide verbal answers to the questions, a  
25 nod of the head or another non-verbal response won't be able

1 to be picked up by the court reporter.

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

10 Do you understand those instructions?

11 THE WITNESS: Yes.

12 MR. KOTZ: Okay. I'm going to give you the  
13 standard perjury language. As you can see, your response to  
14 statements given today are provided after you've sworn an  
15 oath and will be taken down verbatim by the court reporter.

16 This is an official U.S. government law enforcement  
17 investigation. The claims asserted in this case are serious  
18 ones. It is very important that you tell me everything you  
19 know about the matter at hand and are completely forthcoming  
20 and truthful with me.

21 I'm formally advising you that your testimony today  
22 is subject to the laws of perjury. Providing false or  
23 misleading testimony under oath is a very serious offence.  
24 If the evidence shows the testimony you have given is false,  
25 we may refer it as appropriate.

1           A     I went to the University of Michigan,  
2 undergraduate. Got a master's from the London School of  
3 Economics and then went to law school at the University of  
4 Maryland.

5           Q     Okay. What year did you get your degree from  
6 Michigan?

7           A     1986.

8           Q     And then what year did you go to the London School  
9 of Economics?

10          A     The following two years, so 1989 I got the degree.

11          Q     Okay. And then where did you go to law school?  
12 Maryland?

13          A     University of Maryland.

14          Q     And what year did you graduate law school?

15          A     '92.

16          Q     Okay. What was your first job after graduating law  
17 school?

18          A     Clerk for the --

19                 (Interruption to proceedings.)

20          Q     How long did you do that for?

21          A     For the year clerkship.

22          Q     Okay. What kind of things did you do for them?

23          A     I wrote draft opinions for the judge.

24          Q     Okay. Anything to do with securities issues?

25          A     No, it was mainly -- criminal law was the vast

1 majority of my opinions.

2 Q What about in 1993, what did you do after the  
3 clerkship?

4 A Then I joined the SEC.

5 Q Okay. What was your first position for the SEC?

6 A I worked as a staff attorney in the Division of  
7 Market Regulation.

8 Q What was the -- was that -- what other division was  
9 it in? Office of Compliance, Inspections Examinations? I'm  
10 sorry, what was the division that it was in?

11 A The -- I first worked at the SEC for the Division  
12 of Market Regulation.

13 Q Oh, okay. I'm sorry, Division of Market  
14 Regulation. For how long did you work for the Division of  
15 Market Regulation?

16 A The -- that -- the area I worked in was made into a  
17 separate office and I can't recall the date, '95 I think. So  
18 I stayed in the same position but there was a change in --  
19 so, where I worked was turned into a separate office, the  
20 Office of Compliance Inspections and Examinations.

21 Q Okay. All right. So officially, you didn't start  
22 working for OC until '95 but your office --

23 A And the dates I'm not exactly sure, but yeah, until  
24 it was first formed by Chairman Levitt at the time.

25 Q Okay. And who was your initial supervisor?

1           A     When I first started at the SEC my branch chief was  
2 named [REDACTED].

3           Q     And then do you get a promotion over time at the  
4 SEC?

5           A     Yes.

6           Q     When was that?

7           A     I became a branch chief, again, the dates aren't --  
8 I think in '96, something along those lines.

9           Q     Okay. What kind of duties did you have as a staff  
10 attorney?

11          A     I was in the office of SRO Inspections, so I was  
12 responsible for, you know, conducting inspections as part of  
13 a inspection team.

14          Q     And then as a branch chief, what were your duties  
15 there?

16          A     Basically, managing the inspection, managing a team  
17 of attorneys to conduct the inspections.

18          Q     How long did you serve as a branch chief?

19          A     Again, I'm not exactly sure, but approximately four  
20 years maybe.

21          Q     Okay. So until approximately 2000?

22          A     Yes.

23          Q     Okay. And then in 2000 you left the SEC; is that  
24 right?

25          A     I think it was '99, yeah.

1 Q How come you left the SEC?

2 A My former boss, Personal Privacy, was Personal Privacy of  
3 Knight Securities and he asked me to join him in his firm.

4 Q What was your position at Knight Securities?

5 A Regulatory counsel.

6 Q How long did you work at Knight Securities for?

7 A A short period of time, maybe three, four months.

8 Q What kind of things did you do there at Knight  
9 Securities?

10 A Drafted -- you know, again, in the short period of  
11 time, drafted comment letters and worked on, you know,  
12 regulatory issues for the firm.

13 Q And then after three or four months with Knight  
14 Securities you went back to the SEC?

15 A Correct.

16 Q How come you left Knight Securities after only a  
17 few months?

18 A Yes, my wife still worked here, still worked at the  
19 SEC so we -- I was commuting by train up to New Jersey every  
20 week and so there's personal -- that was not working out as  
21 intended. There was a lot of stress on, you know, on me.  
22 And then -- so, that's one -- part of -- one part of the  
23 reason, the other reason was I didn't like the job itself.

24 I thought Knight Securities, you know, was growing  
25 very fast and so I then, you know, also talked to Lori about,

1 you know, getting a promotion at the SEC. So I thought that  
2 was very desirable for me, vis-...-vis my job at Knight  
3 Securities.

4 Q That was Lori Richards?

5 A Yes, ma'am -- yes, sir.

6 Q Okay.

7 A Ma'am for Lori.

8 Q Now, do you recall that at some point in time there  
9 was an action brought by the SEC against Knight Securities?

10 A Yes.

11 Q Okay. What was that about?

12 A It was a, you know, fundamentally at its core, best  
13 execution issue.

14 Q Were there allegations that Knight Security was  
15 engaged in front-running?

16 A Yes.

17 Q Okay. And was that going on while you were at  
18 Knight Securities or --

19 A I don't know. It could have been when I was there  
20 also.

21 Q Okay. But the allegations didn't surface until  
22 after you left Knight Securities; is that right?

23 A Correct.

24 Q Okay.

25 MS. STEIBER: Did your departure from Knight

1 Securities have anything to do with front-running or --  
2 execution violations?

3 THE WITNESS: No.

4 BY MR. KOTZ:

5 Q All right, so you came back in about 2000 you think  
6 to the SEC?

7 A I -- this was probably -- I remember July '99 if my  
8 memory serves me correct.

9 Q Okay, July 1999. And what was your position when  
10 you returned to the SEC?

11 A I think I was an assistant director.

12 Q Okay. Who was your supervisor at that point?

13 A Maryann Gajella. No, I'm sorry, I'm confused when  
14 I was promoted to associate director and assistant director.  
15 I'm not sure if that's correct.

16 Q Okay.

17 A I thought when I came back from Knight Securities I  
18 was, at some point, promoted to associate director.

19 Q Okay. And then subsequently you were --

20 A Before that I was assistant director.

21 Q Okay.

22 A I apologize.

23 Q All right. What about in the period of time 2003  
24 to 2006, what was your position at that time?

25 A Branch chief. And then at some point I was a -- I

1 was promoted to assistant director and then I worked --

2 MR. COBB: No, he said 2000.

3 BY MR. KOTZ:

4 Q 2003 through --

5 A Oh, I'm sorry. I'm in '93. 2003 to '06 I would  
6 have been associate director.

7 Q Okay. So in that period of time, 2003 to 2006,  
8 where you were associate director, who did you report to  
9 then?

10 A To Lori Richards.

11 Q Okay. And what were your duties as associate  
12 director?

13 A I was responsible for the -- running the SRO  
14 Inspection Program.

15 Q Okay. How many people did you have under you at  
16 that point?

17 A It varied over time, but maybe as little as 10 to  
18 15, to as many as 25 or so.

19 Q Okay. Who were your direct reports when you were  
20 associate director?

21 A I think assistant directors would have been Eric  
22 Swanson and Mark Donohue.

23 Q Okay. So in that 2003 to 2006 period you  
24 supervised both Eric Swanson and Mark Donohue?

25 A Directly, yes.

1 Q Okay. And then how long did you serve as an  
2 associate director?

3 A Until I left the Commission two-and-a-half years  
4 ago.

5 Q Okay. So that was --

6 A Back in --

7 Q -- 2007?

8 A 7th November 2007.

9 Q How come you left the Commission that time?

10 A Mainly because there was a good opportunity  
11 presented to me and it was about that point in my career that  
12 I felt it was a good time to leave the Commission.

13 Q And what's the position that you left to go to?

14 A I went to the head of compliance at where I am now,  
15 Getgo LLC.

16 Q And you remain in that position today?

17 A Correct.

18 Q Okay. When did you first hear of Bernard Madoff or  
19 Madoff Securities?

20 A Early on in my career.

21 Q So that would be in the '90's you think?

22 A Early, yeah. Mid-90's, like --

23 Q Okay. What did you hear of Bernie Madoff or Madoff  
24 Securities in the mid-90's?

25 A I conducted an exam of the market-making unit.

1 Q Okay. In the mid-90's?

2 A I think -- again, I don't recall the exact dates  
3 but it was a limit order display exam.

4 Q Okay, yeah. We'll get to the specific exams in a  
5 minutes, but was -- so that was the first time you heard of  
6 Bernie Madoff, when you conducted the exam? You weren't  
7 aware of them before that?

8 A Not that, I mean, the first time I now can  
9 recollect learning about Madoff was when we -- when I was  
10 asked to do an exam.

11 Q And what was Bernie Madoff's reputation at that  
12 time?

13 A I -- the firm's -- I didn't know what his  
14 reputation was --

15 Q Okay.

16 A -- I knew what the firm's reputation was.

17 Q What was the firm's reputation?

18 A That it was one of the, if not the largest third  
19 market-maker in which they executed over the -- you know,  
20 listed securities over-the-counter. And they had a very good  
21 reputation in terms of their execution quality of retail  
22 customer orders.

23 Q Okay. And did you ever -- were you ever aware of  
24 Bernie Madoff's involvement with SEC functions or SEC  
25 matters?

1 MR. COBB: Ever or about that time?

2 BY MR. KOTZ:

3 Q In that time.

4 A The time -- again, as a junior attorney I was not  
5 familiar with that, no.

6 Q You ever hear that Bernie Madoff had a friendship  
7 with former Chairman Arthur Levitt?

8 A Now or at that time?

9 Q At that time.

10 A I wasn't aware of that, no.

11 Q Okay. Are you aware of that now?

12 A Yes.

13 Q Meaning now within the last year?

14 A Recently, yeah, now within the last -- just from  
15 what I've read the --

16 Q Okay, subsequent to December 2008 you mean?

17 A Correct.

18 Q Okay. Have you ever met Bernie Madoff in person?

19 A Yes.

20 Q How many times?

21 A Maybe three.

22 Q Okay. And that's --

23 A I'm guessing, but that's approximately what I  
24 think.

25 Q What were those times?

1           A     During the exams and then at -- he was at Eric  
2 Swanson's wedding, would be the last time.

3           Q     Okay.

4           MS. STEIBER: Did you see him at SEC events?

5           THE WITNESS: I don't recall.

6           BY MR. KOTZ:

7           Q     Okay, well we'll get into the exams, but did you  
8 have a conversation with him at Eric Swanson's wedding?

9           A     I didn't -- no, I did not speak with him.

10          Q     Okay. So other than through the exams, the only  
11 time you met Bernie Madoff was at the wedding and you didn't  
12 speak to him at the wedding?

13          A     Well, met, I guess I didn't meet him, but he was --  
14 the only time I saw him would have been at the exams and at  
15 the wedding.

16          Q     Okay.

17          MS. STEIBER: Did you receive any personal phone  
18 calls from him that were not exam-related?

19          THE WITNESS: No, not that I recall.

20          BY MR. KOTZ:

21          Q     Okay. Let's talk about policies in OC for a  
22 minute. Were there formal policies and procedures for  
23 handling tips or complaints when you were in OC?

24          A     Formal policies?

25          Q     Yes.

1           A     I would have -- I wouldn't be aware of formal  
2 policies.

3           Q     Wouldn't be aware?

4           A     Right.

5           Q     Why wouldn't you be aware of them?

6           A     I mean there were -- I don't recall like a written  
7 policy on how to handle them.

8           Q     Okay. So you were not aware of any formal policies  
9 about how to handle complaints --

10          A     Yeah, I'm -- how were you -- formal like written  
11 policies in a manual or something like that, I'm not aware of  
12 those.

13          Q     There were informal policies?

14          A     There would be -- if I got a tip or complaint I  
15 would handle them then probably, depending on what the tip or  
16 complaint was and -- certain way to make sure that they were  
17 handled appropriately.

18          Q     So what was that way?

19          A     I would -- if it made sense to conduct an  
20 examination given what the facts, I would have then  
21 assigned -- I would assign -- I would ask someone to, you  
22 know, basically -- up an exam or inspection.

23          Q     Okay. But would you log somewhere, anywhere, that  
24 you got a tip or complaint?

25          A     Not that I recall, no.

1 Q And how would you decide whether there was  
2 information that would necessitate doing an examination?

3 A Again, if the complaint seemed -- I guess, things  
4 like the credibility of it, whether it was in my jurisdiction  
5 as it were, those would be the main factors.

6 Q Okay. And were there times where you would refer  
7 the information or complaint to the enforcement division?

8 A I don't recall doing that.

9 Q Okay. Would there be situations that if you got a  
10 complaint that you would feel that enforcement should be  
11 provided a copy of the complaint or would your decision be  
12 either to do an examination or not?

13 A Yeah, I don't recall getting the complaint, the tip  
14 or complaint that if I didn't follow up in my program that it  
15 made sense to forward it on to someone else.

16 Q So if the complaint was credible and had  
17 allegations of potential violations of securities laws you  
18 would decide to do an examination or inspection?

19 A If it was within -- my jurisdiction, yes.

20 Q Okay. Did you receive tips or complaints yourself,  
21 personally, while you were at OC?

22 A I'm thinking I -- nothing comes to mind that I can  
23 recall.

24 Q Okay. But you received them from others; is that  
25 right?

1 A I'm sorry, I'm --

2 Q You would receive tips or complaints from other  
3 people?

4 A You mean within the building?

5 Q Yeah, within OC.

6 A Yeah, that was probably -- yes, I do recall several  
7 instances of that.

8 Q Okay. And who would they come from? Would they  
9 come from Lori Richards?

10 A I think it depends.

11 Q Okay. Do you remember any tips coming to you from  
12 Lori Richards?

13 A Yes.

14 Q Okay.

15 BY MS. STEIBER:

16 Q How many tips or complaints did you receive from  
17 any source during your years at OC?

18 A You know, I can only recall, right now, two.

19 Q And as an associate director --

20 A But again, you'd have to define what exactly a tip  
21 or complaint is, but I only recall two that come to mind, but  
22 my guess is there were probably more.

23 Q And as an associate director, how many tips or  
24 complaints did OC receive per month, approximately?

25 A I don't know. I mean, you know, there was a

1 hotline that I'm aware of and things like that that other  
2 people within OC managed. So I assume that tips or  
3 complaints within my jurisdiction would flow to me from that  
4 source would be probably the main source of that I would have  
5 been aware of.

6 Q From this hotline? And what would the hotline do  
7 with the tips or complaints?

8 A I assume that there was -- if it made sense for my  
9 jurisdiction to follow up then they -- I assume they would  
10 have alerted me.

11 Q I'm just wondering if there's a database or  
12 something that you're aware of that the hotline kept.

13 A I would assume they tracked it but I'm not aware of  
14 that.

15 Q Okay.

16 BY MR. KOTZ:

17 Q What is a cause examination?

18 A It -- there -- it would be an out-of-cycle exam  
19 that for some reason made sense, you know, they had some  
20 cause to do it out of cycle or not within the routine  
21 inspection process.

22 Q So if you got a tip -- and you said depending on  
23 the tip if it's credible and within your jurisdiction you  
24 would have an exam or inspection be done, would you at that  
25 point do that kind of an examination, a cause examination?

1           A     In our vernacular that would probably -- I would --  
2 probably would refer to that as a cause exam, yes.

3           Q     Now you mentioned your jurisdiction. What was your  
4 jurisdiction?

5           A     Primary jurisdiction was inspection of  
6 self-regulatory organizations. And then as part of that  
7 program we primary -- we were focused on surveillance  
8 investigatory and enforcement programs at the SRMs and then  
9 as part of the surveillance programs, a lot of times you'd  
10 have to conduct trading exams because the records wouldn't  
11 exist solely at the SRMs. Then we also started, as we got  
12 more staff to do trading examinations of broker-dealers or  
13 for brokers or specialists, things like that.

14          Q     Okay. So if a tip or complaint came in and it  
15 there was determination that you would do a cause  
16 examination, who would determine what the focus of the  
17 examination would be?

18          A     Typically being -- if I was referred the tip I  
19 would decide what the focus would be, maybe in consultation  
20 with my assistant directors.

21          Q     Okay. But in -- the final decision would be made  
22 by you as associate director?

23          A     Yeah, but it's very -- I have a very collaborative  
24 approach, it wasn't dictatorial.

25          Q     Okay. How long would it typically take from the

1 time OC receives a credible tip or complaint to begin a cause  
2 examination?

3 A Depending on staffing issues it -- the planning  
4 memos should start, you know, more or less immediately,  
5 within the next, you know, within a week or so or two at the  
6 most.

7 Q So if it took several months for the planning memo  
8 to start, would you consider that too long of a period of  
9 time?

10 A No, I mean, again, it depends on what's starting  
11 the -- when it was written or finished, but I would assume  
12 that they would start thinking about how to do the exam and  
13 staffing it and things like that.

14 Q Right away?

15 A Well, you know, within a matter of weeks, yes.

16 Q Okay. All right, let's talk -- you mentioned some  
17 of the different matters you were involved in related to  
18 Madoff Securities, so let me ask you about that. We can show  
19 you a document, this is marked as Exhibit 2 and this is a  
20 chart of Madoff exams. It says at the top, "Appendix A, List  
21 of Examinations and Staff." Yeah, this was created by OC.

22 (SEC Exhibit No. 2 was marked  
23 for identification.)

24 A Created by OC in response to --

25 Q A request to identify the different exams that

1 related to Madoff in connection with the investigation, but  
2 not during his time there.

3 MR. COBB: So reasonably created as a summary?

4 MS. STEIBER: Right.

5 BY MR. KOTZ:

6 Q Right. Correct. So if you see under 1998  
7 inspection of eight third-market firms, HQ, 1997 to 1998, you  
8 see your name appears there along with several others?

9 A Yes.

10 Q Do you recall that inspection, the 1998 inspection  
11 of eight third-market firms?

12 A Yes, I do, vaguely.

13 Q What do you recall about it?

14 A I'm sorry, am I on the right one?

15 MR. COBB: I don't know. I was just trying to read  
16 both pages.

17 THE WITNESS: Around 1998?

18 MR. COBB: 1998 on this one though, right?

19 MR. KOTZ: Right.

20 MR. COBB: Trifocals just killing me.

21 THE WITNESS: I recall we were -- I recall the  
22 issue of best execution was front and center in terms of  
23 the -- either recent adoption or the process to adopt the  
24 order-handling rules, so we followed up on the issues that  
25 are -- the focus of the order-handling rules such as best

1 execution and limit order display. That's what I recall.

2 BY MR. KOTZ:

3 Q Do you recall if there was any conclusion that the  
4 inspection came to about Madoff?

5 A I don't recall.

6 Q At the next one on this, Exhibit 2, right above it  
7 it says 1999 limit order display review, HQ.

8 A Yes.

9 Q And your name is listed on that one as well.  
10 And -- so you were involved in that examination?

11 A Yes.

12 Q Okay. So what do you recall about that one?

13 A That I recall more clearly, we did a limit order  
14 display exam of Madoff.

15 Q What does that mean, "limit order display exam of  
16 Madoff?"

17 A In '97 the SEC passed a rule requiring  
18 market-makers and specialists to display customer limit  
19 orders that are better than the NBBO and so once the rule --  
20 so we were basically making sure that people were complying  
21 with the new rules -- or Madoff was complying with the new  
22 rules.

23 Q And what was your involvement with that  
24 examination?

25 A I think I was a branch chief on that exam.



1 Q Okay. Do you recall that at that time OC  
2 recommended a deficiency letter be sent out?

3 A I recall that we sent out a deficiency letter.

4 Q Okay.

5 BY MS. STEIBER:

6 Q Do your recall that OC took the position that an  
7 enforcement action should be brought in that case?

8 A I recall that we felt that it -- the violations  
9 were material enough to refer to enforcement, yes.

10 Q And do you recall how enforcement reacted to your  
11 recommendation that an action should be brought?

12 A I don't recall.

13 Q Do your recall who made the decision that a  
14 deficiency letter would be the appropriate result to the  
15 exam?

16 A I don't recall. What I recall is that we sent a  
17 deficiency letter and also referred to enforcement. I don't  
18 recall that that was the final result.

19 BY MR. KOTZ:

20 Q So did you know if an enforcement action was ever  
21 brought against Madoff?

22 A I do not know. But obviously, I'm guessing that  
23 nothing was ever brought, but I don't know.

24 Q Now, on 3b, the letter is referenced to Shana  
25 Madoff Skoller, do you know if you met Shana Madoff at that

1 time?

2 A During the exam, the onsite portion, I don't  
3 recall, but it's possible.

4 Q Do you recall who the contact person on that exam  
5 was from Madoff?

6 A It was always Peter Madoff.

7 Q Did you have any contact with anyone else at Madoff  
8 Securities during this 1999 limit order display exam?

9 A I mean, I would say 99 percent of the  
10 communications were with Peter Madoff. I think other people  
11 might have said hello or something to that regard, but he was  
12 the point person.

13 Q Okay. Did you have any contact with Bernie Madoff  
14 in connection with the 1999 limit order display exam?

15 A I think he said hello to the team, if I recall  
16 correctly.

17 Q But that was it?

18 A That's all I recall.

19 Q Do you recall why you referred these reports to  
20 enforcement for further action?

21 A I don't recall.

22 Q Okay. Going back to the chart, the next matter  
23 listed was the 2003 QQQ trading review and your name is  
24 associated with that as well. Do you remember that exam?

25 A Just a very vague recollection.

1           Q     Okay. Let me show you a document, perhaps that  
2 will help. This is a memorandum from you, Eric Swanson, Matt  
3 Daugherty to Lori Richards, dated March 3, 2003, and we're  
4 going to mark this as Exhibit 4. Thank you. And if you can  
5 see attached to Exhibit 4 is an April 8, 2003 document  
6 request from Eric Swanson to Peter Madoff.

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

9                                 (The witness examined the documents.)

10           MR. COBB: And the record will reflect the act of  
11 describing documents. Is there a question about --

12           MR. KOTZ: Well, I just wanted --

13           MR. COBB: Does he recall it?

14           MR. KOTZ: Well, I just wanted him to read it  
15 first.

16           MR. COBB: Sure.

17           MR. KOTZ: And then I'm going to show him another  
18 document.

19           THE WITNESS: How much you -- I can read it  
20 carefully, I mean, do you want me to spend a lot of time? I  
21 mean, I'm not --

22           MR. KOTZ: Right. Well, just -- you don't have to  
23 read it and analyze it, just kind of read it over and then  
24 I'm going to show you another document and ask you a question  
25 about it.

1 THE WITNESS: Okay, sure.

2 MR. KOTZ: Okay? This document you can mark --

3 MR. COBB: Read it over.

4 MR. KOTZ: -- as Exhibit 5. This is an e-mail from

5 [REDACTED] OCIE Staff Attorney

to Eric Swanson with an attached memorandum from

6 [REDACTED] OCIE Staff Attorney

to Tom Eidt dated September 12, 2003, Re: Madoff

7 Activity on QQQ.

8 (SEC Exhibit No. 5 was marked for  
9 identification.)

10 (Witness examined the documents.)

11 THE WITNESS: You said this is an e-mail or --

12 MR. KOTZ: No, it's a -- yeah, there's an e-mail  
13 dated Monday, October 20, 2002 --

14 THE WITNESS: Oh, with the attachment?

15 MR. KOTZ: -- attachment.

16 MR. COBB: And the attachment is the memo?

17 MS. STEIBER: Yes, the attachment is the memo.

18 MR. KOTZ: And I'll just point you out to  
19 something, you can continue to read it afterward if you want.

20 THE WITNESS: Okay.

21 BY MR. KOTZ:

22 [REDACTED] OCIE Staff Attorney

23 Q In the memo from [REDACTED] to Tom Eidt it says, "We  
24 decided to investigate trading in the security based on the  
25 fact that the market for QQQ is often locked or crossed. We  
have suspected that when one of these types of markets -- for

1 security, that market-makers and specialists were violating  
2 their duty at best execution on customer trades." My  
3 question is is that your recollection of what led to this  
4 examination?

5 A Yes, that's a fair sentence.

6 Q And what was your role in this triple Q  
7 examination?

8 A I was apprised that, if I recall, that -- I often  
9 encouraged my staff to come up with ideas, I think Brad came  
10 up with this, I'm not sure. And so my role would have simply  
11 said, "Sure, go ahead and do that."

12 Q Okay. And then while the examination was ongoing  
13 did you have any role?

14 A Not that I recall, no.

15 Q Did you have any contacts with anyone at Madoff  
16 Securities during this triple Q examination?

17 A Not that I recall.

18 Q Okay.

19 BY MS. STEIBER:

20 Q As the associate director with examinations going  
21 on under you, would you monitor the exams to make sure that  
22 they were completed? Would you follow up on the  
23 examinations?

24 A Rely on Eric and Mark to basically manage the  
25 day-to-day part of the exams.

1 Q And then at some point did -- like monthly, would  
2 they come and report to you the exam findings or did you  
3 track it on a spreadsheet?

4 A I think we tracked all of our exams and inspections  
5 in a, you know, I think -- I don't know what -- in an Excel  
6 type database or something like that.

7 Q Did you put all of those exams in the Starz  
8 database? Is that what you're referring to?

9 A I think we had, in-office -- the office had a  
10 track -- you know, a summary of all the open inspections and  
11 exams and I would get copies of that.

12 Q And would you follow up to make sure that they were  
13 being worked on or --

14 A I mean, where I felt -- I would ask questions and  
15 see how things were going, sure.

16 MR. KOTZ: Okay, show him the e-mail.

17 MR. COBB: Are you done with five or --

18 MS. STEIBER: Yes.

19 BY MR. KOTZ:

20 Q Yeah. Okay, we're going to mark the next document  
21 as Exhibit 6. And this is an e-mail from OCIE Staff Attorney to Matt  
22 Daugherty 8/27/2003, 5:26 p.m. And here it references Matt,  
23 "We had a second call with Madoff and I think we understand  
24 these trades a lot better." Do you know if you were on the  
25 phone with any of the calls with Madoff in connection with

1 this exam?

2 (SEC Exhibit No. 6 was marked for  
3 identification.)

4 A I don't recall that I was, no.

5 Q Okay. Do you know when he says, "We had a second  
6 call with Madoff," who he's referring to? Is that Peter  
7 Madoff?

8 A I don't know.

9 Q Okay, let me show you another document. This is an  
10 e-mail from you to Eric Swanson dated 10/29/2003, 3:52 p.m.  
11 We're going to mark this as Exhibit 7. And this document  
12 you -- it's entitled, "Call Madoff Re: Fleet ASAP." Do you  
13 remember why you were suggesting to Eric Swanson that he call  
14 Madoff?

15 (SEC Exhibit No. 7 was marked for  
16 identification.)

17 A '03, I don't recollect why.

18 Q Do you know what Fleet is? Re: Fleet ASAP?

19 A Fleet is a broker-dealer in -- I'm pretty sure.

20 Q So is it a different broker-dealer? Is it related  
21 to Madoff?

22 A Right, it's a separate broker-dealer.

23 Q Okay. So do you have any idea why you would be  
24 suggesting call Madoff Re: Fleet?

25 A I could guess, but maybe Fleet was sending Madoff

1 orders, their retail order -- something to do with that.

2 Q Okay.

3 A But that's a guess.

4 Q Okay. I understand that. Mark the next document  
5 as Exhibit 8. And this is a memorandum from OCIE Staff Attorney to  
6 Eric Swanson dated November 10, 2003, Re: Examination of  
7 Madoff, Execution --

8 (SEC Exhibit No. 8 was marked for  
9 identification.)

10 MR. COBB: You want this back? I'm trying to --

11 BY MR. KOTZ:

12 Q Okay. If you look in the second paragraph it says,  
13 "The staff has found numerous inconsistent instances of bad  
14 executions by MADF, Bernard L. Madoff Investment Securities  
15 LLC."

16 A I'm sorry, I don't see where you're reading.

17 Q I'm sorry, second paragraph.

18 A Yeah.

19 Q See where it says --

20 A "The staff has found --" Okay.

21 Q "-- resulting in some loss to the customers  
22 involved." So "Staff has found numerous inconsistent  
23 instances of bad executions by Madoff resulting in some loss  
24 to the customers involved." So you recall that that was the  
25 conclusion of the triple Q exam? And then if you can -- if

1 you also look at the --

2 A I don't recall that.

3 Q Okay.

4 MR. COBB: Go through it and look at the  
5 appendices.

6 THE WITNESS: Okay.

7 BY MR. KOTZ:

8 Q If you could take a look at the third page in the  
9 document which has conclusion. You see where it says, "The  
10 staff believes that there's a best execution problem with  
11 Madoff. The staff further believes that Madoff and its  
12 broker customers have thus far failed to adequately monitor  
13 this behavior. Based on these conclusions, the staff  
14 recommend that a deficiency letter be sent out outlining the  
15 problem areas, as well as recommending that Madoff execute  
16 customer orders at ECNs when it is able to do so rather than  
17 proprietorially taking that price, all that is getting the  
18 customer a worse IT price."

19 Do you recall that in the triple Q exam, staff  
20 concluded that there was a best execution problem with Madoff  
21 in general?

22 A I mean, obviously I see it now, but I don't recall,  
23 you know, obviously this is refreshing -- this I agree with,  
24 it says what it says.

25 Q Okay. And do you recall that the staff recommended

1 that a deficiency letter be sent out?

2 A I mean, without seeing this I wouldn't have  
3 recalled it, but yes, I can see that they -- that's what they  
4 recommended.

5 Q Okay. And the first page of this document, Exhibit  
6 8, it says at the top, BE-Final. Do you see that?

7 A Yes.

8 Q Do you know what that would refer to?

9 A Probably best ex-final, would be my guess. I'm  
10 guessing.

11 Q Is that your handwriting?

12 A It's no my handwriting, no.

13 Q Do you know if a deficiency letter was ever sent  
14 out in connection with the triple Q exam?

15 A I don't recall.

16 Q Who would have made the decision to -- whether or  
17 not to send out a deficiency letter?

18 A Deficiency letter would typically be done by --  
19 recommended by the branch chief and the assistant director.

20 Q So the --

21 A And then they would probably cc me or alert me  
22 depending on how serious it was.

23 Q Okay. But who would actually make the decision as  
24 to whether to send it, not recommend that it be sent but  
25 decide that they would send it?

1           A     I mean, it's -- depending on how serious it is,  
2     it's something that a branch chief could do, but they would  
3     certainly alert their assistant -- the assistant director --

4           Q     Okay.

5           A     -- or cc them.

6           Q     Now, if a deficiency letter was sent out, would it  
7     be in the work papers?

8           A     It should be in the work papers, yes.

9           Q     Okay. Now, we had testimony from OCIE Staff Attorney and I  
10    wanted to tell you what he said and give -- ask you to  
11    comment about this. He indicated to us that he didn't  
12    believe a deficiency letter was ever sent out and when asked  
13    why he said, "I remember seeing this memo -- sending this  
14    memo, and frankly, there were a lot of projects at the time  
15    that would kind of die off. I mean, you know, you do some  
16    initial review and then you go up the chain and I think the  
17    superiors had determined, "Well, I got other things to worry  
18    about." Those old projects just kind of languished and I had  
19    a lot of projects like that."

20                   And then when asked specifically about this project  
21    he said, "There was never any further direction. It was a  
22    pretty common occurrence." Is that an accurate reflection of  
23    what happened in OC at that time?

24           A     I would disagree with that characterization.

25           Q     Okay, in what way?

1           A     Well, I mean, he's -- that's his perception of what  
2 was going on at the time, but -- above him, but I would  
3 disagree with that description.

4           Q     So what was your perception of what went on and  
5 that you would disagree?

6           A     Well, if he felt things died there might have been  
7 reasons why they died and maybe he wasn't aware of.

8           Q     Okay.

9           MS. STEIBER: Is that normal practice, not telling  
10 the staff that performs an examination of the reasons why  
11 their recommendation wasn't accepted?

12           THE WITNESS: I would tell people who worked for me  
13 exactly what was going on.

14           MR. KOTZ: And you don't remember why there's at  
15 least no record, and according to  there was no  
16 deficiency letter sent out in the triple Q exam?

17           THE WITNESS: I don't remember why, no.

18           MR. COBB: Only for clarification, he doesn't know  
19 that there's no record.

20           MR. KOTZ: Right.

21           MR. COBB: Okay.

22           MS. STEIBER: But wouldn't you, as the associate  
23 director, keep track of what open projects there were and  
24 what conclusions each project had?

25           THE WITNESS: Yes.

1 MS. STEIBER: Where would you keep track of that?

2 THE WITNESS: Like I said, we had a -- Tina Berry  
3 was for the -- most of the years, responsible for keeping  
4 track of our open inspections.

5 MS. STEIBER: Okay, so --

6 THE WITNESS: And so --

7 MS. STEIBER: And so if I go to Tina Berry she  
8 should have a record of the inspections that were under you  
9 as associate director and their resolutions?

10 THE WITNESS: I think that's fair, yes.

11 BY MR. KOTZ:

12 Q So if we went to Tina Berry and/or reviewed the  
13 work files and found no evidence of deficiency letters, isn't  
14 it likely that a deficiency letter was never sent out?

15 A I mean, if you can't find one, I think that's a  
16 reasonable conclusion, yes.

17 Q Okay, next document. Okay, this next document is  
18 an article called "Don't Ask, Don't Tell, Bernie Madoff is so  
19 Secretive He Even Asks his Investors to Keep Mum," by Erin  
20 Arvedlund, 5/7/2001. A two-page document we're going to mark  
21 as Exhibit 9.

22 (SEC Exhibit No. 9 was marked for  
23 identification.)

24 MR. COBB: Read it --

25 (The witness examined the document.)

1 BY MR. KOTZ:

2 Q Okay, do you recall ever seeing this document  
3 before?

4 A I mean, I see it now but I don't recall, no.

5 Q Okay. Do you see where it says at the top, "John,  
6 she is very good. This is a great exam for us. Lori."

7 A Yes.

8 Q Do you think that refers to Lori talking to you?

9 A Yes.

10 Q And you see that this is dated 5/7/2001, and if you  
11 look in the bottom right-hand corner it has a date 5/15/2001.  
12 Do you know whether Lori Richards sent you this article in --  
13 sometime in May of 2001?

14 A I don't know.

15 Q Do you regularly read Barron's?

16 A No.

17 Q Okay. Do you consider it a reputable publication?

18 A Yes.

19 Q Other than recalling specifically this article  
20 right now, do you recall that Lori Richards sent you a copy  
21 of an article about Bernie Madoff and suggested that this  
22 would be a great exam?

23 A I mean, it looks like she did but I don't recall  
24 it.

25 Q Okay.

1 A And it's eight years ago, right?

2 Q I'm sorry?

3 A It's eight years ago, so it's a long time ago.

4 Q Let me ask you just about a couple of things in the  
5 article. The third paragraph down, you see it says, "But  
6 what few on the street know is that Bernie Madoff also  
7 manages more than 6 billion for wealthy individuals. That's  
8 enough to rank Madoff's operation among the world's five  
9 largest hedge funds according to a 2001 report in MarHedge, a  
10 trade publication."

11 Were you aware of the magnitude of Bernie Madoff's  
12 managing of money and the fact that he was a very, very,  
13 large hedge fund, enough to rank him among the world's five  
14 largest hedge funds in the early 2000's?

15 A Was I aware?

16 Q Yeah.

17 A Not -- no, and if I read this it would have been  
18 probably my first awareness of that business.

19 BY MS. STEIBER:

20 Q So if Lori sent you an article, do you think that  
21 you would have read it?

22 A I mean --

23 Q She sent you an article in 2001.

24 A Sure.

25 Q Do you think you would have read it?

1 A Typically I would have, but it's possible I didn't.

2 Q And if you read it in 2001 and you saw that Bernie  
3 Madoff manages more than \$6 billion for wealthy individuals,  
4 would that have seemed like a large amount of money at that  
5 time -- in that time period from 2001 to 2003?

6 A I would have -- yeah, I wasn't familiar with the  
7 hedge fund business, I wouldn't have known. I mean, I would  
8 have saw -- I would have saw they said the five biggest of  
9 the -- I would assume that that's what it would have been.

10 Q Well, you said in the mid-90's that you were  
11 familiar with Bernie Madoff as a market-maker. If you had  
12 read this in 2001 would it have surprised you that he's also  
13 supposedly managing money in the 6 billion range?

14 A That he also had a hedge fund business wouldn't  
15 have surprised me, no. I mean, I didn't -- I simply didn't  
16 know.

17 Q You had never heard of it before but it wouldn't  
18 have surprised you?

19 A I mean, firms have run different businesses.  
20 Obviously, I was focused on the trading business; if they had  
21 other ones I wasn't aware of that. And then, obviously, if I  
22 read this I would have been aware.

23 Q But you were just saying that you're not familiar  
24 with the hedge fund business, so at that point, when you have  
25 an article and -- that's been brought to your attention for a

1 great exam and some of the information you might not be  
2 familiar with, was there someone you would have gone to in OC  
3 so that they could explain it to you?

4 A If I felt a need that I needed to have it explained  
5 to me, yes, I would.

6 Q Okay, so if you read something and you didn't  
7 understand it, would you have felt a need to understand it?

8 A Well, this seems self -- I -- this seems self --  
9 you know, this seems -- it says what it says so I don't see  
10 why I would have asked someone to explain anything to me.

11 Q Okay. So you're unfamiliar with hedge funds, this  
12 is -- and that's not familiar to you and you might have a  
13 great exam but you would not have sought out any more  
14 information about the hedge funds mentioned in the article.  
15 Is that your testimony?

16 A I don't recall either one way or the other seeking  
17 out any other information.

18 Q Okay.

19 BY MR. KOTZ:

20 Q There's a reference in the sixth paragraph to  
21 Fairfield Greenwich. Do you see that? And Fairfield Century  
22 Limited?

23 A Yes.

24 Q And then, "Managed by Bernie Madoff, Fairfield  
25 Century has assets of 3.3 billion." Do you know if OC ever

1 examined any of the Madoff feeder funds like Fairfield?

2 A I do not know.

3 Q Okay.

4 BY MS. STEIBER:

5 Q Did you get a status on what other associate  
6 directors in OC -- what matters they were managing?

7 A I don't recall ever getting any --

8 Q You didn't have like --

9 A -- documents as to what they were doing.

10 Q Not documents, but would you get e-mail, like  
11 updates, showing you what everyone was working on?

12 A No, I don't recall that.

13 Q Did you have OC meetings --

14 A We had a staff meeting in which -- yes, in which  
15 the other associates would talk about, you know, their most  
16 significant projects. So yeah, is -- it was oral but, yeah.

17 Q So -- and you don't remember a hedge fund sweep  
18 that was -- of fund-to-funds that was performed in 2003?

19 A I don't recall, no.

20 BY MR. KOTZ:

21 Q Okay. So if you got an article from Lori Richards  
22 that said, "She's very good. This is a great exam for us,"  
23 what would you have done?

24 A I don't know what I did in this instance.

25 Q Okay, but in --



1 Q Okay. Do you have any recollection of why you  
2 might have forwarded this article to Eric Swanson two years  
3 later?

4 A Typically, I forward articles as an FYI or possibly  
5 for something for us to follow up on.

6 Q Okay. But you don't remember specifically  
7 forwarding this article or seeing this article?

8 A I don't recall, no.

9 BY MR. WILSON:

10 Q Do you recall why Tina Berry sent you these  
11 articles?

12 A I'm only guessing, I mean, because she knows that  
13 we've done exams on Madoff and we might find it interesting.

14 Q But you don't recall any type of conversation about  
15 that?

16 A With Tina?

17 Q Yes.

18 A I don't recall.

19 BY MR. KOTZ:

20 Q Okay, let's show you another document, we'll mark  
21 this Exhibit 11. This is an e-mail from [REDACTED] to  
22 Mavis Kelly dated Wednesday, May 21, 2003, 5:47 p.m. This is  
23 a two-page e-mail with several attachments.

24 (SEC Exhibit No. 11 was marked for  
25 identification.)

1 (The witness examined the document.)

2 MR. COBB: I'm sorry, Exhibit 11? Did we skip one  
3 or did I miss one?

4 MR. KOTZ: This is 10.

5 MR. COBB: Okay, I'm sorry. Thanks.

6 BY MR. KOTZ:

7 Q Have you ever seen this document before?

8 A I don't recall ever seeing this, no.

9 Q No? Do you know whether this document triggered a  
10 cause examination of Bernie Madoff?

11 A I don't know.

12 Q Do you know what did trigger the cause examination  
13 of Bernie Madoff in 2004?

14 A Which cause exam are you referring to?

15 Q The cause exam that Washington Headquarters worked  
16 on.

17 A The one that was within my group?

18 Q Yeah.

19 A I mean -- thought about it, I think it was the --  
20 an article that I was made aware of and I assume it's that  
21 article.

22 Q Okay. Let me show you another document. This is  
23 an e-mail from you to Lori Richards dated December 18, 2003,  
24 6:13 p.m. We're going to mark this as Exhibit 12. And in  
25 this article you say, "Lori, regarding tip IA/IC received

1 about Madoff, a compliance officer and an investment advisor  
2 notified Mavis that he was concerned about the returns  
3 Fairfield was posting." Then you say, "We would like to  
4 contact this compliance officer and get a better  
5 understanding of how the strategy is supposed to work."

6 (SEC Exhibit No. 12a was marked for  
7 identification.)

8 MS. STEIBER: So do you now recall that you were  
9 familiar with this tip from [REDACTED] to Mavis? And  
10 remembering that you're under oath.

11 THE WITNESS: I remember I'm under oath all the  
12 time. Again, I'm -- I can see what's said in this e-mail  
13 and -- so, I'm a little confused by the e-mail because it  
14 seems to be from me but it seems to be written from Eric.

15 MS. STEIBER: Like you had forward -- maybe had  
16 forwarded an e-mail that you were writing with Eric to Lori?

17 THE WITNESS: Yeah, but this doesn't look like a  
18 forward, I -- in terms of the e-mail traffic.

19 MS. STEIBER: Did you and Eric work closely  
20 together?

21 THE WITNESS: Yes.

22 MS. STEIBER: So it was possible that you could  
23 work on an e-mail together and send it to Lori?

24 THE WITNESS: Yes.

25 MR. COBB: Yes, it's possible?

1 THE WITNESS: It's possible, yes.

2 BY MR. KOTZ:

3 Q Okay, I'm going to show you another document.

4 We'll mark this as Exhibit 12. This is an e-mail from you,  
5 Eric Swanson, Mark Donohue, Genevieve Walker, Jackie Wood,  
6 to Lori Richards, dated December 2003.

7 If you see in this document, which is a planning  
8 memorandum, in the background section it says, "The staff  
9 received -- recently received information from an outside  
10 source alleging that Bernard L. Madoff, the principal of  
11 Bernard L. Madoff Investment Securities LLC, Madoff  
12 Securities, a leading market-maker in -- securities has been  
13 front-running violations."

14 Do you see that?

15 (SEC Exhibit No. 12b was marked for  
16 identification.)

17 A Yes.

18 Q Okay. Were you aware that there was an examination  
19 in your group of Bernard Madoff of alleged front-running  
20 violations?

21 A Yes.

22 Q Okay. Do you know what the outside source referred  
23 to in this memorandum was?

24 A I don't -- I can only guess that the article but  
25 I'm not sure.

1 Q You think the article was an outside source and not  
2 the [REDACTED] complaint that was sent in May of 2003  
3 and that is referred to in the December 2003 e-mail?

4 A I don't know, but it makes sense, yes.

5 Q So -- but you do remember that a cause exam was  
6 initiated of Bernard L. Madoff and Madoff Securities; is that  
7 right?

8 A Yes.

9 Q Okay. And --

10 A By my group.

11 Q By your group. And what was your involvement in  
12 that cause exam?

13 A I instructed my staff to do the cause exam.

14 Q Why did you instruct your staff to do the cause  
15 exam?

16 A My recollection is that Lori -- Lori and I had a  
17 discussion, it could be e-mails, I'm not -- I can't remember  
18 exactly, that there's allegations that Madoff may be taking  
19 advantage of his retail order flow.

20 Q Where did those allegations come from?

21 A My recollection is they were from the media, the --  
22 a newspaper article, or Barron's would be my guess.

23 Q Okay. And in that conversation did you talk about  
24 the fact that you had received a complaint from an entity  
25 like Mr. [REDACTED] and then actually followed up with him on

1 several occasions to get information about his allegations  
2 about Bernie Madoff?

3 A I don't recall. I don't recall his allegations.

4 Q And how is the decision made as to what the cause  
5 examination of Madoff would focus on?

6 A Well, my group was responsible for trading exams,  
7 so we focused on, in essence, the trading aspect of the  
8 allegation.

9 Q What was the trading aspect of the allegation?

10 A Well, whether the retail order flow could be, you  
11 know, based on the best execution exam, could be harmed by if  
12 information was passed to other entities.

13 Q What about allegations that were raised by [REDACTED]  
14 [REDACTED] that seemed to indicate Mr. Madoff was not actually  
15 trading at all?

16 A I don't recall those allegations.

17 Q Okay. So is it possible that you made this  
18 decision with Lori as to how to focus the cause exam of  
19 Madoff without being aware of allegations that came in at the  
20 same time by [REDACTED]?

21 A I'm trying to understand your question.

22 Q Well, is it possible that you made the decision to  
23 focus the cause exam of Bernie Madoff on front-running  
24 allegations without being aware that [REDACTED] had  
25 come in and brought allegations to OC that were somewhat

1 different in nature?

2 A Is it possible that I -- I focused on the  
3 front-running aspect of the exam, yes.

4 Q Because you hadn't seen the fact that a complaint  
5 had come in around the same time period that your staff was  
6 working on -- your staff was aware of.

7 MR. COBB: I think that misstates his testimony, he  
8 said he --

9 MR. KOTZ: I'm asking the question.

10 MR. COBB: -- just didn't recall.

11 MR. KOTZ: But I'm asking the question.

12 MR. COBB: Well, you said he said, that was my  
13 objection.

14 BY MR. KOTZ:

15 Q All right, I'll re-ask the question. You made the  
16 decision to -- was it you who made the decision to focus on  
17 front-running in this cause exam?

18 A Look I -- as I recall I got a -- I had a discussion  
19 with Lori saying there was allegations of front-running of  
20 Madoff's retail -- so that's what I -- so therefore, I  
21 focused on that.

22 Q So it was you who made the decision to focus on  
23 front-running?

24 A Was it me?

25 Q Yeah, you.

1           A     That's all I recall that I focused on because that  
2 was -- it could be mainly because that was the area of  
3 expertise for my crew.

4           Q     Okay, but I'm trying to establish who made the  
5 decision to focus on front-running. Was that a decision made  
6 by you?

7           A     I don't recall focusing on front-running, I recall  
8 talking to Lori that there's allegations of front-running so  
9 I said that -- so I said that would be an area that we could  
10 do an exam.

11          Q     Okay, so who made the decision in the Madoff exam  
12 that the exam would look at front-running?

13          A     I made -- I decided the scope of the exam for Mark  
14 Donohue.

15          Q     Okay. And you're not aware that at the same time  
16 period your staff had received a complaint from [REDACTED]  
17 [REDACTED] that made different allegations; is that right?

18          A     I don't recall ever seeing that, no.

19          Q     Let me ask you a couple questions about Exhibit 11,  
20 which is [REDACTED] complaint. I'll just ask you if  
21 this -- the issues at all were ever raised at that time  
22 period. One of the things that [REDACTED] says is -- and you  
23 can look kind of middle way down the page it says, "According  
24 to BMS," do you see that?

25          A     Yes.

1 Q "The options are traded with a number of traders  
2 and crossed on the CBOE." Do you know what the CBOE is?

3 A Yes.

4 Q What is it?

5 A It's an options exchange in Chicago.

6 Q Okay. And you knew what that was at the time?

7 A Yes.

8 Q Okay. Then it says, "With an 8 to 10 billion size  
9 you must see the volume, but unfortunately you don't. We  
10 actually checked with some of the largest brokers, UBS,  
11 Merrill, et cetera, which told us they never traded with them  
12 OEX options. The question is do they really implement the  
13 full strategy?"

14 Do you recall at any time in making a determination  
15 about what the scope of the Madoff exam would be, this issue  
16 about whether Madoff was actually implementing his trading  
17 strategy for options --

18 A I don't recall.

19 Q You don't recall this issue being something that  
20 was discussed or what don't you recall?

21 A I don't recall it being discussed, I don't recall  
22 being aware of it.

23 Q I'm sorry?

24 A I don't recall being aware of it at this time.

25 Q Okay. All right, another question from this

1 document to ask whether you recall being aware of -- you see  
2 where it says, "Accounts are typically in cash at month end?"

3 A Yes.

4 Q Do -- first of all, do you know what is -- is there  
5 any relevance to that, why accounts would be typically in  
6 cash at month end?

7 A I don't know.

8 Q Would there be any securities regulation  
9 requirements that Madoff could avoid by going to cash at the  
10 end of every month?

11 A There could be, I'm not familiar at the top of my  
12 head what those are.

13 Q Okay. And then further down on this Exhibit 11,  
14 [REDACTED] complaint, it says, "There are no third-party  
15 brokers involved in the process. The auditor of the firm is  
16 a related party to the principal." Is that -- would that be  
17 a concern?

18 A Now, obviously, it would be.

19 Q But it wouldn't at that time.

20 A I wasn't aware of this at the -- I can't recall  
21 being aware of this at the time, so --

22 Q Okay, but would it be a concern? Before whatever  
23 happened in December 2008, would that be a concern?

24 A It would be, certainly noteworthy, something that  
25 should be followed up, perhaps.

1 Q And do you know if in connection with the cause  
2 exam of Madoff if anyone did follow up about this issue of  
3 whether there are no third-party brokers involved or anything  
4 about the auditor of the firm? Was that ever followed up?

5 A Not that I recall.

6 Q Okay. And then earlier in that same document,  
7 Exhibit 11, it says, "The firm does not charge any management  
8 or performance fees to these accounts, but rather brokerage  
9 commissions. We estimate the amount of money management --  
10 strategy by BMS, somewhere between USD 8 to 10 billion. Is  
11 that something that would be a concern?

12 A A concern of me at the time, I don't know.

13 Q But I mean, the fact that the firm does not charge  
14 any management or performance fees, is that -- would that be  
15 odd?

16 A Obviously, now having read a lot of stuff in the  
17 media, I understand that that is odd. At the time I might  
18 not have been -- I was not familiar with this part of the  
19 business.

20 Q Okay. And then if you see in Exhibit 11 there are  
21 several attachments. One attachment is another article in  
22 MarHedge entitled, "Madoff Tops Charts, Skeptics Ask How."  
23 Do you see that article?

24 A Yes.

25 Q Do you recall that? Have you ever seen this

1 article before?

2 A I don't recall seeing this article.

3 Q At the time you -- at the time that you made the  
4 determination to have the staff undertake the Madoff cause  
5 exam, were you familiar with the basic characteristics of a  
6 Ponzi scheme?

7 A I would say I -- in the colloquial sense, yeah, I  
8 would understand what Ponzi scheme is.

9 Q Couple of things that were referenced in the  
10 article I wanted to ask you about. If you could see on page  
11 2 of the article, the second page of the article --

12 MR. COBB: Hedge article?

13 BY MR. KOTZ:

14 Q Sorry, yes, MarHedge article, attached to the  
15 [REDACTED] complaint. It says, "Skeptics who express a mixture  
16 of amazement, fascination, and curiosity about the program  
17 wonder first about the relative complete lack of volatility  
18 in the reported monthly returns. Among other things they  
19 also marvel at the seemingly astounding ability to time the  
20 market to move to cash in the underlying securities before  
21 market conditions turn negative and the related ability to  
22 buy and sell the underlying stocks without noticeably  
23 affecting the market."

24 Do you remember that that was an issue that was  
25 discussed or was thought about when you were going to

1 undertake the cause examination of Madoff?

2 A I don't recall that being an issue, no.

3 Q Okay. Do you recall anything about the lack of  
4 volatility in Madoff's returns being an issue?

5 A No.

6 Q Do you know if anybody ever contacted the  
7 individual who wrote this article, Michael Ocrant, in  
8 connection with the Madoff examination?

9 A I did not contact him, I don't know if anyone else  
10 did.

11 Q Okay. You think if you had been aware of this  
12 [REDACTED] complaint the examination's scope might  
13 have been more than just front-running?

14 A It's -- my area was on trading so it's -- it could  
15 have very well been the same, same scope.

16 Q But if you got a complaint that alleged other  
17 areas, for example, that he may not have been trading at all,  
18 you would have done the same type of exam?

19 A It's a hypothetical, I don't know what I would have  
20 done. But certainly, reasonably would have followed up with  
21 it whether it was my group or another -- another group did  
22 it.

23 Q Okay, so even if your group --

24 A There's jurisdiction issues, so I was careful, you  
25 know, we were careful not to do IASE exams -- not careful but

1 simply, you know, we would make sure that the appropriate  
2 area of the OC did the exam. So I probably would have worked  
3 with other areas.

4 BY MS. STEIBER:

5 Q Well, let me ask you about that. You wouldn't have  
6 worked with other areas, is that what you just said? Sorry.

7 A I didn't say that, no.

8 Q Okay. Well, what I don't understand is if you're  
9 going in for an examination and you said your expertise is  
10 trading, and you're the associate director and you're putting  
11 together a team; could you have pulled from the Investment  
12 Advisor part of OC to get an examiner on the team who is more  
13 familiar with hedge fund trading?

14 A I could have done that or could have separated the  
15 issues and had -- you know, have the IC group do the -- do  
16 that exam separately.

17 Q But if you have a registered broker-dealer but not  
18 registered hedge fund, so you would -- you could create the  
19 team though that goes in, because of the BD registration, any  
20 way you want, right? You could have somebody with investor  
21 advisor experience, someone with broker-dealer trading  
22 experience, someone with other types of experience; you don't  
23 have to just have people from the Market Oversight or SRO  
24 group, correct?

25 A There's no requirement or guideline that would --

1 that, correct.

2 BY MR. KOTZ:

3 Q Do you recall what time period it took from the  
4 time that you instructed the staff to initiate the Madoff  
5 exam as to when the planning memo began to be prepared and  
6 the exam was initiated?

7 A I saw the -- if that's a planning memo, but I don't  
8 recall.

9 Q You don't recall it being a particularly long  
10 period of time, many months, before the planning memo was  
11 ever started?

12 A I don't recall that, no.

13 Q Okay. But if the office received a complaint from  
14 [REDACTED] in May of 2003 and the planning memo  
15 didn't -- wasn't drafted until late December 2003, do you  
16 think that was too long a period of time to follow up on a  
17 complaint?

18 A It would depend on a variety of factors that --

19 Q What would those factors be?

20 A Well, resources, how, you know, how credible the  
21 complaint was, et cetera, things like that. But obviously,  
22 the decision was made to do the exam, so typically I would  
23 expect once a decision has been made for the planning memo to  
24 be, you know, done in a relatively short period of time.

25 Q Okay. And that would be a lot shorter than seven

1 months, would you say?

2 A What I'm talking about -- from what -- you know,  
3 when the decision was made to do the exam to start the  
4 planning memo.

5 Q Okay. What about the time period from when the  
6 complaint came in until the decision was made to do the exam,  
7 could that take months?

8 A It could, but I would expect it to, you know, to be  
9 done, you know, in less than months.

10 Q Okay. Why don't we go to the planning memo. Okay,  
11 going back to Exhibit 12, the planning memo. You see in this  
12 memo, which is from you and several others to Lori Richards,  
13 under "Course of Action," number 3 on the first page? See,  
14 it says, "The staff intends to send a letter to NASD  
15 requesting execution data for Madoff Securities for the time  
16 period of January 1, 2001 through December 31, 2002."

17 Why would staff send a letter to NASD requesting  
18 execution data?

19 A Because it's often easier to get trade data  
20 directly from the NASD and it has a certain level of  
21 reliability.

22 Q And do you know who made the decision to -- that it  
23 says that "The staff intends to send a letter to the NASD  
24 requesting execution data?"

25 A I'm pretty sure it was -- my understanding was Mark

1 Donohue was running the exam so I would expect it to be him.

2 Q And do you know whether the staff ever did send a  
3 letter to the NASD requesting execution data for Madoff  
4 Securities?

5 A I don't know if they actually did it but I would  
6 assume they would have.

7 BY MS. STEIBER:

8 Q is it a standard step in a front-running exam to  
9 get trade data from the NASD or from an exchange?

10 A It makes a lot of sense, yes. But I mean,  
11 front-running exams are relatively -- you know, there's -- I  
12 don't recall ever being involved in that many of them, so  
13 whether there's a standard step probably is overstated.

14 Q So it wouldn't be unusual --

15 A No.

16 Q -- to get the trade data and it would be --

17 MR. KOTZ: And appropriate --

18 MS. STEIBER: -- good practice.

19 THE WITNESS: It makes sense to get it, yeah.

20 BY MR. KOTZ:

21 Q Okay, I'm going to show you a document. It's a  
22 draft letter to the NASD from Eric Swanson, December 17,  
23 2003. And we're going to mark this as Exhibit 13. Would  
24 this letter be requesting the execution data from NASD?

25 (SEC Exhibit No. 13 was marked for

1 identification.)

2 A It looks like it, yes.

3 Q And you don't know if this letter was ever sent  
4 out?

5 A This is obviously -- not the signed copy on  
6 letterhead, so --

7 Q Okay. You mentioned earlier that you remembered  
8 two tips that came in while you were in OC. Any of them  
9 relate to Madoff?

10 A That would be this as a tip, yes. I would view the  
11 Madoff -- my recollection is Madoff was -- I would qualify as  
12 a tip.

13 Q Okay, so one of them is the one we're discussing  
14 now and what is the other one?

15 A Again, I use a tip, the Knight Securities case was  
16 started based upon an allegation by an employee there.

17 Q An allegation by --

18 A By an employee at Knight. So I would view that as  
19 a tip as such.

20 MS. STEIBER: Did that come in to you?

21 THE WITNESS: I think -- now that I think about it  
22 more, I think it was part of a arbitration that we became  
23 aware of, so --

24 BY MR. KOTZ:

25 Q Okay, I'll show you another document, mark this as

1 Exhibit 14. This is an e-mail from Lori Richards to you,  
2 12/10/2003, 7:13 p.m. responding to an e-mail from you to  
3 Lori.

4 (SEC Exhibit No. 14 was marked for  
5 identification.)

6 MR. COBB: What's the number?

7 THE WITNESS: 14.

8 BY MR. KOTZ:

9 Q Do you recall anything about an informant on Canary  
10 that also had information about Madoff?

11 A I guess my recollection of why I started the Madoff  
12 exam was based on that tip, so that makes sense.

13 Q A tip from the outside, because previously you  
14 talked about an article?

15 A Right, but again, when I was -- in my recollection  
16 of my discussions with Lori, you know, again, it's a long  
17 time ago, my recollection was it was a tip or somehow she  
18 became aware of the possibility of front-running. So whether  
19 she got it from the article or tip, you know, this seems more  
20 consistent with my recollection.

21 Q Okay. What -- you say in this e-mail in response  
22 to Lori, "How can I get trading records if they're hedge  
23 fund? Can we get a formal order?" Why would you want to get  
24 a formal order? What kind of formal order would you want to  
25 get?

1           A     Again, my guess -- again, this is -- a guess, is  
2     that I felt we couldn't get their -- I felt they probably  
3     weren't registered or I knew that somehow and we couldn't  
4     get -- we would -- couldn't get their records through the  
5     exam process.

6                     BY MS. STEIBER:

7           Q     So why didn't you seek a formal order?

8           A     My understanding is that Madoff agreed to give us  
9     trading records voluntarily, so -- would have needed -- if  
10    they agree to give you the records then it doesn't  
11    necessitate to get a subpoena requiring them to do it.

12          Q     So if you have a registered broker, a  
13    broker-dealer, you can have any of their trading records,  
14    correct --

15          A     Right.

16          Q     -- without needing a formal order? You didn't need  
17    him to agree, he would have to provide all of his trading  
18    records to you.

19          A     Right, but my understanding at the time, obviously  
20    I understand more now, but was that Madoff had a hedge fund,  
21    so that's probably why I said that. But yes, you're right,  
22    all of the records -- broker-dealer records -- would not have  
23    been why I would have said that.

24          Q     Okay.

25                     BY MR. KOTZ:

1 Q And then you say in this, "I will draft a letter to  
2 get that info tomorrow a.m. Okay with you?" Lori says yes.  
3 Do you know if a letter was ever drafted?

4 A Usually when I tell Lori I would do something I  
5 would have instructed people to do it, so -- but I can't  
6 recall whether a letter was actually drafted.

7 BY MS. STEIBER:

8 Q And could you walk us through what the purpose of  
9 drafting a letter would be based on your e-mail? You know,  
10 describe what types of data you were going to request.

11 A Well, I'd say if I can -- again, my -- I don't  
12 recall this but do you want me to run through the e-mail what  
13 I think? "If not, I can fairly easily figure out where their  
14 executing their hedge fund trades and get the trading info  
15 from their executing brokers." So what I meant there was I  
16 would have, hopefully, somehow figured out where the hedge  
17 fund was executing its orders and then send broker-dealer  
18 requests to those entities.

19 Q And then you make --

20 A Also, they were probably executing orders. And  
21 then I say, "But they may be executing their orders  
22 in-house," meaning that I could probably just get -- if  
23 that's the case then I could ask their broker-dealer for the  
24 trading records.

25 Q So if they're executing them in-house you would

1 have just gone directly to them to get the trading records?

2 A To --

3 Q You wouldn't go anywhere else? If they're  
4 executing in-house where would you go to get the trading  
5 records?

6 A To the -- to Madoff broker-dealer.

7 Q Is it -- I want to be clear because I'm confused as  
8 to your going to be investigating potential fraud of a  
9 registrant and you would go to that registrant to request the  
10 trading records?

11 A I was investigating potential front-running so you  
12 would go to the -- you would get trading records from that  
13 entity, yes.

14 Q Is there anywhere else that you could have gone?  
15 If you know that they're executing them in-house and you  
16 don't want to go to the registrant because you want to have  
17 objective third-party records, is there anywhere you could go  
18 to get those trading records?

19 A Like I said previously, you could go to the NASD to  
20 get audit trail data. Whether there's enough information in  
21 that audit trail for these purposes, it depends. Audit trail  
22 would simply say -- would simply have the executing  
23 broker-dealer and the time and the price and the date, so  
24 whether it was enough specificity to -- for the purpose of  
25 the exam you'd have to -- typically you would have to then

1 get more specificity at the broker-dealer level.

2 Q At the broker-dealer level. Is there -- okay, you  
3 go to the NASD, you look at their audit trail and you say you  
4 don't think it's sufficient. Can you go back to the NASD and  
5 ask for additional information?

6 A Well, for instance, if you get -- NASD would say,  
7 we -- you know, Madoff bought 1000 shares of Microsoft, so if  
8 you want to know that. You would not be able to determine  
9 whether it was 1000 shares from the hedge fund or from a  
10 retail client. So that information you -- that degree of  
11 specificity would have, in my understanding, would only be at  
12 the broker-dealer level.

13 Q The broker-dealer. There'd be no -- so you would  
14 have absolutely nowhere you could go objective third-party to  
15 find out if -- who -- for whom the -- or for whom the trades  
16 were executed?

17 A Right, so to know which customer to -- which  
18 customer the trade was for you would have to go to the  
19 broker-dealer level. And again, typically these are omnibus  
20 accounts and the like, so all -- the only information you  
21 would have would be Merrill Lynch or Madoff by 1000 of a  
22 Microsoft and that's what would occur -- and the time and  
23 sales, of course. That's the information that would be at  
24 the SRO level. If you wanted for -- depending on what you  
25 were doing for the exam, if you wanted -- if you needed more

1 specificity you would have to go to the broker-dealer.

2 Q Well, so do you think that a good practice would be  
3 to get the records from the NASD and then also get them from  
4 the broker-dealer so that you could compare what you're  
5 provided?

6 A I mean, often we would just -- often I would just  
7 get the information directly from the broker-dealer. I,  
8 obviously, know what you're asking, you're -- if I thought  
9 there could be -- if I thought the records were -- any reason  
10 think the records were not accurate, yes, I would then want  
11 to verify with the NASD.

12 BY MR. KOTZ:

13 Q Okay, I'm going to show you another document. I'll  
14 mark it as Exhibit 15. This is the e-mail from Lori to you,  
15 it's a reply to the e-mail from you to Lori. The e-mail from  
16 Lori to you is dated 12/18/2003, 4:25 p.m.

17 And then I'm going to show you another document.  
18 It is Lori Richards e-mail 12/18/2003, it's marked 16. And  
19 then the next document we're going to mark -- okay. The  
20 e-mail from Lori Richards to you dated 12/18/2003, 4:25 p.m.  
21 is Exhibit 15. And then the second document is from Mark  
22 Donohue to Matt Daugherty, 12/19/2003, 2:13 p.m. and that's  
23 going to be Exhibit 16.

24 See, it references in both these e-mails are two  
25 calls put in to Madoff by you and Lori Richards. Do you

1 recall having a conversation with Madoff at that time?

2 (SEC Exhibit Nos. 15 and 16 were  
3 marked for identification.)

4 A Yes.

5 Q Okay. And who was on that call, which Madoff was  
6 it?

7 A Bernie and possibly Peter, but I don't recall.

8 Q Okay. And what did -- what happened in that phone  
9 call? What was said?

10 A The purpose of the call, as I recollect, I'm not  
11 looking at the e-mail so it's just as I recollect now, were  
12 basically to verify that he had a hedge fund, to make sure we  
13 understood generally what the -- yeah, I wasn't aware of  
14 hedge funds so I asked questions about what that looked like,  
15 where the trades were executed, things like that. And to  
16 basically make sure that we could -- understood enough so  
17 that we could then start conducting the exam.

18 Q So you had substantive questions you asked Bernie  
19 Madoff in that call about his operations?

20 A Subsequent to the call?

21 Q Substantive questions in that phone call about  
22 Bernie Madoff's operations that were asked?

23 A These were just general questions.

24 MS. STEIBER: But they were general substantive  
25 questions, right? They're not just "I'm going to start an

1 exam next week," they're -- you were asking probing questions  
2 about his operations?

3 THE WITNESS: I think it was just to get an -- I  
4 think my main objective was to make sure that we could send a  
5 document request letter that made sense. It's common  
6 practice to call a firm to make sure, "Hey, you're a market  
7 maker, you know, you execute over-the-counter we're going to  
8 send you over-the-counter document request letters." So it's  
9 very, for me, a common practice.

10 MR. KOTZ: But it was an informational phone call?  
11 You were trying to seek information about his operation?

12 THE WITNESS: And to make sure -- and then --  
13 right, in -- basically to make sure we could then construct a  
14 rational document request letter.

15 MS. STEIBER: Is it usual for you, as the associate  
16 director, to call the registrant before starting an exam?

17 THE WITNESS: Typically, for SRO inspections, yes  
18 it would be me depending on -- yeah, specialists exams it  
19 would be me. It would be kind of how important I thought the  
20 exam was.

21 MS. STEIBER: Wasn't it unusual though, you had  
22 Lori also on the phone call with you? Did you think it was a  
23 really important exam or --

24 THE WITNESS: No, that's not -- I mean, it's  
25 happened before but it's not, certainly not normal.

1 BY MR. KOTZ:

2 Q It's certainly not normal?

3 A It's not normal for Lori to be on a call with me,  
4 no. But it's -- I'm sure it's happened many times in the  
5 past.

6 Q And so why would there be a particular case where  
7 Lori would be on the call as well?

8 A My recollection in this instance was that she got  
9 the, you know, got the tip and I said, "Well, why don't we  
10 call together," or something like that.

11 Q You didn't take any notes of that phone call?

12 A I don't recall taking notes.

13 Q Did Lori Richards say anything to you in particular  
14 about Bernie Madoff in connection with that phone call or  
15 otherwise, in connection with the exam, that would affect  
16 scope or focus of your exam?

17 A I mean, she may have said something. I mean --  
18 said -- helped me -- you know, obviously we would have had a  
19 discussion as to what the scope of the exam would be, but --

20 Q Did she ever indicate to you to back off from any  
21 aspect of examining Madoff's operations?

22 A That's definitely -- I feel strongly that that  
23 would be highly unlikely that she would ever do that and she  
24 did not do that here. I don't recall her ever saying back  
25 off anything in my whole career, so --

1 Q Okay. All right, the next document we're going to  
2 mark as Exhibit 17. This is an e-mail dated 1/29 --

3 MR. COBB: Are you done with these?

4 MR. KOTZ: Yeah.

5 MR. COBB: I'm sorry, it goes so fast. I'm  
6 notorious here for screwing up the exhibits.

7 MS. STEIBER: Hold on. Could we go off the record  
8 for a second?

9 MR. KOTZ: Yeah, why don't we go off the record.

10 (A brief recess was taken.)

11 MR. KOTZ: Okay, now we're going to -- we're going  
12 to mark the document as Exhibit 17, different document than I  
13 previously indicated. This is a -- yeah, this is a  
14 compilation of the OC Headquarters' first Madoff document  
15 request, draft 1 through 7, and a final document request.  
16 And then in addition we're going to put into evidence as  
17 Exhibit 18 a letter from Eric Swanson to Peter Madoff dated  
18 January 6, 2004.

19 (SEC Exhibit Nos. 17 and 18 were  
20 marked for identification.)

21 MR. COBB: Just on -- so the 17 is a series of  
22 drafts that ultimately culminates in 18, is that --

23 MS. STEIBER: Yes.

24 MR. COBB: Okay, thanks.

25 BY MR. KOTZ:

1 Q So do you remember sending out a document request  
2 to Bernie Madoff?

3 A I don't recall specifically, but --

4 Q Do you recall generally sending a document request  
5 as part of the cause exam?

6 A Yes.

7 Q Okay. And do you recall what kind of documents you  
8 were seeking to obtain in that document request?

9 A I don't recall specifically, but it would have been  
10 records to -- consistent with doing the front-running exam.

11 MS. STEIBER: And what were those records  
12 consistent with doing the front-running exam?

13 THE WITNESS: The records that they're laid out in  
14 the letter.

15 MR. KOTZ: Okay.

16 MS. STEIBER: If you were doing a front-running  
17 exam and you were going to make a letter, without looking at  
18 what you have, what would be the documents that you would  
19 want requested? You talked before about audit trail data,  
20 would that be one of the things that you would want?

21 THE WITNESS: I would certainly want sample trades  
22 from the retailers and sample trades from wherever we thought  
23 the proprietary trades were being executed at.

24 MS. STEIBER: Okay, would there be anything else  
25 you would want?

1 THE WITNESS: That would be the -- those trading  
2 records would be the core of the examination. I suppose  
3 you'd want WSPs and things of that nature that are typical to  
4 what --

5 MS. STEIBER: What are WSPs?

6 THE WITNESS: Written Supervisory Procedures. And  
7 the main issue here would be Chinese Walls, to ensure that  
8 order information doesn't flow to a --

9 MS. STEIBER: Anything else you would want?

10 THE WITNESS: That's -- that would be the heart of  
11 the exam from my perspective. You can -- you need that  
12 trading information to see in --

13 MR. KOTZ: Okay. Yeah, if you look at the third  
14 draft, F3 in that document --

15 MS. STEIBER: See the e-mail to you?

16 BY MR. KOTZ:

17 Q In Exhibit 17, the third draft, there's an e-mail  
18 from Mark Donohue to you and Eric Swanson dated 12/24/2003,  
19 4:03 p.m. "Attached is the latest version of the Madoff  
20 document request letter." Do you see that?

21 A Mm-hmm.

22 Q And the next page, do you see the number 1 on the  
23 draft document request letter?

24 A Mm-hmm.

25 Q What type of information was being sought in this

1 draft under number 1?

2 A So what type of information? It looks like --

3 Q Yeah, why would you request the daily profit and  
4 loss statements and daily commission revenues?

5 A I'm a strong believer that we should make sure we  
6 see where the -- on any exam -- where the firm's making money  
7 because that's often a -- of where there's possible  
8 irregularities. If they're losing money then it would  
9 probably be something that would be less interesting than if  
10 they're making.

11 Q Why would you request specifically daily profit and  
12 loss statements or daily commission revenues?

13 A I figure that's -- I don't know.

14 MS. STEIBER: Well that's not audit trail data, is  
15 it?

16 THE WITNESS: No.

17 BY MR. KOTZ:

18 Q Okay. And then if you look on the second page of  
19 this document it says, "Describe in detail the hedging model  
20 or investment strategy identified as the split-strike forward  
21 conversion in a telephone conversation between Lori Richards,  
22 John McCarthy and Bernie Madoff on December 19, 2003." Do  
23 you see that?

24 A Yes.

25 Q Okay. And then the next one, it says, "Identify

1 the four hedge funds discussed in the telephone conversation  
2 between Lori Richards, John McCarthy and Bernard Madoff on  
3 December 19, 2003." Do you see that?

4 A Yes.

5 Q Okay. Then if you look at Exhibit 18, the final  
6 version of the document request, you see that it asks for  
7 monthly profit and loss statements by security and monthly  
8 commission revenues, not daily. Do you have any idea why you  
9 would have asked for monthly when the draft said daily?

10 A Why the change? I don't know.

11 Q Okay. And if you look at paragraph two on Exhibit  
12 18, the final draft, the next page there, it leaves out any  
13 reference to a telephone conversation between Lori Richards,  
14 John McCarthy and Bernie Madoff on December 19, 2003, both in  
15 two and in three. Do you see -- do you have any idea why  
16 it -- that reference to a telephone conversation would be in  
17 the draft but not in the final?

18 A Why they took it out, I don't know. I don't recall  
19 being part of the drafting process.

20 Q Okay, you don't recall being part of the drafting  
21 process? Okay, if you look at the fifth tab in Exhibit 17  
22 you see there's an e-mail, "John and Eric attached to a  
23 document request with the revisions we just discussed." See?  
24 I mean, doesn't it seem as though you were part of the review  
25 process for this document request?

1           A     That would suggest that I discussed something with  
2 Mark, yes.

3           Q     But a minute ago you said you weren't.

4           MR. COBB:  No, he didn't.  He said he didn't  
5 recall.

6           MS. STEIBER:  No, he said he wasn't involved.

7           MR. COBB:  No, he said --

8           THE WITNESS:  I said I don't recall being a part of  
9 the draft.

10          MR. COBB:  You want to read it back or play it  
11 back?  He said he didn't recall being part of the drafting  
12 process.

13          MS. STEIBER:  Does this refresh your recollection  
14 then that you were involved in the drafting process?

15          THE WITNESS:  I mean, no, it doesn't but yes, I  
16 certainly think I -- this looks like a valid and true  
17 document.  This is -- it's starting to be a long time ago so  
18 I don't recall what -- you know, whether or not I was --

19          MS. STEIBER:  And in that final draft, Exhibit 18,  
20 is there a request for audit trail data in that final draft?  
21 That final letter that was sent out?

22          MR. COBB:  You want him to read the whole letter or  
23 you just want him --

24          MS. STEIBER:  He could read it and let me know if  
25 there's any request for audit trail data.

1 MR. COBB: Doesn't that speak for itself? We'll  
2 accept a representation, I mean --

3 MR. KOTZ: But we'd like him to answer the question  
4 if he wants to cooperate with us.

5 THE WITNESS: Looks like in this --

6 MR. COBB: Well, he has been totally cooperating,  
7 he's here voluntarily. You're asking him to read a letter  
8 and tell you whether there's something in there, the letter  
9 speaks for itself.

10 MR. KOTZ: Well, I'd like him to answer the  
11 question.

12 THE WITNESS: So in this letter it looks like  
13 there's not a request for audit trail data.

14 BY MR. KOTZ:

15 Q Okay, thank you for the response. We're going to  
16 show you the next document. Okay, we're going to mark as  
17 Exhibit 19 a letter from Bernard L. Madoff to SEC, Attention:  
18 Eric Swanson, dated January 16, 2004. Do you recall, as part  
19 of the cause exam, receiving a response from Bernie Madoff?

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

22 A I don't recall, no.

23 Q You don't recall that you ever got a response from  
24 Bernie Madoff?

25 A I didn't -- I would have expected a response but I

1 don't recall seeing it or reading it.

2 Q Okay. Do you think you would have seen it or read  
3 it or that would have been something that Eric Swanson would  
4 have done?

5 A -- this is a prosecution of the exam that would  
6 be -- something that I typically wouldn't be involved with.

7 Q Would or would not?

8 A Would not be typically involved with.

9 Q Okay. So do you recall though, in general, that  
10 there were requests made for documents to Madoff and do you  
11 recall whether he provided documents or what happened? What  
12 exactly do you recall about this exam?

13 A I don't recall being part of the day-to-day running  
14 of the exam.

15 Q But do you recall knowing -- learning anything  
16 about the exam, whether Madoff complied with the document  
17 requests or gave information that gave the staff concerns?

18 A I don't recall there ever being -- I don't recall  
19 Mark or Eric or anyone highlighting concerns about whether  
20 documents were being produced or not.

21 Q Do you recall Mark or Eric or anyone else  
22 highlighting any concerns about Madoff's responses or the  
23 exam?

24 A I don't recall, no.

25 Q So it was pretty -- kind of routine thing you had

1 allegations of front-running and what did you find in these?

2 A My recollection is when I asked Mark whether he was  
3 finding indicia of front-running that he said, no, he has not  
4 yet come up with any indicia of front running. But I don't  
5 recall when exactly I asked him and that would have been at  
6 some point during the examination --

7 Q And do you recall --

8 A -- several times.

9 Q I'm sorry, several times?

10 A Possibly, I might have asked Mark several times,  
11 "Hey, how's it going," or something like that. That's just  
12 my general recollection.

13 Q And do you recall whether there was a final  
14 determination of whether Bernie Madoff was front-running?

15 A My recollection is Mark said they did not find any  
16 indicia of front-running.

17 Q Okay. Did they do a closing report in connection  
18 with the exam?

19 A Not that I recall.

20 Q Why wouldn't they do a closing report? Was that  
21 normal to do a closing report? You would just end an exam  
22 with Mark saying he didn't think there was front-running and  
23 that would be the end of it?

24 A Typically, staff is supposed to -- when they finish  
25 an exam they're supposed to close it out and I think there

1 should have been a close-out memo is my understanding.

2 MS. STEIBER: Is there anything else you do at the  
3 end of an exam to show the -- for the registrant?

4 THE WITNESS: If there was -- typically there would  
5 be deficiencies of some nature so we would typically send a  
6 deficiency letter.

7 MS. STEIBER: What about a meeting with the  
8 registrant at the end?

9 THE WITNESS: I don't view that as a -- it could  
10 have happened on exams but I don't remember that being a  
11 typical thing to do.

12 MS. STEIBER: So it would be the closing report and  
13 the deficiency letter, it wouldn't be the two main indicia of  
14 the exam being closed?

15 THE WITNESS: That's fair, I guess.

16 BY MR. KOTZ:

17 Q Okay. And you don't remember anyone raising to you  
18 any concerns about Madoff's responses to the document  
19 requests? We've had significant testimony that the folks on  
20 the exam had very grave concerns about some of the things  
21 Madoff was saying. You don't remember anybody bringing that  
22 to your attention?

23 A I do not, no.

24 Q Were you hands-on as an associate director or -- it  
25 just -- I'm just trying to understand. Folks that worked on

1 the exam, through e-mails and testimony, have relayed that  
2 there were very significant concerns about what Madoff was  
3 providing them, what information he was giving them. And it  
4 seems as though they never, at least according to you, they  
5 never brought it to your attention. Do you think that was  
6 because you were hands-off with these exams or with this  
7 particular exam or is there any --

8 MR. COBB: I think his testimony was not that they  
9 never brought it to his attention, it was that he didn't  
10 recall anybody bringing it to his attention.

11 BY MR. KOTZ:

12 Q Okay. So it may have been that you had -- were  
13 actively involved in these discussions about concerns about  
14 Madoff's operations you just don't remember?

15 A It's very possible if they were serious that I was,  
16 you know, Mark or Eric came to me, but I don't recall those  
17 conversations.

18 Q Okay. I'm going to show you another document, I'm  
19 going to mark this as Exhibit 20. This is a -- notes of a  
20 telephone call with [REDACTED] dated 1/29/2004. If  
21 you see, there's references here to returns are too  
22 consistently high for this strategy, not doing that strategy  
23 because ops and training is not in high. He doesn't  
24 understand how he consistently makes money off this strategy,  
25 perhaps he doesn't really use the strategy. The volume of

1 options trading doesn't seem to be enough to protect the size  
2 of the equity trading." Do you remember a phone call back  
3 with the complainant [REDACTED]?

4 (SEC Exhibit No. 20 was marked for  
5 identification.)

6 A I don't recall -- I've never -- I don't recall ever  
7 recognizing the name or talking to him or her.

8 Q And you don't recall at any point anybody who  
9 worked on the exam come to you and say, "We talked to some  
10 individual and this is what he said?"

11 A I don't recall that.

12 Q And you don't recall any issues that were raised  
13 about how Madoff really doesn't use the strategy after the  
14 exam was initiated, when they did follow up to get  
15 information from the person who submitted the complaint?

16 A I mean, no, I don't -- my focus was on the issue of  
17 front-running. I don't recall that issue.

18 Q Right, if you look back at Exhibit 12b there's an  
19 e-mail from you to Lori Richards where it says, "We would  
20 like to contact this compliance officer and get a better  
21 understanding of how this strategy is supposed to work." So  
22 does that seem as though that you, or you and Eric, actually  
23 requested that they call [REDACTED] back?

24 A This certainly asks Lori. Yes, according to this  
25 e-mail that makes -- that seems a reasonable conclusion.

1 Q So looking at the -- we showed you [REDACTED]  
2 complaint and this information about the conversation with  
3 [REDACTED]. In retrospect, do you think it was a mistake to  
4 focus the scope of the exam on front-running when these other  
5 allegations were brought to the SEC's attention?

6 A For me?

7 Q Yes.

8 A It was not a mistake for me to focus on that, on  
9 front-running, because that's where my area, my team's area  
10 of expertise led.

11 Q So even if you get allegations of other matters  
12 that could be indicia of potentially, a Ponzi scheme, you  
13 would have focused only on front-running?

14 A Well, the other allegations, at least the way I  
15 read them, were more appropriate handled by the Investment  
16 Advisor Investment Company Group.

17 Q So do you think it was a mistake not to bring to  
18 anyone else's attention that there were allegations other  
19 than what you were looking at relating to Bernie Madoff?

20 A Was it a mistake not to bring it to other people's  
21 attention?

22 Q Right.

23 A It -- the other allegations should have been  
24 brought to other people's attention, yes.

25 Q And in fact, if those allegations had been brought

1 by you or your office to the other people's attention,  
2 perhaps Bernie Madoff's Ponzi scheme would have been  
3 uncovered. Okay?

4 A I don't know.

5 Q But if a complaint comes in and folks working for  
6 you are looking at the complaint and reacting to the  
7 complaint and you're referencing the complaint in an e-mail,  
8 wouldn't that be your responsibility, as the associate  
9 director, to make sure that all the allegations in the  
10 complaint are looked at, not just the front-running ones?

11 A I think my responsibility is to take information  
12 that's consistent with my program and to follow up on those  
13 complaints.

14 Q So you wouldn't have any responsibility if other  
15 issues were brought to your attention that were not within  
16 your program to relay that to anyone else?

17 A I think from the documents you provided me it -- I  
18 probably was comfortable that the IAIC group had the  
19 information that you're speaking of. So I think I -- so  
20 my -- if you're asking me what's reasonable and what's not, I  
21 think it's reasonable that I would have expected them to, if  
22 they were aware of the complaints, I would have expected them  
23 to follow up on those complaints that were consistent with  
24 their program.

25 BY MS. STEIBER:

1 Q So you're -- you'd be surprised we have testimony  
2 from the Investment Advisor Group that says when you were  
3 given this complaint, because it's a registered  
4 broker-dealer, that they -- you were expected to look at all  
5 of the allegations and they thought that you were conducting  
6 an exam that looked at all of the allegations?

7 A Would I be surprised if they said that?

8 Q Would you be surprised, do you think?

9 A I mean, if that's what they said, yeah, again, I'm  
10 just explaining to you what I would -- what my expectations  
11 would be. The broker-dealer issue that -- from this  
12 information is obviously -- front-running, so that's what I  
13 followed up on.

14 BY MR. KOTZ:

15 Q And you don't -- do you feel you have any  
16 responsibility to ensure that someone else, somewhere,  
17 follows up on other allegations that are brought to your  
18 staff's attention?

19 A Again, I took the information that I -- I took the  
20 information and started a front-running exam. If there are  
21 IASE issues embedded in the complaint then, you know, I would  
22 have expected them to follow up on those as appropriate.

23 Q Okay. I'll show you the next document. Mark it as  
24 Exhibit 21. This is a conference call with Madoff dated --  
25 or notes of a conference call with Madoff dated 2/4/04. Do

1 you recall if you participated in the conference call with  
2 Madoff in February 2004?

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

5 A February '04, I don't recall being part of a call,  
6 no.

7 Q I'm sorry?

8 A I don't recall being part of a conference call with  
9 Madoff.

10 Q At any point in time?

11 A No, I February of '04.

12 Q Okay.

13 A I said previously, yes, I was in a call with Lori  
14 with Madoff.

15 Q Okay, but that's the only call you remember being  
16 on with Madoff was the one with Lori?

17 A On the -- for this front-running exam that's the  
18 only one I recall, yes.

19 Q But with respect to another exam? The previous one  
20 we talked about?

21 A I said previous exams I could have been on calls  
22 with -- it probably would have been Peter on the other exams,  
23 yes.

24 Q But the point person on the cause exam in 2004,  
25 that was Bernie Madoff?



1 you know what that reference is "To get OATS from NASD?"

2 A OAT stands for order audit trail that NASD keeps.

3 Q And what would be the purpose of getting OATS from  
4 NASD?

5 A As I stated before, it would be a way to get trade  
6 data.

7 Q What about ACT? What does ACT refer to?

8 A OATS and ACT are basically audit trails. ACT is a  
9 subset of OATS. ACT would be -- is typically easier to get  
10 and quicker, historically. But ACT is time and sales and  
11 firm. So it would have the name of the firm, the time of the  
12 trade and the date and the price, things like that.

13 Q And do you know if the staff ever got OATS from  
14 NASD, or ACT?

15 A I don't know.

16 Q Okay. Do you recall any issues that arose about  
17 whether Madoff needed to register as an investment advisor in  
18 the course of the cause exam of Madoff?

19 A I don't recall that being an issue for my exam.

20 Q Okay. Now let me show you a document that may be  
21 able to refresh your recollection. I'm going to mark this as  
22 Exhibit 23, this is an e-mail from Genevieve Walker to  
23 Mark Donohue, Jacqueline Wood, February 4, 2004, 2:03 p.m.

24 I'm going to show you that document and then the  
25 second document we're going to mark as Exhibit 24, this is a

1 memorandum from Lori Richards, you, Eric Swanson, Mark  
2 Donohue and Matt Daugherty to Dan Gray dated March 11, 2004.

3 Does this refresh your recollection that the  
4 investment advisor issue actually was an issue in your exam?

5 (SEC Exhibit Nos. 23 and 24 were  
6 marked for identification.)

7 A Yes.

8 Q Okay. A minute ago you didn't think it was?

9 MR. COBB: He said he didn't recall.

10 THE WITNESS: I didn't recall it being an issue,  
11 no.

12 BY MR. KOTZ:

13 Q Okay. So now that you see the document, do you  
14 recall anything about this issue?

15 A I still don't recall, no. But obviously, yes,  
16 there's a draft document to Dan Gray.

17 Q And why would they -- why would you and Lori, Eric  
18 and Mark, Matt, send a memo to Dan Gray about this issue?  
19 Who is Dan Gray?

20 A I think he -- I think it's referring to Dan Gray in  
21 Market Regulation.

22 Q Why would the memo go to him about this issue?

23 A I haven't read the memo in detail but it --  
24 typically we'd send memos if we had questions of securities  
25 laws or interpretation or guidance, things like that.

1 Q And you don't remember whether this issue was  
2 resolved as to whether Bernie Madoff should register as an  
3 investment advisor at that time?

4 A Right, I don't recall.

5 MS. STEIBER: Could you review the last paragraph  
6 to see if it --

7 THE WITNESS: The "additionally" paragraph? Okay.

8 BY MR. KOTZ:

9 Q Does that refresh your recollection as to what  
10 happened with that issue regarding the investment advisor and  
11 your exam?

12 A I'm still -- don't recall this issue, but it says  
13 what it says.

14 Q Okay. I'll show you the next document marked as  
15 Exhibit 25. This is the second set of document requests to  
16 Bernie Madoff, drafts 1 through 10 and a final request. Do  
17 you remember an additional document request that went out to  
18 Bernie Madoff?

19 (SEC Exhibit No. 25 was marked for  
20 identification.)

21 A I don't recall.

22 Q I'm going to show you another document marked as  
23 Exhibit 26. This is a draft letter from Eric Swanson to  
24 Peter Madoff. Do you recognize, personally, any of the  
25 handwriting on this letter?

1 (SEC Exhibit No. 26 was marked for  
2 identification.)

3 A It's not mine and I don't recognize whose it is.

4 Q You see that there's -- on the face of Exhibit 26  
5 there's question one, which is crossed out. Do you see that?

6 A Yes.

7 Q What kind of information was being requested here  
8 that was crossed out?

9 A We call it trading data.

10 MS. STEIBER: Would this be audit trail trading  
11 data that's requested?

12 THE WITNESS: Right, audit trail I also refer to  
13 SRO, but it would be trading data from the firm, it looks  
14 like.

15 MR. KOTZ: And if you look at Exhibit 11 in the  
16 previous document, which is the final letter that was sent to  
17 Madoff dated February 18, 2004 --

18 THE WITNESS: February 18, 2004? Yes.

19 MR. KOTZ: Do you see that the information  
20 contained in the draft that was crossed out in 26 was not put  
21 in the final?

22 MS. STEIBER: Of those notes -- next letter.

23 MR. COBB: So the next letter is on 26 and then  
24 your question is is that request in the February 18th letter,  
25 which you represent is the final letter?

1 MS. STEIBER: Correct.

2 MR. COBB: Okay.

3 THE WITNESS: Right, so this is not in here,  
4 correct.

5 BY MR. KOTZ:

6 Q And do you have any idea why it wasn't in there or  
7 what "save for next letter" refers to?

8 A I don't.

9 Q Huh?

10 A I do not.

11 Q All right, next document we're going to show you,  
12 Exhibit 27. This is a letter from Bernie Madoff date March  
13 11, 2004 to Eric Swanson in response to the second document  
14 request. I'll ask you if you ever saw this letter.

15 (SEC Exhibit No. 27 was marked for  
16 identification.)

17 (The witness examined the document.)

18 A I don't recall seeing this letter.

19 Q Okay. And do you recall anything about any  
20 responses from Bernie Madoff, any representations made by  
21 Bernie Madoff in his responses to the document requests?

22 A I do not recall, no.

23 Q Okay, the next document is a series of documents  
24 we're going to mark as Exhibit 28. It says, "Bernard L.  
25 Madoff Investment Securities LLC, New York, London, Period

1 Ending 12/31/01." Do you know what this document is?

2 (SEC Exhibit No. 28 was marked for  
3 identification.)

4 MS. STEIBER: If you refer back to that March 1st  
5 letter, the first line says, "In response to your letter of  
6 February 18, 2004, we are providing copies of client account  
7 statements reflecting all the transaction data related to the  
8 accounts of those clients utilizing the split-strike forward  
9 conversion strategy." Okay. And this is a sample of -- I'm  
10 making representation, this is a sample of one of those  
11 customer statements that was provided in response to the  
12 second document request.

13 MR. COBB: "This" being Exhibit 28?

14 BY MS. STEIBER:

15 Q Exhibit 28. Looking at that client customer  
16 statement, would you describe that it contains trading, audit  
17 trail data information?

18 A Well, it's an account statement that has trading  
19 information in it.

20 Q Would that be audit trail information?

21 A I would call this an account statement not a audit  
22 trail.

23 Q If you were conducting a front-running examination,  
24 would the data provided in that customer statement be  
25 sufficient to perform an adequate or good front-running

1 examination?

2 A It's possible, yes.

3 Q Why do you say it's possible?

4 A We're talking about front-running a retail order  
5 flow --

6 Q Okay, how --

7 A -- so if you -- so typically, front-running  
8 means -- it's almost always in the context of large blocks of  
9 orders. So if I'm Fidelity and I'm going to sell 10 million  
10 shares of Microsoft, then if I have that information before  
11 they prosecute their execution strategy then I can trade  
12 ahead of that order because that order typically will move  
13 the market. So if I buy before they start selling, that  
14 price is -- then I will get better prices because of that  
15 market information.

16 In a retail -- in this exam we're talking about  
17 retail order flow of 100 shares and none of the orders by  
18 themselves would move the market, so the information is not  
19 valuable to front-run. So I think the theory of this  
20 front-running inspection was whether -- or my theory of it at  
21 the time was whether or not you could, in almost a real-time  
22 sense -- you would need, you know, strong technology -- you  
23 could see trends from the retail flow and act upon the trends  
24 before, you know, the next group of retail orders got  
25 executed.

1           So the premise on this whole exam was how do you  
2 front-run retail orders. And I think, you know, I think at  
3 the time and probably today, I think it's -- I think -- I'm  
4 still not -- I still do not think it's very easy if not --  
5 if -- and almost -- whether it's possible to front-run retail  
6 orders except in the context of pre-opening orders.

7           So that's -- yeah, I do remember asking mark to  
8 concentrate on the pre-open where you most likely would have  
9 market-moving information, the intraday trading. The  
10 intraday trading I think was much more difficult to -- much  
11 more difficult for that information to be front-ran.

12           So back to your question if you're looking at -- if  
13 you have account statements which show you bought 10,000  
14 shares on a certain day, I think that's, to me, enough  
15 information to know that that's unlikely to have front-ran  
16 retail customer orders because it's simply -- there's no  
17 information in retail order flow to determine -- to take  
18 advantage of that to get a better price for Exxon or Home  
19 Depot.

20           Q     So you think -- you could have been the one that  
21 told Mark Donohue not to seek any other trade data other than  
22 what's in this customer statement?

23           A     I mean, I definitely -- like I said, the  
24 front-running -- should have included trading data from  
25 retail side and from the proprietary side. I don't recall

1 and would certainly be surprised if I ever said, "Don't get  
2 the proprietary trading data."

3 Q Now, if -- do you think if your exam team had gone  
4 to the NASD and gotten the trade data they would have  
5 discovered that Madoff wasn't trading? Discovered it was,  
6 potentially, a Ponzi scheme?

7 A The -- well, actually, the trade data from the  
8 market-making unit would have been at ACT and from what I've  
9 seen those are real trades. What I understand -- what I  
10 recall from the phone call with Madoff was that most or all  
11 of his trading was done out of London so those trades would  
12 not have been included in the SRO audit trail.

13 Q So if he was trading in London he wouldn't have  
14 trading records?

15 A He would have trading records, yes.

16 Q Oh, he would have trading records but --

17 A Or should have had trading records.

18 Q So there's nowhere you could go to get trading  
19 records if he's trading in London? I want to understand, if  
20 he's trading in London it seems that, to me, you would still  
21 have places you could go --

22 A Well, I would have expected Mark and the team to  
23 get the trading records from his trading in London. He  
24 should have a trade blotter in London.

25 Q And do you know if that was ever requested? Did

1 you talk to Mark about requesting a trade blotter?

2 A I do recall that -- I do recall talking to him  
3 about getting the retail -- samples of the retail flow and  
4 samples of the proprietary trades, which should have been the  
5 trade record from London, from his broker-dealer in London.

6 Q Now, what -- could you give a little bit more  
7 detail about what Madoff said about trading in London and why  
8 you recall that?

9 A On the phone -- yeah, again, I knew nothing about  
10 his hedge fund and he explained in general terms about his  
11 hedge fund and that most -- it might have been most or all  
12 his trading was done out of London. I recall that because  
13 that means my theory of the front-running case getting trade  
14 data from the broker-dealer on the retail side or proprietary  
15 side means we would have had to have gotten trade data from  
16 London, so I just viewed that as noteworthy.

17 BY MR. KOTZ:

18 Q Okay, I'm going to show you another document, we'll  
19 mark that as Exhibit 29. This is an e-mail from you to Personal Privacy  
20 [REDACTED] dated March 9, 2004, 12:31 p.m.

21 See you're providing information to Personal Privacy  
22 about Madoff Securities. You see part of what you tell  
23 Personal Privacy is, "Madoff has consistently generated revenues --"  
24 I'm sorry, "Madoff has consistently generated returns for the  
25 hedge funds of around 10 percent per year, which we have been

1 told is high given the conservative nature of the strategy  
2 and market conditions over the last several years. We're in  
3 the process of analyzing one year of transactions in all the  
4 hedge funds for which Madoff executes this strategy."

5 So do you recall having any -- first of all, who is

6 Personal Privacy

? Where did he work?

7 (SEC Exhibit No. 29 was marked for  
8 identification.)

9 A Division of Enforcement.

10 Q Okay. Why would you provide information to the  
11 Division of Enforcement?

12 MR. COBB: You mean why did he in this instance or  
13 why would he generally?

14 BY MR. KOTZ:

15 Q Well, both I guess. Let's start with why did you  
16 in this instance.

17 A I mean, they might be having -- they might -- often  
18 I would -- they would come to me for when they didn't  
19 understand trading or market issues, so that's -- that would  
20 be a typical interaction I would have with the Division of  
21 Enforcement in general.

22 Q Okay. But why would you provide them information  
23 about a particular registrant that you were examining?

24 A Do you mind if I -- should I read the whole e-mail  
25 or --

1 Q Please, sure.

2 A Okay.

3 (The witness examined the documents.)

4 THE WITNESS: I'm sorry, are these e-mails part of  
5 the chain? It's on page -- their not page numbered but it  
6 starts with subject?

7 MS. STEIBER: I'm actually not sure. I have a call  
8 in to OC because they recently produced these e-mails and I'm  
9 waiting for a call back to say, you know, exactly -- if they  
10 are just from a search that mail came out this way. We just  
11 want to ask you a question about that first e-mail.

12 THE WITNESS: First one, okay. I'm sorry, I was  
13 reading --

14 MS. STEIBER: Yeah.

15 THE WITNESS: These look like they're not related.

16 MS. STEIBER: Right.

17 THE WITNESS: Okay. So I mean, this e-mail looks  
18 like -- I think vaguely recall kind of apprising Personal Privacy of kind  
19 of interesting issues that are -- that could possibly --  
20 exams that could possibly be referred to enforcement at some  
21 time. That's what --

22 BY MR. KOTZ:

23 Q Do you think you were referring the facts that  
24 Madoff had consistently generated returns of about 10 percent  
25 per year, which is high given the conservative nature and the

1 market conditions, to enforcement for their possible  
2 investigation of Madoff?

3 A Yeah, I would -- I mean, again, I don't recall  
4 this, but that's, you know, looking at the -- maybe a  
5 heads-up as opposed to this is -- usually referral -- an  
6 actual referral is more formal with a memo, but it certainly  
7 is a heads-up to Personal  
Privacy about issues we see at Citadel with  
8 Madoff.

9 Q Okay. And so one of the issues you saw at Madoff  
10 had to do with his consistently high returns?

11 A Yeah, I mean it's part of the story that I'm giving  
12 him a heads-up about.

13 Q And you say, "We are in the process of analyzing  
14 one year of transactions in which all of the hedge funds for  
15 which Madoff executes his strategy," do you know how that  
16 analysis was done?

17 A I'm sorry, where's that sentence? "We're in the  
18 process of analyzing one year of transactions in all the  
19 hedge funds for which Madoff executes his strategy." How  
20 it's done?

21 Q How would you have gone about analyzing that one  
22 year of transactions?

23 A I don't know.

24 Q Do you remember analyzing one year of transactions  
25 in all of Madoff's hedge funds?

1 A I do not, no.

2 Q Do you know if anybody with investment advisor  
3 experience was brought in to analyze those returns?

4 A I don't recall anyone being brought in.

5 Q Do you know if falsification of returns would have  
6 been something that you looked into in your analysis of one  
7 year of transactions?

8 A I'm sorry?

9 Q Do you know if falsification of the returns would  
10 have been part of the analysis that you were in the process  
11 of conducting?

12 A To determine whether they were false?

13 Q Yeah.

14 A I don't know.

15 Q But I mean, would that be -- it talks about an  
16 analysis of one year of transactions in all the hedge funds  
17 for which Madoff executes the strategy. As part of that  
18 analysis would you look at whether the returns were  
19 falsified?

20 A I don't know. I don't recall my team doing this  
21 exam or part of the front-running exam.

22 Q Right, but I mean if you said to Personal Privacy  
23 that you're in the process of doing this, I assume you did --  
24 your team actually did it.

25 A I would assume so too, yes.

1 Q Okay.

2 MS. STEIBER: I just wanted to go back real quickly  
3 to Exhibits 12a and 13, which one of them is the planning  
4 memo that's addressed to you in which in section 3a it talks  
5 about requesting trading data from the NASD and then that  
6 draft letter to the NASD. If -- you had testified earlier  
7 that Madoff told you he was trading in Europe?

8 MR. KOTZ: London.

9 MS. STEIBER: Oh, sorry, in London. Why would you  
10 be drafting a letter to the NASD or why would that be part of  
11 your process if you really believed that he was trading in  
12 London?

13 THE WITNESS: Well, front-running is kind of two  
14 sets of data. Of one -- we would certainly need the data  
15 about the retail flow and that would be easy to get from the  
16 NASD.

17 MS. STEIBER: Okay.

18 MR. KOTZ: Okay, we're going to mark two exhibits  
19 now, Exhibits 30 and 31. The first one, Exhibit 30, is an  
20 e-mail from Genevieve Walker to Alex Sadowski, 4/6/2004,  
21 6:49 p.m.

22 And then the next one, Exhibit 32 is an e-mail from  
23 Mark Donohue to Genevieve Walker --

24 (SEC Exhibit Nos. 30 and 31 were  
25 marked for identification.)

1 MR. COBB: I'm sorry, you went 30 and then 32.

2 MR. KOTZ: -- dated 4/7/2004. I'm sorry, 9:29 a.m.

3 MS. STEIBER: So this is Exhibit 30 and 31.

4 BY MR. KOTZ:

5 Q Yeah. So Exhibit 30 is 4/6/2004, 6:49 p.m. e-mail  
6 and 31 is the 4/7/2004, 9:29 a.m. e-mail from Donohue from  
7 Genevieve Walker.

8 You can see in these e-mails, the first e-mail  
9 Genevieve Walker says to Alex Sadowski asking which are  
10 the priority of her projects. And she said, "I'm not sure  
11 where the hedge fund project falls on our list of priorities  
12 as of right now, please advise." And then Alex Sadowski  
13 responds, "Get the mutual fund work completed first."

14 And then the 4/7/2004 e-mail, we have Genevieve  
15 Walker working on -- asking -- sending an e-mail to Mark  
16 Donohue saying, "Should we just focus on mutual funds and  
17 return to Madoff when we're done?" And Mark Donohue saying  
18 to Genevieve Walker, "Concentrate on mutual funds for the  
19 time being."

20 First, was that the team that was working on your  
21 Madoff exam, Genevieve Walker, Jacqueline Wood and Mark  
22 Donohue? Is this the same exam that you have been talking  
23 about?

24 A That's my recollection, yes.

25 Q Okay. So were you aware that Mark Donohue

1 instructed Genevieve Walker to stop working on the Madoff  
2 exam in favor of mutual funds work?

3 A I don't read it that he told her to stop, but I  
4 wasn't aware of either of these e-mails.

5 Q Okay. Were you aware at any point in time that  
6 there was a shift in priorities from the Madoff exam to  
7 mutual funds work?

8 MR. COBB: Well --

9 THE WITNESS: I mean, Mark says concentrate on the  
10 mutual fund, that doesn't mean, you know, there's eight hours  
11 in a day, you can obviously -- I assume what he meant was,  
12 you know, focus on that and get it done first but it doesn't  
13 mean stop working on Madoff or --

14 MR. KOTZ: So --

15 THE WITNESS: And Mark certainly didn't tell me,  
16 "I'm having people stop working on Madoff," or anything like  
17 that.

18 MR. KOTZ: Okay. So were you aware that there was  
19 a almost one-year period where no work was done on the Madoff  
20 examination?

21 THE WITNESS: I was not aware of that, no.

22 MR. KOTZ: Would it surprise you to hear that? I  
23 mean based on your recollection do you think that that could  
24 have happened that there was this year-long period where  
25 nothing was done on the Madoff exam from the moment that Mark

1 Donohue told Genevieve Walker to concentrate on mutual  
2 funds until a year later?

3 THE WITNESS: April '04 to April '05, that would  
4 surprise me, yes.

5 MR. KOTZ: Okay. I'm going to show you the next  
6 document, we're going to mark this as Exhibit 32. This is an  
7 e-mail from Mark Donohue to Eric Swanson, 3/16/2004. See,  
8 Eric Swanson says to --

9 (SEC Exhibit No. 32 was marked for  
10 identification.)

11 MS. STEIBER: 2005.

12 MR. KOTZ: 2005, I'm sorry.

13 MS. STEIBER: This is almost a year later.

14 MR. KOTZ: 3/16/2005, that's right. You see Eric  
15 Swanson sends an e-mail to Mark Donohue on March 16, 2005,  
16 "What is the status of the Madoff hedge fund thingee?" And  
17 Mark Donohue says, "Dead, we never found any real problems."

18 Were you aware that in or around the period of  
19 March 2005 when the NYRO folks began asking questions about a  
20 Madoff exam they were working on that they went to your staff  
21 to ask what happened with your exam? Are you -- do you  
22 remember that?

23 MR. COBB: I'm sorry, just let me -- that's two  
24 questions. First you asked him whether he was aware of this  
25 exchange and then you added that other communication to his

1 staff. So is that two questions, right?

2 BY MR. KOTZ:

3 Q Yeah, I don't think I did but we'll -- are you  
4 aware of the Mark Donohue -- Eric Swanson trying to find out  
5 what happened with the Madoff hedge fund thingee?

6 A No, I mean I was aware that Mark told me, I can't  
7 remember the date, that they weren't find anything so it's  
8 consistent with this.

9 Q But --

10 A But I don't know the -- I don't recall the dates  
11 when I asked Mark.

12 Q But where you aware that Eric Swanson was trying to  
13 find out whatever happened with the Madoff examination in  
14 2005?

15 A No, I don't recall this. I don't recall this  
16 e-mail.

17 Q Do you recall at some point in time that the folks  
18 in New York asked for information or documentation from your  
19 office about Madoff -- about your Madoff exam?

20 A I recall that John Nee -- was doing a similar exam.  
21 I mean, I got the sense it was after in time to our exam, but  
22 I do recall that, yes.

23 Q Okay. And you recall that John Nee asked you to  
24 provide documents relating to your exam to provide to them?

25 A I mean, I recall us sending our files, as it were,

1 to John Nee to incorporate it in his exam.

2 Q At that point in time that you sent your files to  
3 John Nee, did you have an understanding that your Madoff exam  
4 had been completed?

5 A My understanding is that we did not find any  
6 indicia of front-running, yes.

7 Q Okay. Would it surprise you that that's not what  
8 Mark Donohue testified? And in fact, Mark Donohue testified  
9 that there were significant questions that were pending but  
10 that the exam hadn't been worked on for almost a year.

11 A That would surprise me, yes.

12 Q Do you think that that could have happened and you  
13 weren't aware of it?

14 A I'm not aware of it, so yes, it could have  
15 happened. I'm sorry, what do you -- what could have  
16 happened?

17 Q Do you think that Mark is not providing truthful  
18 information or is it that you just weren't aware that this  
19 was happening?

20 A I certainly believe Mark is providing truthful  
21 information, no question about that. Was I aware of those  
22 details at the time or now, I don't recall being aware of  
23 them.

24 Q Would that be concern that an exam that was  
25 operating under you would be left dormant for almost a year?

1 A It's concerning, yes.

2 Q Do you remember -- what was your reaction when you  
3 found out that the New York office was also conducting an  
4 exam of Madoff?

5 A I remember being mildly upset about that.

6 Q Why was that?

7 A Because it meant that we probably didn't put our  
8 information into the tracking system like we're supposed to  
9 do.

10 Q So you weren't aware that New York was doing an  
11 examination of Madoff at the same time and New York wasn't  
12 aware that you were; is that right?

13 A I was not aware that they were, I don't know what  
14 they were aware of.

15 Q Did you discuss your examination with the New York  
16 office?

17 A I remember John Nee contacting us or me, but I  
18 don't recall me discussing it clearly. I'm sure it was  
19 discussed with them.

20 Q What do you say clearly was discussed with them?

21 A Well, I think I told -- I asked Mark and maybe Eric  
22 to, you know, deal with the fact that we have two ongoing  
23 exams of the same firm at the same time or in near terms. So  
24 you know, I would have instructed them to coordinate and make  
25 sure you're as helpful -- if theirs was ongoing, as helpful

1 to them as possible, something like that.

2 Q Do you recall that at that time Mark and Eric  
3 really hadn't really gotten very far in their exam and so  
4 there really wasn't much information for them to provide to  
5 New York?

6 A I mean, I do recall that Mark told me that he was  
7 not finding anything, but I would have assumed there would  
8 have been documents to provide from the exam.

9 Q Do you think that the exam that was conducted under  
10 you, the Madoff cause exam, was conducted in a adequate way?

11 A I mean, now you're telling me that there was  
12 nothing done for a long period of time, I think that shows a  
13 certain level of inadequacy, yes.

14 MR. COBB: If in fact it's true, you have no  
15 knowledge of that.

16 THE WITNESS: Right.

17 MR. KOTZ: Do you recall it being difficult to find  
18 the Madoff documents when they were being sent up to the New  
19 York regional office because people didn't know where they  
20 were because the matter hadn't been worked on for so long?

21 THE WITNESS: I do recall Genevievette, issues with  
22 Genevievette, that -- and, you know, of putting one and one  
23 together that maybe the documents -- if the documents were  
24 kept by here and then we had trouble with documents that she  
25 was responsible for keeping.

1 MR. KOTZ: What kind of trouble did you have with  
2 the documents that Genevieve was responsible for keeping?

3 THE WITNESS: Like sloppiness, things like that. I  
4 think there's doors were locked and it was hard to get to  
5 them sometimes, just vague recollections.

6 MR. KOTZ: What about in terms of Genevieve's  
7 work? Was her work sloppy?

8 THE WITNESS: I would say she was one of the weaker  
9 employees I've had in my career.

10 MR. KOTZ: What about Jacqueline Wood?

11 THE WITNESS: I would say on the contrary, she's  
12 probably one of the best I've ever had.

13 MS. STEIBER: Were you aware of problems between  
14 Mark Donohue and Gen Walker?

15 THE WITNESS: Yes.

16 MS. STEIBER: What were you aware of?

17 THE WITNESS: I think she made an allegation  
18 against him.

19 MR. KOTZ: Did you -- were you aware of any  
20 allegations that Ms. Walker made against Mr. Donohue relating  
21 to the Madoff exam?

22 THE WITNESS: No.

23 MR. KOTZ: Okay, you weren't aware of Ms. Walker  
24 stating that she wanted to continue to work on the Madoff  
25 exam but wasn't allowed to?

1 THE WITNESS: I wasn't aware of that, no.

2 MR. KOTZ: Do you think that the difficulties  
3 between Mark Donohue and Ms. Walker might have had an impact  
4 on how the Madoff exam was run?

5 THE WITNESS: I don't think it should have. I  
6 mean, it's unfortunate she was a weak member, but the data  
7 analysis could have done -- been done by Jackie at a high  
8 level, so -- but it's certainly, you know, probably didn't  
9 help, obviously.

10 MR. KOTZ: Okay. Do you remember ever following up  
11 to find out what happened with NYRO's exam?

12 THE WITNESS: Following up, I don't recall.

13 MR. KOTZ: Do you remember at any point -- do you  
14 remember at any point in time learning that the enforcement  
15 division was looking into Madoff?

16 THE WITNESS: I, obviously, became aware of it in  
17 the media but I don't recall at the time ever being made  
18 aware of it, no. The Enforcement Division in New York or  
19 generally?

20 MR. KOTZ: Anywhere.

21 THE WITNESS: Anywhere, yeah.

22 MR. KOTZ: All right, next document I'm going to  
23 show you is Exhibit 33. This is an e-mail from you to Eric  
24 Swanson dated 2/28/2006. We're going to mark this as Exhibit  
25 33. And the next document we're going to mark as Exhibit 34,

1 which is an e-mail from John Nee to Eric Swanson, cc Peter  
2 Lamore dated 2/28/2006 at 3:03 p.m.

3 And you see you're asking Eric Swanson, "Any news  
4 on that NYRO exam of Madoff," in the 2/28/2006 e-mail. And  
5 then in the 2/28/2006 e-mail, 3:03 p.m. there is a response  
6 from John Nee saying, "We closed out the examination after  
7 looking for and not finding any evidence of front-running,  
8 see attached report. However, shortly thereafter our  
9 enforcement people got an anonymous complaint alleging Madoff  
10 is either front-running or is the biggest Ponzi scheme ever."

11 Does that refresh your recollection as to whether  
12 you became aware at any point that enforcement was looking  
13 into Madoff?

14 (SEC Exhibit Nos. 33 and 34 were  
15 marked for identification.)

16 A If these are accurate, yes.

17 Q Do you remember if you reviewed the examination  
18 closing report that the NYRO office provided you?

19 A I don't recall looking at it in detail, no.

20 Q Did you have any particular reaction that  
21 enforcement was looking into Madoff for an allegation of the  
22 biggest Ponzi scheme ever?

23 A I don't recall having a reaction, but --

24 Q Okay.

25 A -- but probably was.

1 Q Okay. Let me show you the next document we're  
2 going to mark as 35. This document is the day after you  
3 received this e-mail on February 28, 2006 that gave  
4 information about Madoff possibly having the biggest Ponzi  
5 scheme ever.

6 And this is an e-mail dated 3/1/2006, 9:15 p.m. An  
7 e-mail exchange between you and John McCarthy, where you  
8 say -- I'm sorry, between you and Eric Swanson where you say  
9 in the e-mail, Wednesday, March 1st at 8:00 to Eric Swanson,  
10 "Two things, one put the squeeze on Shana. Two, Cutler gave  
11 Lori a tip we should follow up on."

12 So this is the day after you find out that Madoff  
13 may have been running the biggest Ponzi scheme ever. Do you  
14 recall why you're asking Eric Swanson to put the squeeze on  
15 Shana?

16 (SEC Exhibit No. 35 was marked for  
17 identification.)

18 A Yeah, I mean it's -- I think it has to do with the  
19 conference that was coming up, if I recall correctly.

20 Q Okay. But the Shana in this e-mail, 3/1/2006  
21 e-mail, that refers to Shana Madoff; is that right?

22 A Yes.

23 Q Okay.

24 A And these are what -- at night or on weekends I  
25 would, things that I would kind of to remember I would shoot

1 off an e-mail. One, you know, put the squeeze on Shana,  
2 two --

3 Q Do you remember what the tip was? "Cutler gave  
4 Lori a tip we should follow up on," was that the tip related  
5 to Madoff?

6 A No, I -- again, pretty much well remember it was --  
7 Cutler gave very few tips to me, obviously, most of it went  
8 the other way. I do remember he wanted us to look into  
9 possible -- possibility of insider trading in CDSs and that's  
10 about the right period of time.

11 Q And why were you asking Eric Swanson to put the  
12 squeeze on Shana?

13 A Because I wanted to -- originally, I did not  
14 decline to go to a conference, a big annual conference, I  
15 think I was getting pressure at that time. You know, Lori  
16 was really encouraging senior staff to participate in  
17 conferences and she was -- if I recall correctly, like, you  
18 know, the emcee of the conference in Florida so I wanted --  
19 you know, I asked her previously, and this is a follow up to  
20 that, whether she could get me on a panel.

21 Q And why would Eric be putting the squeeze on her?

22 A Probably just asking Eric to because he  
23 communicated with her more than I did so I just, you know,  
24 when you're talking to her, you know, remind her if she's had  
25 any luck with getting me on a panel.

1 Q So that has nothing to do with you finding out that  
2 Madoff was potentially running the biggest Ponzi scheme ever?

3 A To me it's -- it has nothing to do with it, it's  
4 something completely separate.

5 Q Okay. Did you ever -- strike that. When did you  
6 first meet Shana Madoff?

7 A It's possible during those exams and the late -- in  
8 late 90's, but when I recall interacting with her would have  
9 been when we started the SIA breakfast.

10 Q So would you say your interactions with her were  
11 all professional or were there any social in nature?

12 A They were primarily professional until this period  
13 of time.

14 Q Okay. Next document we're going to -- an e-mail  
15 we're going to mark it as Exhibit 36. This is an e-mail from  
16 you to Personal Privacy dated 12/19/2005, 10:57 a.m. Do  
17 you know who Personal Privacy is? Is that how I  
18 pronounce her name, do you know?

19 (SEC Exhibit No. 36 was marked for  
20 identification.)

21 A I don't know but it sounds right to me.

22 Q She has a reference in there -- Personal Privacy is  
23 sending an e-mail to you saying, "Shana would like to send  
24 you something but, unfortunately, we don't have your mailing  
25 address. Would you be so kind to send it to me?" Do you

1 know what Shana was trying to send you?

2 A I do not know.

3 Q Did Shana ever send you a gift?

4 A I don't recall ever getting a gift, no.

5 Q Okay. Do you remember an SAA conference took place  
6 around March 19th or March 20, 2006 in Florida?

7 A Yes.

8 Q Okay. I'm going to show you an e-mail, we're going  
9 to mark this as Exhibit 37. This is an e-mail between you  
10 and Shana Madoff, 3/19/2006, 5:42 p.m. You said before that  
11 you had a professional relationship with Shana up to a  
12 certain point and then it might have been more social.

13 What do you recall about the social relationship?  
14 Here is a reference to grabbing a cocktail and lots of other  
15 e-mails, but, you know, if you want to just tell me first  
16 based on your recollection, what was the nature of the  
17 relationship?

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

20 A Until the -- yeah, I probably don't recall ever  
21 doing anything social at all, maybe a dinner the night before  
22 one of the breakfasts before that. And then this -- at this  
23 conference she, you know, we -- you know, I met her for beers  
24 and we had beers. So that was the first time I kind of ever  
25 talked to her about anything personal, you know, non-work

1 related.

2 Personal Privacy



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Q Okay. We're going to mark the next document as Exhibit 38. This is an e-mail from Shana Madoff to you dated Monday, April 17, 2006, 5:10 p.m.

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Do you see in this e-mail Shana says to you, "Thank you for your kindness, I really want to get some alone time with you because I want to talk to you about the other night. Hope all is well." Do you know what she was referring to in wanting to get some alone time with you to talk about the other night?

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(SEC Exhibit No. 38 was marked for

1 identification.)

2 A I think so, yes.

3 Q What was that?

4 A I think -- again, I can't remember the exact night,  
5 but it, you know, within a matter of days I was in New York  
6 with Eric and she and Eric -- or Eric asked me to go to a  
7 karaoke bar with -- and meet up with Shana. She was with  
8 Eric at the time. And then the karaoke bar turned out to be  
9 a -- I call it a strip club, but a high-end strip club, and I  
10 was extremely upset. But they kind of where having -- looked  
11 like they were having fun at my expense, so I think it became  
12 a big deal between Eric and myself.

13 Q And how are they having fun at your expense?

14 A Well, because the told me we were going to a  
15 karaoke bar but it was not a karaoke bar.

16 Q And so you were uncomfortable being at a strip  
17 club?

18 A I was then and generally don't like going to places  
19 like that.

20 Q Okay. I'm going to show you another document, this  
21 is marked as Exhibit 39. This is an e-mail 4/21/2006 from  
22 Alex Sadowski to you.

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

25 MR. COBB: I'm sorry, 4/21 did you say?

1 MS. STEIBER: Yes.

2 BY MR. KOTZ:

3 Q This e-mail and some subsequent e-mail reference  
4 there being secrets from you and issues with full disclosure  
5 about Eric Swanson and Shana Madoff. Do you recall that  
6 there was a time period where there was an issue about  
7 information being kept from you about their relationship?

8 A Yes, I do.

9 Q Okay. So what do you recall about that?

10 A Well, I mean, Eric and I -- I was very much against  
11 him having a relationship with her and I made it clear

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21 Q Did the fact that she worked for a registrant have  
22 any impact on your feelings about whether Eric Swanson should  
23 maintain a relationship with her?

24 A The driving motivation -- that was not even -- the  
25 driving motivations were much more personal than that. That

1 issue wouldn't have really come into play.

2 Q I'm sorry, would not have come into play?

3 A That would have not -- that would not have -- in my  
4 mind then and now, that would be kind of -- there's -- what  
5 drew me to the conclusions would not have been that fact.  
6 That would have been, I guess, irrelevant in this --

7 Q So you didn't think there was anything  
8 inappropriate about the fact that Shana was a registrant,  
9 Eric worked for the SEC, potentially he would be regulating  
10 the entity that Madoff -- that Shana worked for? This was a  
11 company that had been examined three, four times and  
12 investigated by the SEC.

13 A I -- you know, it might have played a minor role in  
14 my thinking, but I think, you know, if she was -- again, it  
15 was a very personal -- why I didn't want him dating her was  
16 more personal than kind of the fact that she worked at a  
17 broker-dealer.

18 Q Did you have any concerns about the Madoff  
19 operations in terms of the fact that you had done an  
20 examination of front-running or that perhaps that part of  
21 what you were concerned about Eric being involved with was a  
22 person who may have been in a company or the compliance  
23 officer of a company that was involved in illegal things?

24 A I mean, at that time I didn't view Madoff a company  
25 that was doing illegal things.

1 Q So that's no.

2 A Ask the question again.

3 Q So the fact that you had done an exam, you hadn't  
4 found front-running but yet there was still questions about  
5 Madoff's returns --

6 MS. STEIBER: You had that complaint from Nee  
7 saying that maybe their running the largest Ponzi scheme  
8 ever.

9 THE WITNESS: Oh, I see. Again, my -- the reason  
10 why I was against him dating Shana were, I would say more  
11 profound than that -- those sorts of issues didn't come into  
12 play.

13 BY MR. KOTZ:

14 Q You just didn't like Shana for whatever reason?

15 A That's fair, I guess.

16 Q And there was a time period when you and Alex  
17 Sadowski were kind of sharing information about what happened  
18 with Eric and Shana; is that right?

19 A Is it right that I would have shared information  
20 with Alex?

21 Q Yeah.

22 A Yes.

23 Q Okay. And then there was an incident where you saw  
24 them, you saw Eric and Shana together, I think at his  
25 apartment, his roommate was there. What was the roommate's

1 name?

2 MS. STEIBER: OCIE Staff Accountant

3 BY MR. KOTZ:

4 Q OCIE Staff Accountant, and you got very upset. Do you  
5 recall that?

6 A Yeah, vaguely, but yes I do recall that.

7 Q Okay.

8 A I guess I was surprised.

9 Q And did you indicate to Eric Swanson that if he  
10 didn't cut of his relationship with Shana Madoff he would  
11 lose you as a friend?

12 A I mean, that's consistent with how I felt, yes.

13 Q Okay. But in the end Eric Swanson didn't cut off  
14 his relationship with Shana, in fact, he married her. Is  
15 that right?

16 A That's right.

17 Q So how did that resolve itself given that you were  
18 so upset and I guess you're still friends with him today  
19 aren't you?

20 A Yes.

21 Q Okay. So how did that resolve itself?

22 A Slowly. I mean, something that still, to this day,  
23 I'm somewhat upset in.

24 Q And how did you feel when you found out that in  
25 December 2008, that Bernie Madoff had admitted to a Ponzi

1 scheme? Did you feel like if, perhaps, Eric had listed to  
2 you he might not be involved with somebody who, at least now,  
3 has an uncle who's, you know, one of the most famous  
4 fraudsters ever?

5 A That thought came to my mind, yes.

6 Q I'm going to show you another document. This is  
7 Exhibit 40. This is an e-mail from you and Alex Sadowski,  
8 Thursday, April 6, 2006 at 2:01 p.m. Do you recall what you  
9 were referring to when you said, "I guess we won't be  
10 inspecting Madoff any time soon?"

11 (SEC Exhibit No. 40 was marked for  
12 identification.)

13 MR. COBB: Do you recall the context of the e-mail?

14 THE WITNESS: Yeah.

15 MR. COBB: This is 40, I'm sorry? Yeah, 40. God,  
16 I wish I could see.

17 THE WITNESS: I mean, I recall this general  
18 situation, yes.

19 MR. KOTZ: What do you recall about the general  
20 situation?

21 THE WITNESS: That I was upset about it and, you  
22 know, probably more accurate description would be saying Eric  
23 won't be inspecting Madoff anytime soon. But it's -- the  
24 real point is to -- for me to tell Eric -- or I'm sorry,  
25 Alex, that, "Hey, I'm aware of what's going on." The point

1 of it was not about our inspection program.

2 MR. KOTZ: Did you think at any point in time that  
3 Eric's relationship with Shana Madoff had an impact on the  
4 operations of the SEC such that, you know, decisions would be  
5 made about whether Madoff would be inspected?

6 THE WITNESS: Certainly, if an inspection of Madoff  
7 was in the offing he would not be part of it, certainly.

8 MR. KOTZ: But would that factor into decisions of  
9 your group whether you would be involved in a Madoff  
10 inspection?

11 THE WITNESS: It -- mainly, I mean, again, it would  
12 mainly be whether he would be involved but not the group in  
13 general, no.

14 MR. KOTZ: So the group could do a Madoff  
15 inspection without Eric?

16 THE WITNESS: Yes.

17 MR. KOTZ: Did you feel at any point in time that  
18 Eric should formally recuse himself from all Madoff matters  
19 after he developed a relationship with Shana Madoff?

20 MR. COBB: Well, were there any Madoff matters  
21 after that?

22 MR. KOTZ: I mean, was there any responsibility on  
23 Eric Swanson's part to take any action after he started  
24 developing a relationship with the compliance officer or  
25 registrant?

1 THE WITNESS: I would view that -- I mean, I would  
2 view that as peculiar. I mean, if it -- if a matter came up,  
3 certainly he would -- should be recused. But as people that  
4 are into romantic relationships, they may or may not -- they  
5 don't proactively recuse themselves is my typical experience.

6 MR. KOTZ: What about if somebody was say,  
7 interviewing for a job with a particular company? Somebody,  
8 Eric Swanson was interviewing for a job with Madoff, would he  
9 send out some kind of recusal saying, "From now on I'm not to  
10 be involved in any Madoff matters?"

11 THE WITNESS: Yeah, I think there's a -- again, I'm  
12 not that familiar with the process, but I think you're  
13 supposed to alert -- if I understand it -- I mean, I told  
14 Lori when I was interviewing at Getgo. I don't know if  
15 that's a policy or simply a process that I did.

16 MR. KOTZ: Do you think that that same type of  
17 policy should apply when somebody is involved in a romantic  
18 relationship?

19 THE WITNESS: I don't view that as unreasonable,  
20 but again, I think the main thing is to ensure that if  
21 there's an -- if there's a regulatory matter before someone  
22 that should recuse themselves that they handle it  
23 appropriately.

24 MR. KOTZ: I'll show you the next document. I'll  
25 mark it as Exhibit 41. This is an e-mail from Eric Swanson

1 to you dated 4/23/2006 at 5:33 p.m. You see at the bottom of  
2 the page an e-mail from you to Steve Luparello, where you  
3 say, "Shana, Steve, Mike and John, I'm sorry for such short  
4 notice but it looks like the SEC contingent is going to have  
5 to back out of the Greenwich breakfast. Obviously, we can  
6 proceed -- you all can proceed without us but given the usual  
7 aspects of this breakfast I understand that it creates  
8 difficulties without SEC involvement." Do you recall why the  
9 decision was made for the SEC contingent to back out of the  
10 breakfast?

11 (SEC Exhibit No. 41 was marked for  
12 identification.)

13 THE WITNESS: I'm not sure on the dates but I think  
14 after the karaoke thing I made the decision I don't -- you  
15 know, want to basically limit my interactions with Shana, so  
16 I was asking her to -- I told Eric to cancel the breakfast.

17 MS. STEIBER: Why, because she was playing a joke  
18 on you?

19 THE WITNESS: I just felt that Eric was comporting  
20 himself in a way that he never did in the past, I just  
21 wanted -- I just felt it was better for me not to be, you  
22 know, involved in that situation.

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Personal Privacy

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22 BY MR. KOTZ:

23 Q Do you think there's, generally, any concerns about  
24 having too much fraternization between SEC examiners and  
25 registrants or representative of registrants? Is there a

1 point at which there's too much interaction and  
2 fraternization?

3 A There's -- yeah. When, obviously, people are  
4 married to people at broker-dealers, et cetera, so I mean,  
5 you know, I think it's just simply a matter of judgment  
6 what -- where that line is.

7 Q Okay. You don't think that it creates sort of an  
8 appearance problem when there's too much fraternization or  
9 interaction between examiners and registrants at these kind  
10 of social functions?

11 A It certainly could, yes.

12 Q Okay, I'll show you the next document, we'll mark  
13 it as Exhibit 42. And this is an e-mail from Eric Swanson to  
14 John McCarthy dated 4/27/2006, 9:46 a.m.

15 Here in an e-mail below in the exchange on April  
16 27, 2006, 10:46 a.m., you emailed to Eric Swanson "red flag."  
17 You can look at the whole thing and see if you can figure out  
18 what the red flag refers to.

19 (SEC Exhibit No. 42 was marked for  
20 identification.)

21 (The witness examined the document.)

22 A Yeah, I remember this.

23 Q What was it referring to?

24 A Replacing -- I think if I was to do a full  
25 sentence -- right now, you're doing things that I -- now

1 you're doing things that I ask you to do. Meaning, I'm being  
2 sarcastic, you know, actually being cooperative again like  
3 you used to be is maybe is how -- would have been better.

4 Q Does it seem that Eric doesn't get that. He says,  
5 "You're asking me to do this, what am I supposed to do?"  
6 He's -- it seems --

7 A Yeah, I recall -- I think what I -- I'm sorry.

8 Q Go ahead, I'm sorry.

9 A What I recall is that I canceled the breakfast then  
10 basically said, "Okay, we'll do the one more." The hedge  
11 fund one I felt was actually relatively important, the one up  
12 in Greenwich, so I think we -- Eric was kind -- I put him in  
13 probably an awkward situation of canceling it then kind of  
14 rescheduling it is my recollection.

15 Q Okay.

16 A And then that was the last one.

17 Q And do you remember when -- around the time that  
18 Eric left the SEC there was a going-away party for him?

19 A Yeah, it was at my house, yes.

20 Q Okay. And Shana attended this party?

21 A Yes.

22 Q Okay, was that a problem given your concerns about  
23 their relationship or was that -- as the process sort of took  
24 place you were more relaxed or mellow about the relationship?

25 A I think it was a point I was getting mellow, but

1 I still did -- again, I still did not view her in a positive  
2 vein and probably didn't want her coming to my house would be  
3 my guess.

4 Q And then how long --

5 A But things were -- things were mellowed out, if I  
6 recall correctly, by that time significantly more than --

7 Q And how long after Eric left the SEC did you leave  
8 the SEC?

9 A I left in November '07.

10 Q So about a year afterward?

11 A Makes sense.

12 Q Okay. Did your departure have anything to do with  
13 Eric or Shana?

14 A I left the SEC for completely unrelated reasons,  
15 yes.

16 Q Okay. What was your reaction when you first heard  
17 that Bernie Madoff had admitted to conducting a Ponzi scheme  
18 given the fact that there was an examination that you were  
19 involved in?

20 A One of surprise.

21 Q We discussed here several exams that the OC  
22 division did of Madoff, are you aware of other registrants  
23 where there were so many exams done over a short period of  
24 time?

25 A I mean, it -- probably -- you could probably find

1 many examples of similar.

2 Q Where there were three or four exams conducted at  
3 the same entity?

4 A I mean, I -- I'm guessing but I don't -- I think  
5 you could find many examples of that. I mean, obviously, if  
6 you look at a Merrill Lynch, but that's not really an apples  
7 to apples example. But a relatively small firm is -- a  
8 relatively small firm that just has, as it turns out, two  
9 lines of business, and it's probably -- it would probably be  
10 fewer examples of that.

11 Q And do you think there are other examples of  
12 situations where not only were there several exams of a small  
13 firm but also an enforcement investigation opened up of a  
14 small firm?

15 A Are there examples -- I assume that would be  
16 relatively unusual, but again, I don't know.

17 Q Okay. Were you surprised overall that OC, in  
18 either your exam or the NYRO exam or other exams, didn't  
19 discover the Ponzi scheme?

20 A I mean, I was not surprised, in my judgment, given  
21 the scope of the exam under me that we didn't find it, no.

22 Q What about the New York regional office exam that  
23 they did?

24 A Certainly, with the Markopolos memo, information  
25 like that, I think the odds should go up significantly they

1 would find it.

2 Q Did you have occasion to read Harry Markopolos'  
3 memo?

4 A I did. I read most of -- not every word.

5 Q When?

6 A When it came out in the Wall Street Journal.

7 Q After December 2008?

8 A Yes.

9 Q Okay. And what was your impression of that letter  
10 written by Mr. Markopolos?

11 A It's -- kind of speaks for itself. It's  
12 exhaustive, obviously he was obsessed with the issue and --

13 Q Do you think it was a credible document?

14 A Again, reading in the Wall Street Journal with  
15 20/20 hindsight it made a lot of accurate points.

16 Q Do you think if you had access to that document  
17 when you did your exam you would have been able to uncover  
18 Madoff's Ponzi scheme?

19 A The answer is I don't know.

20 Q Okay. Do you think OC examiners have the necessary  
21 qualifications to be effective?

22 A Some do, some don't.

23 Q What about the folks on your team?

24 A Again, getting up the learning curve and  
25 understanding the markets and trading takes a long time. So

1 you know -- but, you know, most of the highly-motivated staff  
2 end up getting pretty far up the learning curve, but not all.

3 Q Do you think at the time that your team conducted  
4 the Madoff cause exam they were experienced enough, had  
5 enough qualifications to be able to do an adequate job?

6 A Certainly, I think Mark did and Eric did, yes.

7 Q What about the rest of the team?

8 A Like I say, Genevievette was one of the weaker  
9 employees I've had, so I would probably say no to her. But  
10 Jackie, with proper direction, could do a decent job.

11 Q Okay. Did Eric Swanson's relationship with Shana  
12 Madoff have any impact at all on the cause exam that you  
13 headed?

14 A None that I'm aware of, no.

15 Q Since Bernie Madoff confessed to the Ponzi scheme  
16 in December of 2008, have you had any conversations with any  
17 current or former employees about the examination, the cause  
18 exam that you worked on?

19 A I spoke, only socially, with Lori. Spoke very  
20 briefly with Eric, but not about the exam. I speak a lot to  
21 Alex because he works for me now, presently, but, you know,  
22 not about the exam.

23 Q Okay. Were you aware that Alex had come and spoke  
24 to us?

25 A He had to ask me for time off, yes.

1 Q Okay. And did you and Alex talk about the  
2 substance of the conversations in the interview he gave us?

3 A He talked, he told me generally what he talked  
4 about and said he couldn't, you know, wasn't allowed to speak  
5 about the testimony. So --

6 Q So what did he tell you generally about what he  
7 talked about?

8 A He said there were a lot of personal stuff, I think  
9 he said something to that effect.

10 Q Did he say anything about substantive matters  
11 relating to the exam?

12 A He didn't -- he did not talk to me about that at  
13 all, no, or reference it.

14 MS. STEIBER: When did you speak to Lori about the  
15 exam?

16 THE WITNESS: I never spoke to Lori about the exam.

17 MS. STEIBER: When was the last time --

18 THE WITNESS: I spoke to her socially, yes, saw her  
19 at a restaurant recently and we've had coffee a couple times,  
20 but not about issues -- it's very clear we can't talk about  
21 anything Madoff.

22 MR. KOTZ: What about with Eric Swanson? Have you  
23 ever had a conversation with him about the Madoff matter?

24 THE WITNESS: No. Again, I think, except in the  
25 context of, "How are you doing? How are you holding up?"

1 Things like that.

2 MR. KOTZ: And you went to Eric Swanson's wedding  
3 with Shana Madoff?

4 THE WITNESS: Correct.

5 MR. KOTZ: Who else from either current or former  
6 SEC employees were there?

7 THE WITNESS: Well, the people I knew, there  
8 where -- I mean, Steve Luparello was I guess a former, Lori,  
9 my wife, I think Alex was there, and perhaps others I can't  
10 recall off the top of my head.

11 MR. KOTZ: Just to kind of be clear, was there any  
12 effort at all by anyone to limit your scope of your Madoff  
13 investigation or back off from the Madoff investigation?

14 THE WITNESS: None whatsoever.

15 MR. KOTZ: Okay. And in your time at the SEC did  
16 you ever see situations where powerful influential people got  
17 preferential treatment because of their position?

18 THE WITNESS: Got preferential treatment? No, I've  
19 never seen that.

20 MR. KOTZ: When you were conducting the Madoff  
21 cause exam, was it a factor that Madoff had been an  
22 influential person who was previously head of the NASDAQ,  
23 otherwise well-known figure in the industry?

24 THE WITNESS: If it was a factor it would have been  
25 probably an opposite factor. I think a lot of people are

1 excited to work, you know, like specialists case because  
2 they're high profile. Madoff might have had -- fallen into  
3 that category.

4 MR. KOTZ: Okay. So anything else about the Madoff  
5 cause exam or Madoff investigations or otherwise relating to  
6 Bernie Madoff that we haven't asked you today that is  
7 relevant?

8 THE WITNESS: You seem pretty comprehensive, so  
9 that's all I can think of.

10 MS. STEIBER: Can we just go back to -- I think you  
11 covered this earlier -- but looking back there's nothing  
12 different that you would do in your exam if you had to do it  
13 all over again?

14 MR. COBB: Based on the same information he had at  
15 the time?

16 MS. STEIBER: Based on the same information you had  
17 at the time, is there anything different that you would wish  
18 that you had done?

19 THE WITNESS: Well, you referred to an 11-month  
20 period that -- where nothing was done, so I would like to  
21 have done something differently in regard to that, yes.

22 MS. STEIBER: What about have a closing report for  
23 the exam, would that be something that should have been in  
24 place?

25 THE WITNESS: Again, I mean, is that a do or -- is

1 that incredibly important to me at this stage whether  
2 there -- or not there's a closing report? No, it's whether  
3 or not they did a good job investigating the exam and looked  
4 for front-running aggressively. Yes, would I have liked them  
5 having a closing report? Sure, but I don't think that's  
6 demonstrative of, you know, why, you know, the results of the  
7 exam, per se. But yes, I would like that.

8 MS. STEIBER: What about make sure that they went  
9 to a third party to retrieve trading data?

10 THE WITNESS: Again, vis-...-vis the -- as I  
11 understood the exam, you know, that you'd have records in  
12 London and records in the U.S., vis-...-vis the retail shops.  
13 So getting -- I think in retrospect, getting third-party  
14 records of the London trades would have probably -- I assume  
15 they were done over-the-counter, I think there would have to  
16 have been indicia of that the records he provided us were  
17 false.

18 MS. STEIBER: But you still wish that they had  
19 requested any such records?

20 THE WITNESS: Well, again, for the retail records,  
21 getting them from the broker-deal directly makes sense to me  
22 because you need -- we would have probably needed the level  
23 of detail they provided. Yes, obviously, if there's indicia  
24 that these records could be false or falsified, yes, I would  
25 have liked to verify them with a third party.

1           But I don't think there, at the time, there was any  
2   indicia that, you know, the retail flow was false data and,  
3   in fact, it probably wasn't false data. Obviously, the  
4   London trades would have been false, from my understanding.

5           MR. KOTZ: Okay, I think that's all we have. I  
6   caution you as we've cautioned others, not to discuss your  
7   testimony with anyone else. And you signed that  
8   confidentiality agreement. And that you will get back to us  
9   on --

10          MR. COBB: I promise.

11          MR. KOTZ: -- signing your agreement, having your  
12   firm look at it. Okay? All right, we are off the record.

13          (Whereupon, at 1:10 p.m. the examination was  
14   concluded.)

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