

Rodriguez, Diane G.

From: Thanasules, Thomas
Sent: Tuesday, April 20, 2004 1:33 PM
To: Rodriguez, Diane G.

Is this just an investment?

Good afternoon Diane,

I wanted to inform you that I have started reviewing the e-mails they have provided. Certain e-mails have come to my attention that appear to raise questions regarding another entity named, Bernard L Madoff Investment Securities. ("Madoff"). As far as I know right now Madoff is a registered broker-dealer. In brief, my IA has entered into a total return swap agreement with another entity whereby one of the underlying investments is a account that appears to be managed by Madoff. As I am reviewing these e-mails there is some back and forth regarding underlying investment in the Madoff account as follows: is Investment Adviser #1's Fund of Funds vehicles)

Committee members,

We at Personal Privacy are concerned about our Personal Privacy investment. First of all, we spoke to an ex-Madoff trader (who was applying for a position at Personal Privacy and he said that Madoff cherry-picks trades and "takes them for the hedge fund". He said Madoff is pretty tight-lipped and therefore he didn't know much about it, but he didn't really know how they made money. Personal Privacy heard a similar story from from a large hedge fund consultant who also interviewed an ex-trader. The head of this well-respected group told us in confidence that he believes that Madoff will have a serious problem within a year. We are going to be speaking to him in 11 days to see if we can get more specifics.

Another point to make here is that not only are we unsure as to how Personal Privacy makes money for us, we are even more unsure as to how Personal Privacy makes money from us; i.e. why does he let us make so much money? why doesn't he capture that for himself? There could well be a legitimate reason, but I haven't heard any explanation we can be sure of. Additionally, there is a \$4 billion Madoff pass-through fund (Fairfield Sentry) that charges 0 and 20% and it's not clear why Madoff allows an outside group to make \$100 million per year in fees for doing absolutely nothing (unless he gets a piece of that). The point is that as we don't know why he does what he does we have no idea if there are conflicts in his business that could come to some regulator's attention. Throw in that his brother-in-law is his auditor and his son is also high up in the organization (imagine that!) and you have the risk of some nasty allegations, the freezing of accounts, etc., etc. To put things in perspective, if Personal Privacy went to zero it would take out 80% of this year's profits.

Perhaps the best reason to get out is that we really don't expect to make an outsized return on this investment. Sure it's the best risk-adjusted fund in the portfolio, but on an absolute return basis it's not that compelling (12.16% average return over last three years). If one assumes that there's more risk than the standard deviation would indicate, the investment loses it's luster in a hurry.

It's high season on money managers, and Madoff's head would look pretty good above Elliot Spitzer's mantle. I propose that unless we can figure out a way to get comfortable with the regulatory tail risk in a hurry, we get out. The risk-reward on this bet is not in our favor.

Please keep this confidential.

Investment Adviser #1 Portfolio Manager

Committee members,

I share the concern at [Personal Privacy] about the [Personal Privacy] investment.
Investment Adviser #1 Portfolio Manager

In []'s note, I am most worried about the new information in the statement from the ex-Madoff trader to the effect that "Madoff cherry-picks trades and 'takes them for the hedge fund'." We at [Investment Adviser #1] have totally independent evidence that Madoff's executions are highly unusual.

I do not know what to make of the consultant saying "Madoff will have a serious problem within a year."

In all, I very much agree with the sentiment "It's high season on money managers, and Madoff's head would look pretty good above Elliot Spitzer's mantle. I propose that unless we can figure out a way to get comfortable with the regulatory tail risk in a hurry, we get out. The risk-reward on this bet is not in our favor."

A last quote, from [Personal Privacy] I believe: "If you are going to panic, panic early."

Investment Adviser #1 Scientist
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Diane, these are some e-mails I have reviewed. At this point I spoke to the compliance officer regarding Madoff who informed me that they have reduced their investment in this vehicle but not due to anything referenced in the aforementioned e-mails. At this point I do not know any further details, however, I am currently putting together a request list, asking for due diligence folders, type of information they receive regarding their investment, etc.

Anyway, I will call you in a few minutes to hear your thoughts. Thank you.