

**UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK**

SECURITIES INVESTOR PROTECTION
CORPORATION,

Plaintiff,

v.

BERNARD L. MADOFF INVESTMENT
SECURITIES LLC,

Defendant.

Adv. Pro. No. 08-01789 (LGB)

SIPA LIQUIDATION

(Substantively Consolidated)

In re:

BERNARD L. MADOFF,

Debtor.

IRVING H. PICARD, Trustee for the Substantively
Consolidated SIPA Liquidation of Bernard L.
Madoff Investment Securities LLC and the Chapter 7
Estate of Bernard L. Madoff,

Plaintiff,

v.

SQUARE ONE FUND LTD.,

Defendant.

Adv. Pro. No. 10-04330 (LGB)

**TRUSTEE'S STATEMENT OF MATERIAL FACTS
IN SUPPORT OF MOTION FOR SUMMARY JUDGMENT**

Plaintiff Irving H. Picard, the trustee (“**Trustee**”) for the liquidation of Bernard L. Madoff Investment Securities LLC (“**BLMIS**”) and the substantively consolidated chapter seven estate of Bernard L. Madoff (“**Madoff**”), in support of his motion for summary judgment against defendant Square One Fund Ltd. (“**Square One**”), respectfully submits this statement of material facts for which there is no genuine issue to be tried under Local Rule 56.1 of the U.S. District Courts for the Southern and Eastern Districts of New York.

I. Background and the Trustee

1. On December 11, 2008 (the “**Filing Date**”), Madoff was arrested by federal agents for criminal violations of the federal securities laws, including securities fraud, investment adviser fraud, and mail and wire fraud. Contemporaneously, the Securities and Exchange Commission (“**SEC**”) commenced an action in the United States District Court for the Southern District of New York. Compl., *SEC v. Madoff*, No. 08-cv-10791 (LLS) (S.D.N.Y. Dec. 11, 2008), ECF No. 1.

2. On December 11, 2008, the United States government initiated a criminal action against Madoff for criminal violations of federal securities laws, including, inter alia, securities fraud, investment adviser fraud, and mail and wire fraud. Compl., *United States v. Madoff*, No. 08-mj-02735 (S.D.N.Y. Dec. 11, 2008), ECF No. 1.

3. On December 15, 2008, under 15 U.S.C. § 78eee(a)(4)(A), the SEC consented to combining its action with the action initiated by the Securities Investor Protection Corporation (“**SIPC**”). Application of SIPC at 10, *SEC v. Madoff*, No. 08-cv-10791 (LLS) (S.D.N.Y. Dec. 15, 2008), ECF No. 5. Thereafter, under 15 U.S.C. § 78eee(a)(4)(B), SIPC filed an application in the District Court alleging, among other things, that BLMIS could not meet its obligations to securities customers as they came due, and its customers needed the protections afforded by the Securities Investor Protection Act (“**SIPA**”). *Id.* at 2-3.

4. Also, on December 15, 2008, the District Court granted SIPC’s application and entered an order pursuant to SIPA, which, in pertinent part:

- i. appointed the Trustee for the liquidation of the business of BLMIS pursuant to 15 U.S.C. § 78eee(b)(3);
- ii. appointed Baker & Hostetler LLP as counsel to the Trustee pursuant to 15 U.S.C. § 78eee(b)(3); and
- iii. removed the case to the Bankruptcy Court pursuant to 15 U.S.C. § 78eee(b)(4).

Order, *SEC v. Madoff*, No. 08-cv-10791 (LLS) (S.D.N.Y. Dec. 15, 2008), ECF No. 4 (“SIPC Liquidation Order”).

5. By orders dated December 23, 2008 and February 4, 2009, respectively, this Court approved the Trustee’s bond and found that the Trustee was a disinterested person. Accordingly, the Trustee is duly qualified to serve and act on behalf of the estate. Order, *Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC*, Adv. Pro. No. 08-01789 (SMB) (Bankr. S.D.N.Y. Dec. 23, 2008), ECF No. 11; Order, *Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC*, Adv. Pro. No. 08-01789 (SMB) (Bankr. S.D.N.Y. Feb. 4, 2009), ECF No. 69.

6. On April 13, 2009, an involuntary bankruptcy petition was filed against Madoff, and on June 9, 2009, the Bankruptcy Court substantively consolidated the chapter 7 estate of Madoff into the SIPA Proceeding. Involuntary Petition, *In re Bernard L. Madoff*, No. 09-11893 (SMB) (Bankr. S.D.N.Y. Apr. 13, 2009), ECF No. 1; Consent Order, *Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC*, Adv. Pro. No. 08-01789 (SMB) (Bankr. S.D.N.Y. June 10, 2009), ECF No. 252.

II. BLMIS Operated a Ponzi Scheme Through Its Investment Advisory Business

A. BLMIS

7. In January 1960, Madoff registered as a broker-dealer with the SEC. Declaration of Bruce G. Dubinsky, dated June 11, 2025 (“**Dubinsky Decl.**”), Attach. A (Expert Report of Bruce G. Dubinsky, dated October 23, 2024 (“**Dubinsky Report**”)) ¶ 36, n.19. Madoff was assigned Registrant Number 8-8132. Through that registration, the broker-dealer became a member of SIPC when SIPA was enacted in 1970. SIPC Liquidation Order; Declaration of Marco Molina, dated June 24, 2025 (“**Molina Decl.**”), Ex. 1 (SEC Form BD for Bernard L. Madoff, Dec. 31, 1959 (PUBLIC0003607)).

8. From 1960 through January 1, 2001, BLMIS operated as a sole proprietorship. *See* Dubinsky Report ¶¶ 36, 38.

9. Effective January 1, 2001, BLMIS was registered as a New York single member limited liability company. *Id.* ¶ 38. On January 12, 2001, BLMIS amended its SEC Form BD to reflect its change in corporate form from a sole proprietorship to a single member limited liability company, and all the assets and liabilities of the sole proprietorship were transferred to the limited liability company. Molina Decl. Ex. 2 (Amended Form BD for Bernard L. Madoff, January 12, 2001) (PUBLIC0636416)); *see also* Dubinsky Report ¶ 38, n.23.

10. In response to the direction in the SEC Form BD to “[b]riefly describe details of the succession including any assets or liabilities not assumed by the successor [BLMIS],” Madoff replied:

EFFECTIVE JANUARY 1, 2001, PREDECESSOR WILL
TRANSFER TO SUCCESSOR ALL OF PREDECESSOR’S
ASSETS AND LIABILITIES, RELATED TO PREDECESSOR’S
BUSINESS. THE TRANSFER WILL NOT RESULT IN ANY
CHANGE IN OWNERSHIP OR CONTROL.

Molina Decl. Ex. 2. at PUBLIC0636424; *see also* Dubinsky Report ¶ 38, n.23.

11. Madoff further certified that no “accounts, funds, or securities of customers of the applicant are held or maintained by such other person, firm, or organization.” Molina Decl. Ex. 2. at PUBLIC0636420.

12. In 2006, BLMIS registered as an investment advisor. Dubinsky Report ¶ 39.

13. BLMIS operated three business units: (i) a proprietary trading business; (ii) a market-making business; and (iii) an investment advisory business (“**IA Business**”). *Id.* ¶ 36.

14. The proprietary trading and market-making businesses were referred to within BLMIS as “**House 5**” and are collectively referred to here as the “**Proprietary Trading Business**.” *Id.*

15. The Proprietary Trading Business operated as a securities broker-dealer, providing executions for other broker-dealers, banks, and financial institutions. *Id.* ¶ 46.

16. The market-making operations was a market maker primarily in Standard and Poor's ("S&P") 500 stocks, U.S. convertible bonds, preferred stocks, warrants, units, and rights. *Id.* and n.30.

17. The IA Business customer accounts were administered in two groups: (i) the split-strike conversion accounts; and (ii) the non-split strike conversion accounts (which included convertible arbitrage accounts). *Id.* ¶ 41.

18. The Proprietary Trading Business and the IA Business were units of BLMIS, both operated by Madoff. *Id.* ¶¶ 36, 48.

B. BLMIS Was Not Trading Securities

19. Bruce Dubinsky, a forensic accountant with more than 40 years of experience in financial fraud investigations, was retained by the Trustee as an expert witness in this matter. Mr. Dubinsky conducted numerous analyses from which he concluded that BLMIS did not conduct any trading on behalf of its IA Business customers. *See* Dubinsky Report, Section VI, A, B.

20. At various times, BLMIS reported to its IA Business customers that the money they deposited with BLMIS was invested in investment strategies called the "convertible arbitrage" strategy or the "split-strike conversion" strategy. BLMIS did not execute either strategy on behalf of its IA Business customers. *Id.* ¶¶ 19-24.

21. Mr. Dubinsky analyzed BLMIS's execution of the convertible arbitrage strategy and determined that trading never occurred dating back as far as the 1970s. *Id.* at Section VI, A(1)(a).

22. In the early 1990s, the IA Business changed its primary purported investment strategy to the split-strike conversion strategy (“**SSC Strategy**”). *Id.* ¶ 155; *see also* Section VI, A(1).

23. The SSC Strategy, as purportedly executed by BLMIS, involved (a) purchasing a basket of stocks and options based on the Standard & Poor’s (“**S&P**”) 100 equity Index; (b) selling call options on the index and buying put options to hedge against price changes in the underlying basket of stocks, *id.* ¶ 156; and (c) purchasing US Treasury bills when the IA Business purported to have closed out of its SSC strategy positions. Dubinsky Report at n.207. The SSC Strategy is a “collar strategy” designed to reduce risk caused by the volatility of the underlying stock. *Id.* ¶ 157. BLMIS did not conduct this strategy on behalf of its customers. BLMIS did not conduct this strategy on behalf of its customers.

24. Mr. Dubinsky’s analysis demonstrated that BLMIS did not conduct any trading on behalf of its IA Business customers based on (a) purported equity and option trades that exceeded the entire reported market volume for certain days; (b) hundreds of thousands of trades priced outside of the trading day’s price range; (c) the low volatility in its reported daily trading performance compared to the actual market behavior and the performance achieved by BLMIS in the Proprietary Trading Business unit as measured by the volume weighted average prices for its sales and purchases; (d) the rate of return on the purported investments reflected an abnormally high level of consistently positive yearly returns when compared with relevant market indices; (e) no records from the Depository Trust Corporation (“**DTC**”) evidencing that any legitimate trades occurred; and (f) a lack of Options Clearing Corporation (“**OCC**”) records to confirm the reported IA Business options trades. *Id.* at Section VI, A(1)(c)(i)-(v), A(1)(e)(i)-(iv).

i. Volume of Equity and Option Trades

25. Mr. Dubinsky analyzed the equity and option trades that the IA Business purportedly made in the SSC Strategy between January 2000 and November 2008. His analysis compared the daily volumes of stocks reported as purchased or sold by the IA Business on the customer statements with the actual market volumes reported by Bloomberg. *Id.* ¶¶ 159-60.

26. Between January 2000 and November 2008, Mr. Dubinsky identified 912 instances over 105 days when the IA Business's purported stock transactions exceeded the overall market volume for the day, meaning the volume that BLMIS claimed to have purchased or sold on behalf of all IA Business customers exceeded the volume of equities traded on the entire market for those days. *Id.* ¶ 159.

27. For example, on July 14, 2000, the aggregated IA Business customer statements reported purchases of 2,822,680 shares of AIG (as reflected in the column titled "IA Business Purported Volume"), but the total market volume that traded that day for all AIG shares in the market was only 1,692,800 (as reflected in the column titled "Actual Market Volume"). Similarly, the IA Business reported trading 17,709,440 shares of GE on September 13, 2000, but the total market volume that traded all day for GE shares in the market was only 7,604,800. *Id.* ¶ 159, Ex. 11 to Dubinsky Report ("Split-Strike Conversion IA Business Equity Volume Analysis, Analyzed Time Period"); *see also* Ex. 12 to Dubinsky Report ("Split-Strike Conversion IA Business Options Volume Analysis, Analyzed Time Period").

28. Mr. Dubinsky concluded that BLMIS's trading in excess of market volumes demonstrated that the IA Business did not trade on behalf of its customers. *Id.* at Section VI, A(1)(c)(i), ¶¶ 159-60, Ex. 11 and 12 to Dubinsky Report.

ii. Equity and Options Trade Prices Were Outside Daily Price Range

29. For the analyzed period of 2000-2008, Mr. Dubinsky determined that there were 99,972 equity transactions purportedly executed outside the daily market traded price range. The purported prices for these transactions exceeded the daily high price by as much as \$8.96 and were below the daily low by as much as \$105.04. There was no evidence in the BLMIS books and records that the almost 100,000 transactions were mistakes, and there were no DTC records evidencing that the trades were actually executed. Equity trades that were reported as having been executed outside the daily price range of the entire U.S. equities market could not have occurred. *Id.* ¶¶ 161-63, Ex. 13 to Dubinsky Report (“Split-Strike Conversion IA Business Equity Price Analysis, Analyzed Time Period”).

30. Mr. Dubinsky performed the same analysis on options trades for the same time period and identified 34,501 options transactions traded outside of the daily price range. He identified options that traded above the daily high price by as much as \$15.25 and below the daily price by as much by as much as \$6.05. Options purportedly executed outside the daily price range could not have occurred. *Id.* ¶¶ 164-66, Ex. 14 to Dubinsky Report (“Split-Strike Conversion IA Business Options Price Analysis, Analyzed Time Period”).

iii. Volume Weighted Average Price Analysis

31. The absence of actual trading was also evidenced by how frequently the IA Business reported purchases or sales of equity at extremely favorable prices. Mr. Dubinsky compared the trading records of the IA Business against the market-derived Volume Weighted Average Price (“VWAP”) for the respective stocks between 2000 and 2008. *Id.* ¶¶ 168-72.

32. VWAP is a trading metric that gives the average price a security has traded throughout the day, calculated based on both volume and price. VWAP is a widely used industry

metric that allows a firm to see how well its traders are doing compared to the rest of the market. *Id.* ¶¶ 168-69.

33. Based on Mr. Dubinsky's analysis, he determined that the IA Business purportedly executed 83% of the daily buy transactions by share volume below the VWAP, and 72% of the daily sell transactions by share volume above the VWAP. In other words, BLMIS bought low and sold high at a remarkably consistent rate compared to the rest of the market, which was an indication of fraud. *Id.* ¶ 170-72.

34. Mr. Dubinsky further compared the IA Business's purchase and sale of the same stock actually traded by the Proprietary Trading Business on the same days. The VWAP on the Proprietary Trading Business's traders were consistently at or near VWAP, which is consistent with actual trading. The IA Business, however, consistently outperformed VWAP by such wide margins that it evidenced the fictitious nature of the trades. *Id.* ¶¶ 171-72.

35. Mr. Dubinsky concluded that the low volatility in reported daily trading performance compared to the actual market behavior and the performance achieved by BLMIS in the Proprietary Trading Business unit as measured by VWAP demonstrated that the IA Business did not trade on behalf of its customers. *Id.* ¶¶ 170-72

iv. Annual Rates of Return

36. To further determine whether the IA Business engaged in trading, Mr. Dubinsky analyzed the volatility of the IA Business's reported average annual rate of return for the SSC Strategy as compared with the volatility of the annual rate of return as reported by Bloomberg for the two major market indices, the Standard & Poor's ("S&P") 100 Index and the Dow Jones Industrial Average (the "**Dow Jones**") from December 31, 1996 through December 11, 2008. *Id.* ¶¶ 176-79.

37. Because the SSC Strategy was supposedly engineered around the S&P 100, with a basket of stocks in the S&P 100 and using S&P Index options, the IA Business's returns should have performed similarly (i.e., related from a statistical perspective) to the returns of the S&P 100 Index. In other words, if the market goes down, the returns should have gone down and vice versa. *Id.* ¶ 175; *see also* Pomerantz Decl. Ex. A (Pomerantz Report) ¶ 318.

38. Mr. Dubinsky's analysis showed, however, that the volatility in the IA Business rates of return did not mirror the volatility of the rates of returns of the major indices. The IA Business rates of return stayed within a small range, generally between 10-12% for most years and going up to 20% for the year of 1999. *Id.* ¶¶ 177-78. The returns for the major market indices ranged from a high of 31% to a low of -37% (specifically, the S&P 100 swinging widely from a high of 31% to a low of -37%, and the Dow Jones from a high of 25% to a low of -34%). *Id.* ¶ 177.

39. While the returns available in the major indices went up and down, representing the volatility in the market, the IA Business returns stayed steady for the twelve-year period examined, never having a negative year or month (even throughout 2008). *Id.* ¶¶ 177-78.

40. Mr. Dubinsky concluded that the rate of return on the purported investments reflected a lack of volatility when compared to the relevant market indices, and the rates of returns never exhibited a negative period, which demonstrated that the IA Business was not engaged in trading. *Id.* ¶ 179.

v. Securities Listed on the IA Business Customer Statements Did Not Reconcile with DTC Records

41. Mr. Dubinsky compared the trades purportedly executed for the customer accounts in the IA Business with the records maintained by the DTC, an organization in the United States that clears and settles equity transactions in the U.S. market. *Id.* at Section VI, A(1)(e).

42. When equity trades are recorded at the DTC, this creates the official record of where that stock is held. The ownership of the stock can be confirmed with the DTC. *Id.* ¶ 192.

43. BLMIS had a single account with the DTC, the “**0646 account.**” All equity trades made by BLMIS should have been reflected in the DTC records pertaining to its account. *Id.* ¶ 207.

44. Mr. Dubinsky’s analysis confirmed that the securities that were cleared through BLMIS’s DTC account, the 0646 account, were traded by the Proprietary Trading business. No IA Business trades were cleared through BLMIS’s DTC account. *Id.* ¶¶ 207-11.

45. The Proprietary Trading Business shares reflected in the DTC records matched the BLMIS records evidencing those trades. *Id.*

46. Mr. Dubinsky concluded that the Proprietary Trading Business actually executed those trades in the marketplace, as confirmed by the DTC records. However, Mr. Dubinsky could not account for the stock purportedly traded for the customers in the IA Business in any DTC records. *Id.* ¶ 207.

47. Based on his analysis, Mr. Dubinsky concluded that the IA Business could not have legitimately executed the equity trades reflected on the customer statements. *Id.* ¶ 210.

48. Because there were no records from the DTC showing that BLMIS owned the securities listed on the IA Business customer statements, BLMIS created fake DTC records for the IA Business. Mr. Dubinsky discovered dozens of fake DTC screen inquiries to document purported trading activity of the IA Business. *Id.* ¶¶ 197-206.

49. BLMIS installed software on the IA Business computer system that recreated fake DTC reports that were meant to look like official reports. *Id.* ¶¶ 204-05.

50. Mr. Dubinsky explained that there would be no reason, if one were doing legitimate trading and had owned the stocks, to go into a computer system and write code that used form-

printing software to print out a report that mimicked what the DTC puts out, because there would instead be a real DTC report. *Id.* ¶ 206. Mr. Dubinsky made this determination by examining the metadata of the fake DTC screens, and the code embedded in the document to record characteristics of the document, including when it was created. *Id.* ¶¶ 197-203.

51. Based on Mr. Dubinsky's analysis of the DTC records, Mr. Dubinsky concluded that there was no evidence that any legitimate trades occurred on behalf of the IA Business. *Id.* ¶ 206.

vi. Reported Options Trades Could Not Be Reconciled to OCC Records

52. The options purportedly executed for the customer accounts in the IA Business could not be reconciled with the records of the OCC, an organization that clears and settles options transactions in the U.S. market. *Id.* ¶¶ 217, 220-21.

53. Mr. Dubinsky explained that BLMIS had a single account with the OCC, and the IA Business purportedly traded S&P Index options ("OEX"), which are traded exclusively on the Chicago Board of Option Exchange ("CBOE"). *Id.* ¶ 166, n.182.

54. Mr. Dubinsky reviewed the OCC records for the BLMIS account from October 31, 2002 through October 2008. *Id.* ¶ 218 and n.204. Based on his review of those records, Mr. Dubinsky was able to reconcile and confirm the options that were traded by the Proprietary Trading Business but could not account for the options purportedly traded for the customers in the IA Business. *Id.* ¶¶ 219-20. Mr. Dubinsky found that the options purportedly traded on behalf of the IA Business customers, as recorded in the IA Business trading records, were not shown on OCC records and were not cleared through the OCC. *Id.* ¶ 220.

55. For example, on October 31, 2005, records for the Proprietary Trading Business and the OCC indicate that 20 options described as "S&P 100 INDEX November 590 Call" were

purchased and held by BLMIS. The aggregate number of “S&P 100 INDEX NOVEMBER 590 CALL” options reported on IA Business customer statements for the same date totaled 658,342. *Id.* ¶ 221.

56. Based on his analyses, Mr. Dubinsky concluded that BLMIS did not conduct any options trading on behalf of its IA Business customers. *Id.* ¶ 220.

C. The IA Business Did Not Purchase Treasuries for IA Business Customer Accounts

57. In addition to purchasing stocks and options collars, BLMIS claimed it would intermittently invest IA Business customer funds in U.S. Treasury bills as part of the SSC Strategy. *Id.* ¶ 44.

58. Mr. Dubinsky found no evidence of such purchases having been made on behalf of IA Business customers. While BLMIS purchased Treasury bills with customer funds, these purchases did not match the allocation of Treasury bill transactions that appeared on customer statements. *Id.* ¶¶ 224, 230-38.

59. For the period of 2002 through 2007, Mr. Dubinsky reviewed the BLMIS books and records to identify the unique Treasury bills held by the Proprietary Trading Business on December 31 of each of those years. *Id.* ¶ 223. He then compared those holdings to (i) those Treasury bill positions held at BLMIS’s account at the DTC, which serves as the custodian or the clearing house for treasuries, and (ii) the Treasury bills purportedly held by the IA Business for its customers. *Id.* ¶¶ 224-25.

60. Mr. Dubinsky prepared a summary table of his review of these voluminous records, which accurately represents his comparison of the Treasury bill positions in the Proprietary Trading Business and the positions purportedly purchased by the IA Business for its customers:

Table 5
Comparison of Year-End US Treasury Positions:
Proprietary Trading Business vs. IA Business

Year-End	Proprietary Trading Business	IA Business	Proprietary Trading Business positions as a percent of IA Business positions
2002	\$84,000,000	\$30,975,765,000	0.27%
2003	\$70,000,000	\$33,643,020,000	0.21%
2004	\$70,000,000	\$37,935,258,000	0.18%
2005	\$75,000,000	\$40,913,910,000	0.18%
2006	\$70,000,000	\$48,342,420,000	0.14%
2007	\$80,000,000	\$56,990,055,000	0.14%

Id. ¶ 225, Table 5.

61. The amount of Treasury bills held by the Proprietary Trading Business was *de minimis* compared to those purportedly held on behalf of IA Business customers. For example, by the end of 2007, the \$80 million in Treasury positions held by the Proprietary Trading Business (as recorded on the DTC records) was only 0.14 percent of the approximately \$57 billion in Treasury positions purportedly held by the IA Business. *Id.* ¶ 225.

62. Mr. Dubinsky further analyzed whether Treasury bills purportedly purchased for IA Business customers matched those Treasury bills reported as being purchased and held by BLMIS's brokerage accounts. Mr. Dubinsky determined that 100% of the treasuries held by the brokerage accounts were not the same treasuries as purportedly held by the IA Business accounts because of different maturity dates, different purchase and sale dates, and/or they had a different reported volume. *Id.* ¶¶ 226-38.

63. Mr. Dubinsky additionally determined that even if one were to add up all of the treasuries in those eight brokerage accounts and the Proprietary Trading Business, they would be short of what was reported on the IA Business customer statements. *Id.* ¶¶ 230-31 and Fig. 36; *see*

also Ex. 22 to Dubinsky Report (“Purported IA Business Treasuries versus Actual Treasuries Held by BLMIS, December 1998 to December 2007”).

64. Frank DiPascali, a former BLMIS employee, now deceased, gave certain testimony at the multi-day criminal trial held in *United States v. Bonventre, et al.*, 10-CR-228 (LTS) (S.D.N.Y.) (“DiPascali Testimony”), ECF Nos. 858, 862, 884; also attached as Exhibits 3-5 to the Molina Declaration. In his criminal trial testimony, DiPascali confirmed that the Treasury bills purchased with the IA Business money were for BLMIS’s cash management and were not purchased for any customer account:

Q. From time to time did you get real treasury bills?

A. Yes.

Q. And what were those real treasury bills for?

A. To invest the excess cash in the IA checking account.

Q. And when you say to invest the excess cash in the IA checking account, for what reason did you get a treasury bill to do that?

A. So as to provide safety and an enhanced yield to what the checking account interest rate was.

Q. So it would be fair to say it would be a way of getting interest on the checking account?

A. More or less, yes.

Molina Decl. Ex. 3 (DiPascali Testimony) at 4931:12-23 (Dec. 5, 2013); *see also id.* at 4921:7–12, 4930:6–4931:5, 4934:3-25; Molina Decl. Ex. 4 (DiPascali Testimony) at 5345:1–5346:3 (Dec. 10, 2013).

65. DiPascali differentiated between the Treasury bills actually purchased for cash management purposes and those fabricated for customers of the IA Business:

Q. And when you bought those real treasury bills to earn interest on the Madoff checking account, what did you have to do?

A. I had to call my broker.

Q. And after you called your broker, was there a process to going out and buying the treasury bill?

A. Yeah, I would tell the broker how much dollars I wanted to commit to treasury bills and typically which one I wanted to buy, and he would take down that information and call me back and typically give me a report that I bought X amount of treasury bills at this price.

Q. And then that would – you would actually get a real treasury bill?

A. Yeah.

Q. Now, for on the IA side, when you had to provide – when you would provide the fake information, what would you do there?

A. I'd look at a pricing service of historical prices of treasury bills, ascertain the price on the date that I needed and write a ticket and put it into the AS/400.

Q. Now, what was your understanding of what Ms. Bongiorno would do with the treasury information that you gave to her?

A. She would put through a buy ticket that was approximately equal to the cash credit balance reflected in the account she was working on, and it would produce a confirmation and an entry on the customer statement that he was now – owned treasuries.

Q. And as with the other trading that was on those accounts, was any of it real?

A. No.

Molina Decl. Ex. 3 (DiPascali Testimony) at 4931:24-4932:18, 4933:4-13 (Dec. 5, 2013) (Dec. 5, 2013).

66. DiPascali further testified that the Treasury bill purchases in the eight brokerage accounts (held at Bank of New York, Bear Stearns, Fidelity, Lehman, and Morgan Stanley) were made at the direction of Mr. Madoff to earn interest on the cash held in JP Morgan Chase Bank, N.A. (“**JPMorgan**”) account #xxxxx1703 (the “**703 Account**”) (further discussed below):

Q. Did Mr. Madoff propose a solution for how to deal with this?

A. He either already had an account or two open or was about to open a new account or a series of them, I don't recall. He was basically giving that responsibility to me. He wanted treasury notes, treasury bills only. As the CDs would get unwound or, I don't remember, they might have unwound them immediately, I'm not sure, but in short order I managed a group of Bernard L. Madoff brokerage accounts that were held at other brokerage firms for the purpose of purchasing short-term U.S. government securities.

Q. These short-term U.S. securities were real, right?

A. Yes.

Q. This was just a way of getting interest on the real cash that was in the 703 account?

A. Yes.

Q. What were some of the firms that you now had responsibility for that had these brokerage accounts?

A. Bear Stearns, Fidelity, Bank of New York, Morgan Stanley, Lehman Brothers.

Q. We talked a little bit about this earlier, when you were buying these short-term securities, what steps would you have to take to buy these real securities on those brokerage accounts?

A. I typically picked up the phone and called the broker or the representative of each of those organizations and communicated my needs. Then he typically got or she typically got back to me and told me what I had done. Sometimes those conversations occurred in the form of faxes. Most of the time they were on the telephone.

Q. This was different than just looking at historical prices and writing something up for the fake trades, right?

A. Yes.

Id. at 4961:15–4962:22 (Dec. 5, 2013).

67. DiPascali explained the nuts and bolts of his process that resulted in Treasury bill transactions showing up on the IA Business customer statements, and further confirmed that they were all fake:

Q. Now can we go to the second page of this document. What is this that we are looking at?

A. It's a spreadsheet that I created that was going to be the nuts and bolts of this exercise. It was going to do a lot of the calculation for me and allow the process to progress swiftly instead of from month to month to month and client to client to client calculate all sorts of stuff, and then have to then create another side to that. This spreadsheet, which is an Excel-based spreadsheet, is identifying certain treasury bills across the top column. The top row is the CUSIP of treasury bills and options. The second row are the symbols of options and then a string of treasury bills. Going on the far left column are a string of account numbers. Those are the accounts that Bernie told us he wanted to use to be the counterparties of the customer option positions. What this is doing is it's allowing me to randomly assign, once I know the total of my customer option positions, a quantity to each of those counterparties. Then, once I've randomly defined what each counterparty's position is, this is calculating what its margin or collateral requirement would be. Once I established that, this spreadsheet allows me to randomly pick a group of treasuries that were going to represent that collateral, and then the whole total number would circle back to what I needed. It's fairly complicated, but it did all the grind work necessary to accomplish what Bernie wanted.

Q. Were any of the treasury bills that are reflected on this real?

A. No.

Id. at 5344:24–5346:3 (Dec. 10, 2013).

68. DiPascali also confirmed that the Proprietary Trading Business did not have an inventory of Treasury bills “that was equivalent to the amount that was on the statements” for IA Business customers. Molina Decl. Ex. 5 (DiPascali Testimony) at 6950:25–6951:9 (Jan. 13, 2014).

D. The IA Business Had No Other Sources of Funds

69. During at least the ten-year period before its collapse on December 11, 2008, BLMIS primarily used three bank accounts for the IA Business: the 703 Account; JPMorgan

account #xxxxxxxx1509 (the “**509 Account**”); and Bankers Trust account #xx-xx0-599 (the “**BT Account**”). Dubinsky Report ¶ 338 n.286; Declaration of Lisa M. Collura, dated June 18, 2025, Attach. A (Expert Report of Lisa M. Collura, CPA, CFE, CFF, dated January 16, 2019 (“**Collura Report**”)), ¶ 17.

70. IA Business customers’ cash deposits were deposited (and commingled) into the 703 Account. Dubinsky Report ¶ 338; Collura Report ¶¶ 20-24.

71. IA Business customer withdrawals were made through two accounts: (1) the 509 Account (funded by the 703 Account); and (2) the BT Account, which was a checking account also entirely funded by the 703 Account during the period for which bank records are available. Collura Report ¶¶ 25-30.

72. The 703 and 509 Accounts were linked commercial business accounts. The 509 Account was a controlled disbursement account that was entirely funded by the 703 Account. Collura Report ¶ 25. An analysis of the 703 Account showed that the money in that account consisted almost entirely of customer deposits. Dubinsky Report ¶ 338; Collura Report ¶ 27.

73. Ninety-seven percent of all cash additions into the 703 Account came directly from IA Business customers. Dubinsky Report ¶ 338, Fig. 52; Collura Report ¶ 24, Fig. 1.

74. The other three percent of inflows into the 703 Account came from income earned on (1) short-term investment activity made directly from the 703 Account (including overnight sweeps, overnight deposits, commercial paper, Certificates of Deposit, and Treasury bills); and (2) investments of BLMIS customer funds made through bank and brokerage accounts held in the name of BLMIS or Madoff. Collura Report ¶¶ 45, 62; Dubinsky Report ¶ 338 & n.286, Fig. 52.

75. Because the short-term investments, including overnight sweeps, were made directly out of the 703 Account, the source of the money for those investments was customer funds. Dubinsky Report ¶ 338; Collura Report ¶¶ 24, 46-48.

76. There were no inflows into the 703 Account from sales of securities for customer accounts. Dubinsky Report ¶¶ 338, 348; Collura Report ¶¶ 24, 32.

77. There were no outflows from the 703 Account to purchase securities for customer accounts. Dubinsky Report ¶ 348, Fig. 54; Collura Report ¶ 32.

78. Apart from two short-term loans BLMIS received from JPMorgan totaling \$145 million in November 2005 and January 2006—both of which were repaid by June 2006—the IA Business did not obtain loans from third parties or from the Proprietary Trading Business sufficient to pay the IA Business customer withdrawals. Dubinsky Report ¶¶ 340-42.

79. The IA Business also did not receive payments of any cash dividends. According to the customer statements, the IA Business reported that it received cash dividends related to purported trading and paid or credited them to the accountholders. Between 1998 and 2008, BLMIS reported that it had paid or credited its customers \$4.3 billion in cash dividends. *Id.* ¶¶ 245-53.

80. Of the more than 8,300 IA Business dividend transactions identified on the customer account statements from 1998 to 2008, not one purported dividend payment matched to a cash addition to the 703 Account. *Id.* ¶¶ 251-52.

81. There is no record of any dividends being received by the IA business. *Id.* ¶ 246.

82. The IA Business did not have any legitimate income-producing activities. The only source of cash available for the IA Business to pay purported investment profits as well as

redemption requests from its customers was from cash that other IA Business customers deposited in the 703 Account. *Id.* ¶¶ 328-35.

83. These transactions rendered BLMIS insolvent. As of the Filing Date, BLMIS had \$530 million in assets, and its liabilities totaled \$19.7 billion. The customer property on hand was grossly insufficient to pay the claims of BLMIS's customers. *Id.* at Section VII, ¶¶ 430-31, Table 13.

84. In December 2008, BLMIS's capital had dwindled to the point where customer redemptions or withdrawal requests grossly exceeded the amounts it had on hand. *Id.* ¶¶ 40, 438-39.

i. The Transfers Were Made by Bernard L. Madoff Investment Securities LLC

85. BLMIS operated as a sole proprietorship prior to 2001. In January 2001, the sole proprietorship was converted to a single member LLC, using the same SEC Registrant Number, 8-8132. Molina Decl. Ex. 2 (Certified amended SEC Form BD); Dubinsky Report ¶ 38, n.23.

86. From December 1998 to August 2002, the bank statements for the 703 and 509 Accounts listed the account holder as "Bernard L. Madoff." Collura Report ¶¶ 20 n.7, 25 n.9.

87. For the time period for which bank records were available (December 1998 through December 2008), the 703 and 509 Accounts were used solely for customer deposits and withdrawals—the business of the IA Business. *Id.* ¶¶ 20-27; Dubinsky Report ¶ 338 n.286, Fig. 52.

88. For the time period for which bank records were available, the face of the bank statements for the 703 Account and 509 Account showed they were designated as "Commercial Checking" accounts. The statements were addressed to the attention of either Tony Tiletnick, a BLMIS employee, or Daniel Bonventre, BLMIS's operations manager, at the BLMIS business

address at 885 Third Avenue, New York, New York. None of the statements were addressed to Madoff personally. Dubinsky Report ¶ 338, n.286, Ex. 31 and Ex. 32.

E. The Plea Allocutions

Bernard L. Madoff

89. The plea allocutions of Madoff and BLMIS employees Frank DiPascali, David Kugel, Irwin Lipkin, and Eric Lipkin, attached as Exhibits 6-11 to the Molina Decl., further establish that BLMIS did not conduct legitimate operations from its IA Business.

90. At a plea hearing on March 12, 2009, in the case captioned *United States v. Madoff*, No. 09-CR-213 (DC), Madoff pleaded guilty to an eleven-count criminal action filed against him by the United States Attorney for the Southern District of New York. Plea Allocution of Bernard L. Madoff, *United States v. Madoff*, No. 09-CR-213 (DC) (S.D.N.Y. Mar. 12, 2009) (the “**Madoff Allocution**”), ECF No. 57 (attached as Exhibit 6 to Molina Decl.).

91. At the plea hearing, Madoff admitted he “operated a Ponzi scheme through the investment advisory side of [BLMIS].” *Id.* at 23:14-23; 31:25–32:1.

92. Madoff further testified at the plea hearing that he never invested his clients’ funds in securities, that he used funds on hand in the JP Morgan account to pay customer redemptions, and that he created false trading confirmations and client account statements to cover up the fact that he had not executed trades on behalf of BLMIS investment advisory clients. Madoff stated:

The essence of my scheme was that I represented to clients and prospective clients who wished to open investment advisory and individual trading accounts with me that I would invest their money in shares of common stock, options, and other securities of large well-known corporations, and upon request, would return to them their profits and principal. Those representations were false for many years. Up until I was arrested on December 11, 2008, I never invested these funds in the securities, as I had promised. Instead, those funds were deposited in a bank account at Chase Manhattan Bank. When clients wished to receive the profits they believed they

had earned with me or to redeem their principal, I used the money in the Chase Manhattan bank account that belonged to them or other clients to pay the requested funds. The victims of my scheme included individuals, charitable organizations, trusts, pension funds, and hedge funds.

Id. at 24:9-24.

93. Beginning in the early 1990s, Madoff represented to IA Business customers that he was using a SSC Strategy based on blue-chip securities. *Id.* at 25:18-24.

94. Madoff further detailed his strategy as follows:

Through the split strike conversion strategy I promised to clients and prospective clients that client funds would be invested in a basket of common stocks within the Standard & Poor's 100 index, a collection of the 100 largest publicly traded companies in terms of their market capitalization. I promised that I would select a basket of stocks that would closely mimic the price movements of the Standard & Poor's 100 index. I promised that I would opportunistically time those purchases and would be out of the market intermittently, investing client funds during these periods in United States Government-issued securities, such as United States Treasury bills. In addition, I promised that as part of the split strike conversion strategy, I would hedge the investments I made in the basket of common stocks by using client funds to buy and sell option contracts related to those stocks, thereby limiting the potential client losses caused by unpredictable changes in stock prices. In fact, I never made those investments I promised clients, who believed they were invested with me in the split strike conversion strategy.

Id. at 25:25-26:18.

95. BLMIS investment advisory customers received account statements from BLMIS that purported to reflect securities transactions and investment returns that appeared as though their investments with BLMIS were profitable. Madoff explained:

To further cover up the fact that I had not executed trades on behalf of my investment advisory clients, I knowingly caused false trading confirmations and client account statements that reflected the bogus transactions and positions to be created and sent to clients purportedly involved in the split strike conversion strategy, as well as other individual clients I defrauded who believed they had invested in securities through me.

Id. at 27:9-16.

96. Madoff stated that the proprietary trading and market making businesses were engaged in legitimate trading. *Id.* at 25:6-11.

97. Madoff also stated that funds from his investment advisory business were transferred to the proprietary trading and market making businesses, via his affiliated London entity. *Id.* at 29:12-22.

Frank DiPascali

98. At a plea hearing on August 11, 2009, in the case captioned *United States v. DiPascali*, No. 09-CR-764 (RJS), Frank DiPascali, a former BLMIS employee, pleaded guilty to a ten-count criminal action charging him with participating in and conspiring to perpetuate the Ponzi scheme. Plea Allocution of Frank DiPascali, Jr., *United States v. DiPascali*, No. 09-CR- 764 (RJS) (S.D.N.Y. Aug. 11, 2009) (the “**DiPascali Allocution**”), ECF No. 12 (attached as Exhibit 7 to Molina Decl.). Mr. DiPascali confirmed Madoff’s explanation of the split-strike conversion strategy and that BLMIS never engaged in the strategy or executed the purported trades reported on customer statements. DiPascali stated:

By the early 1990s Bernie Madoff had stable clients whose accounts he managed as an investment adviser. He attracted a lot of these clients by telling them that the firm would apply a hedged investment strategy to their money. The clients were told that the strategy involved purchasing what we call basket of blue chip common stocks. Hedging those investments by buying and selling option contracts, getting in and out of the market at opportune times and investing in government securities at other times. . . . From at least the early 1990s through December of 2008, there was one simple fact that Bernie Madoff knew, that I knew, and that other people knew but that we never told the clients nor did we tell the regulators like the SEC. No purchases of [sic] sales of securities were actually taking place in their accounts. It was all fake. It was all fictitious. It was wrong and I knew it was wrong at the time, sir.

Id. at 45:21-46:15.

99. At the plea hearing, DiPascali testified that he had been instructed to falsely represent to clients that security trading was occurring in their investment accounts when in fact, no trades were being made. DiPascali explained:

From our office in Manhattan at Bernie Madoff's direction, and together with others, I represented to hundreds, if not thousands, of clients that security trades were being placed in their accounts when in fact no trades were taking place at all.

Id. at 46:21-25.

***Most of the time the clients' money just simply went into a bank account in New York that Bernie Madoff controlled. Between the early '90s and December '08 at Bernie Madoff's direction, and together with others, I did [the] follow[ing] things: On a regular basis I told clients over the phones and using wires that transactions on national securities exchanges were taking place in their account when I knew that no such transactions were indeed taking place. I also took steps to conceal from clients, from the SEC, and from auditors the fact that no actual security trades were taking place and to perpetuate the illusion that they actually were. On a regular basis I used hindsight to file historical prices on stocks then I used those prices to post purchase of sales to customer accounts as if they had been executed in realtime. On a regular basis I added fictitious trade data to account statements of certain clients to reflect the specific rate of earn return that Bernie Madoff had directed for that client.

Id. at 47:5-22.

... I knew no trades were happening. I knew I was participating in a fraudulent scheme. I knew what was happening was criminal and I did it anyway.

Id. at 52:2-5.

David Kugel

100. At a plea hearing on November 21, 2011, in the case captioned *United States v. Kugel*, No. 10-CR-228 (LTS), David Kugel, a former BLMIS trader and manager, pleaded guilty to a six-count criminal action charging him with securities fraud, falsifying the records of BLMIS, conspiracy, and bank fraud. Plea Allocution of David L. Kugel, *United States v. Kugel*, No. 10-

CR-228 (LTS) (S.D.N.Y. Nov. 21, 2011) (the “**Kugel Allocution**”), ECF No. 188 (Exhibit 8 to Molina Decl.).

101. As far as back as the 1970s, there is no evidence that the purported investment transactions reflected in the customer statements of BLMIS’s IA Business customers ever occurred, and in fact, the evidence reveals that those transactions did not and could not have occurred. *Id.* at 32:4-12 (“Specifically, beginning the early ‘70s, until the collapse of BLMIS in December 2008, I helped create fake, backdated trades. I provided historical trade information . . . to create fake trades that, when included on the account statements and trade confirmations of Investment Advisory clients, gave the appearance of profitable trading when in fact no trading had actually occurred.”).

Irwin Lipkin

102. At a plea hearing on November 8, 2012, in the case captioned *United States v. Irwin Lipkin*, No. 10-CR-228 (LTS), Irwin Lipkin, a former BLMIS accountant, pleaded guilty to a two-count criminal action charging him with securities fraud, falsifying the records of BLMIS, and making false statements in relation to documents required by ERISA. Plea Allocution of Irwin Lipkin, *United States v. Irwin Lipkin*, No. 10-CR-228 (LTS) (S.D.N.Y. Nov. 8, 2012) (the “**Irwin Lipkin Allocution**”), ECF No. 288 (Exhibit 9 to Molina Decl.). Mr. Lipkin admitted that BLMIS’s revenue was falsely inflated through fraudulent bookkeeping entries and annual audited reports. *Id.* at 30:23-31:3, 31:10-18, 31:24-32:5.

Eric S. Lipkin

103. At a plea hearing on June 6, 2011, in the case captioned *United States v. Eric S. Lipkin*, No. 10-CR-228 (LTS), Eric Lipkin, a former BLMIS payroll clerk, pleaded guilty to a six-count criminal action charging him with bank fraud, falsifying the records of BLMIS, conspiracy,

and making false statements to facilitate a theft concerning ERISA. Plea Allocution of Eric S. Lipkin, *United States v. Eric S. Lipkin*, No. 10-CR-228 (LTS) (S.D.N.Y. June 6, 2011) (the “**Eric Lipkin Allocution**”), ECF No. 148 (Exhibit 10 to Molina Decl.).

104. Mr. Eric Lipkin admitted that BLMIS created fake reports that replicated those of the DTC, which provides clearance for nearly all equity, bond, government securities, mortgage-backed securities, money market instruments, and over-the-counter derivative transactions in the U.S. Market. The purpose of these fake DTC reports was to purportedly confirm non-existent positions in the IA accounts, and the fake reports were given to auditors and the SEC to mislead them. *Id.* at 32:4-10, 33:22-34:8.

Enrica Cotellessa-Pitz

105. At a plea hearing on December 19, 2011, in the case captioned *United States v. Cotellessa-Pitz*, No. 10-CR-228 (LTS), Enrica Cotellessa-Pitz, a former BLMIS accountant and comptroller, pleaded guilty to a four-count criminal action charging her with conspiracy to falsify the records of BLMIS, conspiracy to obstruct the IRS in the collection of income taxes, and conspiracy to make false filings with the SEC. Plea Allocution of Enrica Cotellessa-Pitz, *United States v. Cotellessa-Pitz*, No. 10-CR-228 (LTS) (S.D.N.Y. Dec. 19, 2011) (the “**Cotellessa-Pitz Allocution**”), ECF No. 1512 (Exhibit 11 to Molina Decl.).

106. Ms. Cotellessa-Pitz admitted that IA Business customer money was funneled to BLMIS’s proprietary trading and market making businesses to falsely inflate their revenue and hide their losses. *Id.* at 31:12-32:12.

III. The Square One BLMIS IA Account

107. Square One is a BVI investment fund that was founded by Luc Estenne in 1998. Molina Decl., Ex. 12 (Square One Fund Ltd. Summary Confidential Memorandum (SQO000001347)) at SQO000001354.

108. Square One exclusively invested with BLMIS from December 15, 1998 through December 11, 2008 through investment advisory account 1FR048. Molina Decl., Ex. 13 (Transcript of Deposition of Luc Estenne (“**Estenne Tr.**”)) at 194:13-17.

109. In the Relevant Period, BLMIS transferred \$25,852,737 to Square One. Exhibit B to the Amended Complaint, ECF No. 167.

110. During the two years prior to the Filing Date, BLMIS made transfers to Square One in the amount of \$6,410,000 (the “**Two Year Transfers**”). *Id.*

111. Each of the Two-Year Transfers was made between December 11, 2006 and December 11, 2008. *Id.* ¶ 192.

112. Square One admitted to the receipt of the Two-Year transfers, that each of the Two-Year transfers was made within December 11, 2006 and December 11, 2008, and that BLMIS operated a Ponzi scheme. Amended Answer to Amended Complaint, ECF No. 240, ¶¶ 187, 192, 1.

A. Analysis of the Square One IA Business Account

113. Ms. Collura was retained by the Trustee to reconcile the cash transactions reflected on the statements of the BLMIS customer accounts with available records and trace the flow of those funds. Collura Report ¶ 7; Declaration of Lisa M. Collura, dated June 18, 2025, Attach. B (Expert Report of Lisa M. Collura, CPA, CFE, CFF, dated December 9, 2024 (“**Collura Square One Report**”)), ¶ 6.

114. For both reconciliation and tracing analyses, Ms. Collura reviewed available third-party bank records. These bank records include hundreds of thousands of pages of BLMIS bank statements, wire transfer data, cancelled checks, and deposit slips. Collura Report ¶¶ 10-12.

115. The reconciliation of the customer statements and bank records was conducted to determine whether the cash transactions on the BLMIS customer statements were accurately reflected as cash transactions—cash deposits or cash withdrawals. *Id.* ¶¶ 14-15, 31.

116. Ms. Collura confirmed that the deposit and withdrawal transactions identified on the BLMIS customer statements corresponded to transactions on the available third-party bank records in the same amount, on or around the same date, and to or for the benefit of the same customer. *Id.* ¶ 15.

117. Ms. Collura reviewed over 225,000 transactions on the customer statements, and over 150,000 transactions on the bank records. She kept track of these transactions by assigning a unique identifier to each of the cash transactions on the customer statements and a different unique identifying number to all of the transactions in the bank records. *Id.* ¶¶ 15, 31.

118. Of the over 225,000 transactions reflected on BLMIS customer statements from December 1998 to December 2008, Ms. Collura was able to reconcile 99.01% of these cash transactions to BLMIS bank records. *Id.*

119. Matthew Greenblatt oversaw the task of reconstructing BLMIS's books and records and calculating the principal balance for each BLMIS account (the "**Principal Balance Calculation**"). Mr. Greenblatt's Principal Balance Calculation applied the Net Investment Method (the Trustee's cash in/cash out net equity methodology), which takes into account all of the customer deposits or inter-account transfers of principal as additions to principal and all of the customer withdrawals or inter-account transfers as reductions to principal. Declaration of Matthew

B. Greenblatt, dated June 11, 2025 (“**Greenblatt Decl.**”), Ex. A (Expert Report of Matthew G. Greenblatt, CPA/CFF, CFE dated November 15, 2012 (“**Greenblatt Report**”)) ¶¶ 4-5; *see also Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC (In re Bernard L. Madoff Inv. Sec.)*, 424 B.R. 122 (Bankr. S.D.N.Y. 2010) (“**Net Equity Decision**”).

120. Mr. Greenblatt prepared a chronological listing of cash and principal transactions reflected in the BLMIS customer statements. Mr. Greenblatt relied on the customer statements because they are the most comprehensive and complete accounting of the debtor’s books and records with respect to transaction-by-transaction line-item detail of the cash and principal transactions and because the customer statements were sent to customers, giving customers the opportunity to correct errors on the statements. Greenblatt Report ¶¶ 10-12, 40-43.

121. The first monthly customer statement which reported dollar amounts for any securities allegedly held at month end was March of 1981. Therefore, the full period in which the Principal Balance Calculation could be performed covered the time period from April 1, 1981 through December 11, 2008. *Id.* ¶ 5 n.1.

122. For Ms. Collura’s reconciliation analysis with respect to Square One, she analyzed the cash transactions in the Square One Account from February 1999 to December 2008. During this time period, the customer statements for the Square One Account reflected 50 cash deposit and withdrawal transactions. All 50 cash transactions reflected on the customer statements for the Square One Account occurred in the ten-year period, December 1999 to December 2008 for which there were available BLMIS bank records. Collura Square One Report ¶¶ 13, 15-20, Exs. 3, 6.

123. She reconciled all of the 50 cash transactions reflected on the customer statements for the Square One Account to available BLMIS bank records, documentation contained in BLMIS

customer files, and/or documents produced to the Trustee related to the Square one Account. *Id.* ¶¶ 14, 21-22.

124. Based on her review of documents contained in the customer file maintained at BLMIS for the Square One Account, Ms. Collura did not find any instance of Square One communicating to BLMIS any disagreement with respect to the accuracy of any cash transaction reflected on the customer statements for the Square One Account. *Id.* ¶¶ 19, 22.

125. For Ms. Collura's tracing analysis with respect to Square One, she analyzed the cash withdrawals from the Square One Account during the two years prior to December 11, 2008 (the "**Two-Year Period**"), totaling \$6,410,000. *Id.* ¶ 23-26.

126. Based on available bank records from BLMIS, she traced 100% of the total amount of cash withdrawals reflected on the customer statements for the Square One Account during the Two-Year Period to a bank account held by Square One. *Id.* ¶ 27, Exs. 5 & 6.

127. For Mr. Greenblatt's analysis with respect to Square One, his Principal Balance Calculation covered the period from the Square One Account opening through December 11, 2008. Greenblatt Decl., Ex. B (Expert Report of Matthew B. Greenblatt, CPA/CFF, CFE dated December 9, 2024 ("**Greenblatt Square One Report**")) ¶¶ 4, 7-22.

128. Mr. Greenblatt determined that on February 1, 1999, the Square One Account had its first transaction of a cash deposit via check wire in the amount of \$2,000,000, all representing principal. *Id.* ¶ 11, Ex. 4.

129. Subsequent to this initial cash deposit, there were 20 additional cash deposits via wires into the Square One Account in the aggregate amount of \$26,097,165, all representing principal. *Id.* ¶ 12, Ex. 4.

130. In sum, these 21 cash deposits provided the Square One Account with a total of \$28,097,167 of principal. *Id.* ¶ 13, Ex. 3.

131. Between February 1, 1999 and December 11, 2008, the Square One Account reflected a total of 29 cash withdrawals totaling \$25,757,791. *Id.* ¶ 14, Ex. 4.

132. The Principal Balance Calculation for the Square One Fund Account demonstrates that between February 1, 1999 and December 11, 2008, of the \$28,097,165 of principal available in the account, \$25,852,737 was withdrawn (\$25,757,791 withdrawn in cash and \$94,946 withheld by BLMIS and paid to the IRS prior to January 1, 2003). *Id.* ¶¶ 14-19, Ex. 4.

133. As a result, the remaining principal balance of the Square One Fund Account, as of December 11, 2008, was \$2,244,428. Of the \$25,852,737 cash withdrawals, a total amount of \$6,410,000 was withdrawn within the two-year period prior to December 11, 2008. *Id.* ¶ 14-19, Ex. 4.

IV. Square One Was Run and Controlled by Luc Estenne and Partners Advisers

134. Luc Estenne (“**Estenne**”) is a Belgian national and well-known investment management professional in Switzerland. Molina Decl., Ex. 13 (Estenne Tr.) at 36:20-24.

135. At all relevant times, Estenne was Square One’s director, investment manager, and principal and was Square One’s primary contact person with BLMIS. Molina Decl., Ex. 14 (ART Fund Abbreviated Unaudited Semi-Annual Report for Dec. 27, 2000 to June 30, 2001 (10-04330_ART_0000007)).

136. Estenne created and runs Partners Advisers S.A. (“**Partners Advisers**”), an investment advisory firm in Geneva, Switzerland. Estenne was Director of Partners Advisers at all relevant times. *Id.*

137. Estenne also created and controlled Square Asset Management, Ltd. (“SAM”), Square One’s investment manager. Molina Decl., Ex. 13 (Estenne Tr.) at 196:9-20; Ex. 15 (Square Asset Management Ltd. Written Resolution, Sept. 28, 2006 (SQO000000605)).

138. SAM delegated its duties vis-à-vis Square One to Partners Advisers. Molina Decl., Ex. 16 (Email from Luc Deblue to Timothée Henry, Apr. 26, 2006 (SQO000002453.C0001)).

A. Luc Estenne Was a Sophisticated Investor—Known for His Rigorous Due Diligence Standards

139. Prior to establishing Square One and Partners Advisers, Estenne worked within the financial sector:

- i. From 1991 to 1993, Estenne worked for JP Morgan Bank’s Global Technology and Operation group in Brussels. Molina Decl., Ex. 17 (Partners Advisers Website (PUBLIC0622535)) at PUBLIC0622555.
- ii. From 1994 to 1996, Estenne was an officer of Bank Brussels Lambert in New York and Brussels, trading proprietary capital. Molina Decl., Ex. 18 (Square One Summary Confidential Memorandum (FADSAD0005900)) at FADSAD0005914.
- iii. Estenne’s LinkedIn profile states that some of his “[s]pecialties” are “[h]edge fund research and management of portfolios of hedge funds” and “[g]eneral management of a hedge fund research and advisory company.” Molina Decl., Ex. 19 (LinkedIn Profile of Luc Estenne (PUBLIC0622561)) at PUBLIC0622561.

140. In 1998, Estenne founded his family office, Partners Advisers. Since its inception, Estenne has been the CEO of Partners Advisers. Molina Decl., Ex. 13 (Estenne Tr.) at 36:11-14, 40:13-15.

141. Partners Advisers is and has at all times been known for its rigorous due diligence process and conservative approach to selecting investments:

- i. Partners Advisers was named Switzerland’s “Most Trusted Investment Management Company of the Year” in the 2014 International Hedge Fund Awards. Molina Decl., Ex. 20 (2014 Hedge Fund Awards Brochure (PUBLIC0627814)) at PUBLIC0627870.

- ii. Partners Advisers materials tout a comprehensive due diligence process and “deep understanding” of markets and securities, including “face-to-face meetings” and ongoing monitoring of the performance of each investment. Molina Decl., Ex. 17 (Partners Advisers Website (PUBLIC0622535)) at PUBLIC0622549–50.

142. In 2000, Estenne authored a book chapter titled “Risk Management Issues for the Family Office” in the book “Managing Hedge Fund Risk” in which he, among other things, teaches investors how to avoid investing in a fraud. Molina Decl., Ex. 21 (Luc Estenne, Risk Management Issues for the Family Office, in *Managing Hedge Fund Risk: From the Seat of the Practitioner—Views from Investors, Counterparties, Hedge Funds and Consultants* (Parker ed., 2000) (PUBLIC0615798)).

143. Estenne authored a second version of this book chapter in 2005 (collectively, the 2000 and 2005 versions of this chapter are referred to as the “**Chapter**”). Molina Decl., Ex. 22 (Luc Estenne, Risk Management Issues for the Family Office, in *Managing Hedge Fund Risk: Strategies and Insights from Investors, Counterparties, Hedge Funds and Regulators* (Parker ed., 2005) (PUBLIC0619484)).

144. In the Chapter, Estenne advises:

- i. The custodian of an investment fund should be independent from the investment adviser to maintain the security of the assets and ensure that they are valued accurately, including that independent custody “ensures control of assets, independent [net asset value] calculations and accuracy of financial statements.”
- ii. That it is “paramount” that investors conduct both pre- and post-investment due diligence on investment advisers “to identify which risks are taken by hedge fund managers in order to generate their performance, and how these risks are measured and managed.”
- iii. That there are 30 risk factors that investors should study as part of their diligence of investment advisers and strategies. These risk factors include counterparty risk, correlation risk, assets under management risk, concentration risk, erratic markets risk, and transparency.
- iv. That investors should demand transparency from their investment adviser, including that the “best transparency level usually available takes the form of

monthly or quarterly portfolio snapshots,” and encouraging investors to conduct periodic in-person diligence visits to obtain “a vote of confidence on the ethics” of the investment adviser.

Molina Decl., Ex. 21 (PUBLIC0615798) at PUBLIC0615803–808; Ex. 22 (PUBLIC0619484) at PUBLIC0619494–99.

145. In March 1998, Estenne spoke on a panel outlining pointers for hedge fund managers, which emphasized that “[t]ransparency, both of the portfolio and the manager, remain critical issues.” A writeup of the panel quoted one of the panelists stating that “[i]f a fund manager will not tell you what he is doing, you have to question what you are doing investing with him.” Molina Decl., Ex. 23 (Article, *Transparency and Administration Are Key* (PUBLIC0637965)).

146. Estenne participated at industry conferences as a panelist where he lectured about the importance of transparency when evaluating an investment adviser, how to conduct investment due diligence, and how to identify and mitigate investment risk. *Id.*

147. In April 2001, at the International Private Banking & Family Office conference in Brussels, Estenne gave a presentation titled “Why do Family Offices Invest in Hedge Funds?” that included topics such as “How to select hedge funds” and “How to construct hedge funds.” Molina Decl., Ex. 24 (International Private Banking & Family Office Brochure (PUBLIC0637950)) at PUBLIC0637952.

148. In 2004, Estenne spoke as a “due diligence specialist[]” at the EuroHedge summit in Paris on issues such as “Hot to spot fraud?”, “Why do funds fail?”, “What is the psychology behind manager impropriety?” and “What are the structural issues?”. Molina Decl., Ex. 25 (EuroHedge Brochure (PUBLIC0619460)) at PUBLIC0619461.

149. A Lloyd’s Bank due diligence questionnaire, filled out by Partners Advisers in 2004, identified Partners Advisers’ capabilities and comprehensive due diligence approach, including a process that “includes a review of all organization/structure risks and all

strategy/portfolio risks” and “also includes at least one on-site visit, a review of the strategy, portfolio management, risk management, backgrounds, organization, compliance, third parties, fund structure, investment conditions. Reference checks on the principals are made as well to insure good quality and morality of the manager.” Molina Decl., Ex. 26 (Lloyds Bank Due Diligence Questionnaire (SQO000018127)) at SQO000018152–53.

150. Jérôme Müller, Partners Advisers’ CIO, testified that Partners Advisers regularly undertook extensive investment and due diligence, including:

- i. Sourcing potential investment ideas with and from the investment community Molina Decl., Ex. 27 (Transcript of Deposition of Jérôme Müller (“**Müller Tr.**”)) at 140:20-141:16;
- ii. Visiting managers face-to-face before and after the investment is made (*id.* at 150:7-19) and verifying checks and balances on managers (*id.* at 94:6-19);
- iii. Written reports following meetings with investment managers (*id.* at 167:21-23, 182:10-19);
- iv. Reviewing audit reports (*id.* at 98:11-13);
- v. Speaking with the fund’s custodian (*id.* at 98:14-17);
- vi. Conducting quantitative due diligence, including analyzing the track record alongside the strategy (*id.* at 99:15-100:10) and analyzing quantitative due diligence factors, such as the R-squared coefficient, beta, alpha, Sharpe ratio, and Sortino ratio (*id.* at 110:14-21);
- vii. Conducting qualitative due diligence, including understanding the strategy (*id.* at 102:7-11); and
- viii. Conducting monthly investment committee meetings to examine portfolios line by line (*id.* at 202:12-23, 203:1-4).

151. Estenne testified that due diligence is important to assess the risk of fraud: “If you can obviously meet the manager, it's better because then you have kind of a feel for the person. If you can't, either you meet his representative, you can have also a kind of subjective assessment of the quality of the organization, of the risk related to the organization, things like that.” Molina Decl., Ex. 13 (Estenne Tr.) at 112:13-20.

B. Partners Advisers Managed Square One's Day-to-Day Activities

152. Neither Square One nor its investment manager, SAM, had any employees. *Id.* at 160:11, 196:09-12.

153. Estenne and Partners Advisers managed Square One's day-to-day activities. *Id.* at 196:07-20.

154. In a May 17, 2005 email, Timothée Henry stated, on behalf of Partners Advisers, that "[t]he name of the fund that 'we' manage is Square One." Molina Decl., Ex. 28 (Email from Timothée Henry to Carol Correia, May 17, 2005 (SQO000003147)).

155. Communications with BLMIS for or on behalf of Square One were sent on Partners Advisers letterhead. Molina Decl., Exs. 29 (Partners Advisers Fax to DiPascali, March 15, 1999 (SQO000000461)); 30 (Partners Advisers Fax to DiPascali, undated (SQO000011014)); 31 (Partners Advisers Fax to DiPascali, Jan. 25, 2000 (SQO000018750)); 32 (Partners Advisers Letter to Madoff, Oct. 12, 2000 (SQO000000477)).

156. Partners Advisers employees carried out tasks for and on behalf of Square One. Examples include:

- i. Timothée Henry sent copies of Square One's board resolutions. Molina Decl., Ex. 33 (Email from Timothée Henry to Katie Brey, Estenne, and others, Dec. 16, 2008 (SQO000006981));
- ii. Luc Estenne, Timothée Henry, and Luc Deblue communicated concerning Square One's offering materials (Molina Decl., Ex. 34 (Email from Luc Deblue to Estenne and Timothée Henry, Apr. 26, 2006 (SQO000002444)));
- iii. Luc Estenne, Timothée Henry, and Luc Deblue worked with Square One's service providers—Bank of Bermuda and Circle Partners—regarding Square One Fund (Molina Decl., Exs. 35 (Emails among Estenne, Timothée Henry, and Paul Smith (SQO000004698)); 36 (Emails among Timothée Henry, Luc Deblue, and Pieter-Jan van der Pols (SQO000002560)); 37 (Emails among Estenne, Timothée Henry, Luc Deblue, and Andrew Yonda (SQO000014311.C0001)));

- iv. Timothée Henry and Luc Estenne authorized redemption requests for Square One (Molina Decl., Exs. 38 (Emails between Timothée Henry and Andrew Yonda, Nov. 25, 2005 (SQO000006031)); 39 (Emails from Timothée Henry to Maxine Trott, Dec. 3, 2004 (SQO000006726)); and
- v. Jérôme Müller circulated Square One quantitative information. Molina Decl., Ex. 40 (Email from Müller to Estenne, Sept. 30, 2003 (SQO000016006)).

157. Throughout the relevant time period, Partners Advisers authored over one hundred Summary Reports on behalf of Square One that, like the Estenne Study, analyzed Square One's performance against the S&P 500 Index (*see, e.g.*, Molina Decl., Exs. 41 (Partners Advisers Summary Report, July 1989 through Apr. 2003 (SQO000013986)); and 42 (Partners Advisers Summary Report, July 1989 through Aug. 2003 (SQO000016001)); over one hundred Portfolio Performance Rankings comparing funds including Square One based on performance rankings, portfolio returns, portfolio correlations, and portfolio risk-reward profiles (*see, e.g.*, Molina Decl., Exs. 43 (Portfolio Performance Rankings, Jan. 1999 through Dec. 2003 (SQO000001904)); and 44 (Portfolio Performance Rankings, Jan. 1999 through Nov. 2003 (SQO000003617)); and quantitative analysis factsheets analyzing Square One against the S&P 500 Index (*see, e.g.*, Molina Decl., Exs. 45 (Quantitative Analysis Factsheet, July 1989 through Jan. 2003 (SQO000001376))—most of which include Partners Advisers branding.

158. While Partners Advisers was managing Square One, it was aware of and actively monitoring the Bayou Fund fraud. A report that Partners Advisers received and reviewed acknowledged that “[t]hey were highly secretive about how the firm worked. Our partnership was kind of a separate thing but we were never really allowed to observe or look at the books or at anything the Bayou Fund or Bayou Securities did.” Molina Decl., Ex. 46 (Email from Randy Shain to Jérôme Müller with attachments, Sept. 29, 2005 (SQO000013396)) at SQO000013415.

V. Square One Was Aware of Red Flags and Concerns with BLMIS

159. In February 1999, Estenne had an in-person meeting with Frank DiPascali. Molina Decl., Ex. 47 (Potential Manager Meeting Report, Feb. 8, 1999 (SQO000000149)).

160. Handwritten notes from a March 1998 meeting with DiPascali show that Madoff wanted to “keep a low profile.” Molina Decl., Ex. 48 (Handwritten Notes, Mar. 4, 1998 (SQO000012498)) at SQO000012500.

161. These handwritten notes also show that Estenne and DiPascali discussed that the SSC Strategy should produce returns that are correlated to the S&P 100, noting “portfolio to keep high correlation with the index.” *Id.* at SQO000012498.

162. Square One opened account 1FR048 at BLMIS on December 29, 1998. Molina Decl., Ex. 13 (Estenne Tr.) at 133:03-13.

163. Estenne met with Madoff in February 2000. Molina Decl., Ex. 49 (Letter from Estenne to Madoff, Feb. 11, 2000 (SQO000011170)).

164. Estenne met with BLMIS personnel—including DiPascali and Madoff—several times throughout the life of Square One’s IA Account. Molina Decl., Ex. 13 (Estenne Tr.) at 257:11-13.

A. Square Knew that BLMIS Did Not Allow Diligence Questions

165. From the outset of Square One’s relationship with BLMIS, Estenne knew that Madoff would not answer questions concerning the operations at BLMIS. Estenne believed that, if he pressed the issue or asked questions, Madoff would terminate the investment. *Id.* at 257:20-23; 260:2-4; 287:20-21.

166. Square One believed investing with BLMIS was a “take it or leave it” situation. *Id.* at 258:19-21.

167. Square One understood “that it was not possible to ask many questions about the strategy” *Id.* at 260:2-4.

168. Square One believed its investors considered it “a favor to be investors into the strategy, which makes it difficult to inquire further about the details of the strategy.” *Id.* at 261:10-16.

B. BLMIS Lacked the Typical Transparency Provided by Investment Advisers

169. Square One’s June 1999 Offering Memorandum and Exhibit A to the Offering Memorandum describe the SSC Strategy in detail. Molina Decl., Ex. 18 (Square One Summary Confidential Memorandum (FADSAD0005900)).

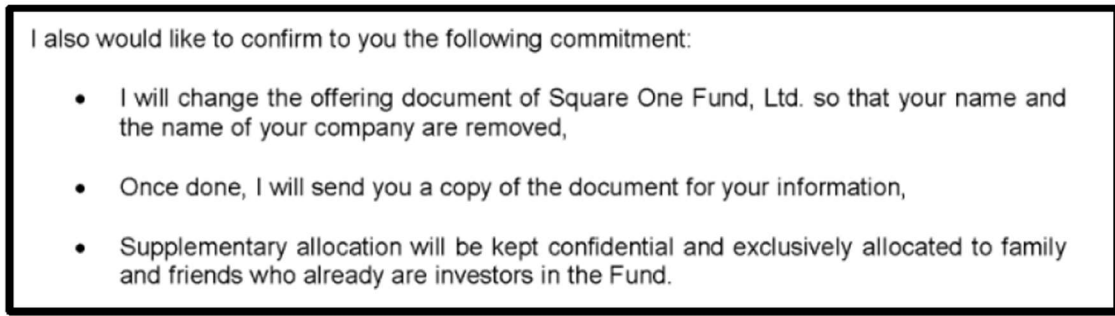
170. Square One’s June 1999 Offering Memorandum and Exhibit A list BLMIS as the investment adviser and state that “[t]he Fund’s investment objective is to provide investors with access to the trading strategy of Madoff securities.” *Id.* at FADSAD0005906.

171. In December 1999, DiPascali informed Estenne that Madoff demanded that Square One remove all mention of BLMIS from the Offering Memorandum. Estenne responded in a fax, apologizing and agreeing to remove BLMIS from the offering memorandum: “I didn’t know Bernard didn’t want to see the name of the company in the private offering memorandum. I have never been told so and regret any convenience it might have create[ed]. I am ready to correct what you want.” Molina Decl., Ex. 50 (Fax from Estenne to DiPascali, Dec. 13, 1999 (SQO000018820)).

172. Estenne testified that he “received a call from Bernie Madoff after the formation of Square One at the time when Square One Fund's document mentioned his name or the name of his company specifically, that he was pissed off about the fact that his name was mentioned, that he

told me that this was creating some problem for him, and that he --and, accordingly, he asked me to remove the name from the documents.” Molina Decl., Ex. 13 (Estenne Tr.) at 182:16-25.

173. Estenne also confirmed directly with Madoff in a fax that he would remove any reference to Madoff or BLMIS from the offering documents:



Molina Decl., Ex. 49 (Letter from Estenne to Madoff, Feb. 11, 2000 (SQO000011170)).

174. Square One then removed all references to BLMIS and Madoff from its offering documents, as demonstrated in the redline of Square One’s offering memorandum attached hereto as Molina Decl., Ex. 51 (Redline of Summary Confidential Memorandum, Oct. 1, 2000 (SQO000011174)) at SQO000011179, SQO000011181, SQO000011189–92.

175. From that day, Square One did not disclose BLMIS or Madoff on any of its offering documents. Molina Decl., Ex. 52 (Square One Table of Issues and Resolutions SQO000002544.C0001)) at SQO000002544.C0005.

176. Square One recognized that BLMIS’s lack of transparency was problematic. In the June 2000 Investment Manager Information report on BLMIS, Square One concluded that “[t]here is a lack of transparency issue and the mystery about his abilities to generate such consistent returns with such a simplistic strategy.” Molina Decl., Ex. 53 (Partners Advisers Investment Manager Information on BLMIS (SQO000011351)) at SQO000011354.

177. In April 2006, Square One’s new administrator, Circle Partners, proposed including Madoff in updated offering materials. Luc Deblue, Partners Advisers’ Risk Manager, responded

that Circle Partners was not to disclose Madoff as the custodian in the offering materials. Molina Decl., Ex. 52 (Square One Table of Issues and Resolutions SQO000002544.C0001)) at SQO000002544.C0005.

178. Square One was concerned about BLMIS's irregular operations and memorialized its concerns in numerous reports:

- i. In a May 26, 2004 Manager Monitoring Report on BLMIS, Square One concluded that a "concern which is nothing new is the lack of separation of functions as Madoff Investment Securities is its own broker, prime brok[er], custodian and administrator." Molina Decl., Ex. 54 (Partners Advisers Manager Monitoring Report on BLMIS, May 26, 2004 (SQO000017481)) at SQO000017481.
- ii. On a June 28, 2000 Investment Manager Information sheet on BLMIS, Square One concluded that negative points included: (i) "lack of independence in the NAV calculation"; (ii) "potential conflict of interest as Madoff as a broker, an investment adviser[] and a custodian"; and (iii) "dependent board of directors." Molina Decl., Ex. 55 (Partners Advisers Investment Manager Information on BLMIS (SQO000011351)) at SQO000011358.
- iii. In a February 1999 Potential Manager Meeting Report, Square One concluded that "[t]he only dark cloud is the potential credit risk we could face as the assets are deposited at Madoff." Molina Decl., Ex. 47 (Potential Manager Meeting Report, Feb. 8, 1999 (SQO000000149)) at SQO000000149.

C. Square One Was Aware of the Lack of Correlation and Trading Anomalies

179. Estenne, on behalf of Square One, analyzed Square One's performance compared to the S&P 500 Index (the "**Estenne Studies**"). Pomerantz Report ¶¶ 88, 320, n.286, n.320; Molina Decl., Ex. 55 (Partners Advisers Summary Report, July 1989 to Oct. 1999 (FADSAI0005930)).

180. This same analysis was run over different time periods, in subsequent versions by Estenne and Partners Advisers. *See* Pomerantz Report Sec. VI; *see also* ¶¶ 89, 121, 198, 237, 313, 320 & n.371-74, n.97, Figs. 28, 49; Molina Decl., Exs. 45 (Quantitative Analysis Factsheet, July 1989 through Jan. 2003 (SQO000001376)); 56 (Summary Report, July 1989 to Nov. 2003 (SQO000003952)); 57 (Partners Advisers Summary Report, July 1989 to Oct. 2003

(SQO000004122_R)); 58 (Square One Analysis, Feb. 1999 to June 30, 2003 (SQO000016757)); and 59 (Square One Analysis, Feb. 19, 1999 to Feb. 28, 2003 (SQO000005410)).

181. The December 2002 Estenne Study analyzed 43 months—from June 1999 to December 2002—where the S&P 500 incurred losses 58% of the time (25 out of 43 months) while the Square One BLMIS Account reflected losses approximately 2% of the time (1 out of 43 months). Molina Decl., Exs. 45 (Quantitative Analysis Factsheet, July 1989 through Jan. 2003 (SQO000001376)); Pomerantz Decl. Ex. A (Pomerantz Report) at ¶¶ 120-22, Fig. 5.

182. The Estenne Studies showed there was little to no correlation between the SSC Strategy and the S&P 500 Index. Pomerantz Report Sec. VI(D)(4); Molina Decl., Ex. 55 (Partners Advisers Summary Report, July 1989 to Oct. 1999 (FADSAI0005930)).

183. The Estenne Studies demonstrated that the SSC Strategy consistently outperformed the S&P 500. Pomerantz Report ¶¶ 237-39.

Figure 28
Excerpt from November 2003 Estenne Study
Cumulative Monthly Returns of Square One v. S&P 500
(June 1999 – November 2003)²³⁴
(purple line is Square One, blue line is S&P 500)



Molina Decl., Ex. 56 (Summary Report, July 1989 to Nov. 2003 (SQO000003952)) at SQO000003954.

184. The Estenne Studies included a “Returns Analysis” that showed BLMIS only posted four negative monthly returns from 1991 – 1998. The Returns Analysis demonstrates a lack

of correlation between BLMIS's purported returns and the S&P 500 Index—particularly in August 1998 where the S&P 500 Index posted a loss of 14.58% and Square One posted a gain of 0.28% and in March 1994 where the S&P 500 Index posted a loss of 4.57% and Square One posted a gain of 1.52%. Molina Decl., Ex. 55 (FADSAI0005930) at FADSAI0005933. The SSC Strategy should have produced returns that were correlated (i.e., related from a statistical perspective) to the returns of the underlying stock or the S&P 100 Index as the returns should have moved in the same direction as the underlying stock or Index. Pomerantz Report ¶ 318.

<u>1991</u>	<u>Jan</u>	<u>Feb</u>	<u>Mar</u>	<u>Apr</u>	<u>May</u>	<u>Jun</u>	<u>Jul</u>	<u>Aug</u>	<u>Sep</u>	<u>Oct</u>	<u>Nov</u>	<u>Dec</u>	<u>YTD</u>
Fund	3.08%	1.46%	0.59%	1.39%	1.88%	0.37%	2.04%	1.07%	0.80%	2.82%	0.08%	1.63%	18.58%
Index	4.15%	6.73%	2.22%	0.03%	3.86%	-4.79%	4.49%	1.96%	-1.91%	1.18%	-4.39%	11.16%	26.30%
<u>1992</u>													
Fund	0.49%	2.79%	1.01%	2.86%	-0.19%	1.29%	0.00%	0.92%	0.40%	1.40%	1.42%	1.43%	14.67%
Index	-1.99%	0.96%	-2.18%	2.79%	0.10%	-1.74%	3.94%	-2.40%	0.91%	0.21%	3.03%	1.01%	4.48%
<u>1993</u>													
Fund	0.00%	1.93%	1.86%	0.06%	1.72%	0.86%	0.09%	1.78%	0.35%	1.77%	0.26%	0.45%	11.68%
Index	0.70%	1.05%	1.87%	-2.54%	2.27%	0.08%	-0.53%	3.44%	-1.00%	1.94%	-1.29%	1.01%	7.06%
<u>1994</u>													
Fund	2.18%	-0.36%	1.52%	1.82%	0.51%	0.29%	1.78%	0.42%	0.82%	1.88%	-0.55%	0.66%	11.49%
Index	3.25%	-3.00%	-4.57%	1.15%	1.24%	-2.66%	3.15%	3.76%	-2.69%	2.08%	-3.95%	1.23%	-1.54%
<u>1995</u>													
Fund	0.92%	0.76%	0.84%	1.69%	1.72%	0.50%	1.08%	-0.16%	1.70%	1.60%	0.51%	1.10%	12.95%
Index	2.43%	3.61%	2.73%	2.80%	3.63%	2.13%	3.18%	-0.03%	4.01%	-0.50%	4.10%	1.74%	34.11%
<u>1996</u>													
Fund	1.49%	0.73%	1.23%	0.84%	1.41%	0.22%	1.92%	0.27%	1.22%	1.10%	1.57%	0.48%	12.98%
Index	3.26%	0.69%	0.79%	1.34%	2.29%	0.23%	-4.57%	1.88%	5.42%	2.61%	7.34%	-2.15%	20.27%
<u>1997</u>													
Fund	2.45%	0.73%	0.86%	1.17%	0.63%	1.34%	0.75%	0.35%	2.39%	0.56%	1.56%	0.42%	14.01%
Index	6.13%	0.59%	-4.26%	5.84%	5.86%	4.35%	7.81%	-5.74%	5.32%	-3.45%	4.46%	1.57%	31.02%
<u>1998</u>													
Fund	0.91%	1.29%	1.75%	0.42%	1.76%	1.26%	0.83%	0.28%	1.04%	1.93%	0.84%	0.37%	13.45%
Index	1.02%	7.04%	4.99%	0.31%	-1.88%	3.94%	-1.16%	-14.58%	6.24%	8.03%	5.91%	5.64%	26.67%

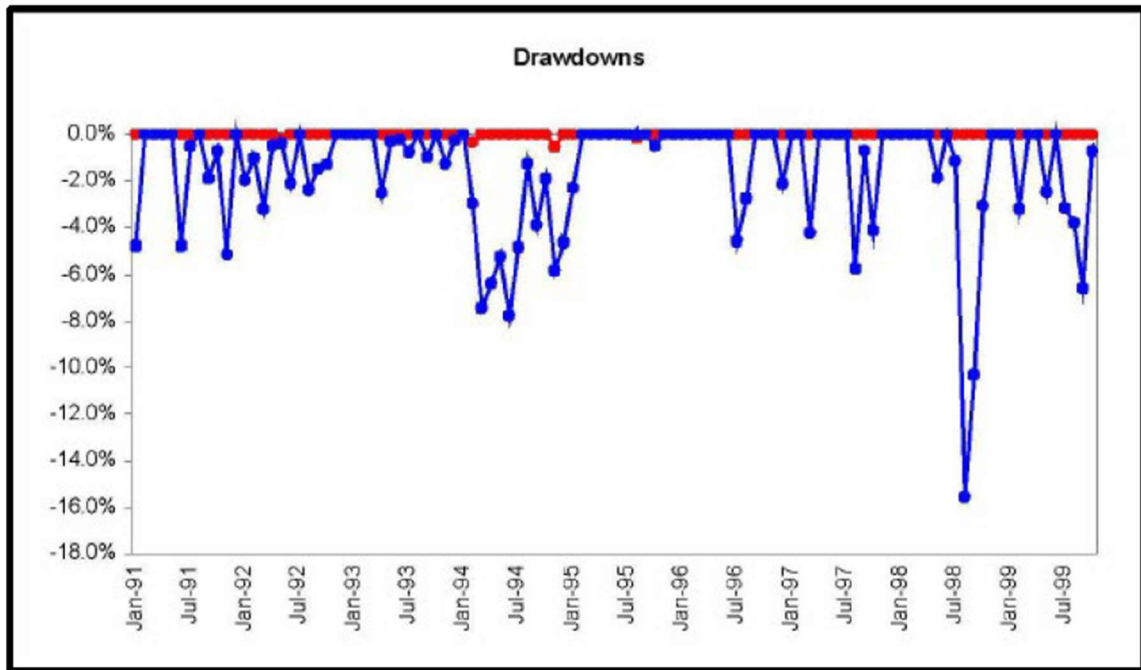
Id.

185. A subsequent analysis, covering the time period between 1999 through 2003, shows that BLMIS posted only five negative monthly returns. The lack of correlation was particularly evident in September 2002 when the S&P 500 Index posted a loss of 11% and Square One posted a gain of 0.12%, and in September 2001 when the S&P Index posted a loss of 8.17% and Square One posted a gain of 0.77%:

<u>1999</u>	<u>Jan</u>	<u>Feb</u>	<u>Mar</u>	<u>Apr</u>	<u>Mai</u>	<u>Jun</u>	<u>Jul</u>	<u>Aug</u>	<u>Sep</u>	<u>Oct</u>	<u>Nov</u>	<u>Dec</u>	<u>YTD</u>
Fund						3.97%	0.31%	1.21%	0.82%	1.40%	1.87%	0.34%	10.31%
Index						5.44%	-3.20%	-0.63%	-2.86%	6.25%	1.91%	5.78%	12.86%
<u>2000</u>													
Fund	2.62%	0.04%	2.15%	0.33%	1.60%	0.60%	0.68%	1.44%	0.17%	1.17%	0.53%	0.40%	12.34%
Index	-5.09%	-2.01%	9.67%	-3.08%	-2.19%	2.39%	-1.63%	6.07%	-5.35%	-0.49%	-8.01%	0.41%	-10.14%
<u>2001</u>													
Fund	2.62%	0.05%	1.02%	1.23%	0.27%	0.80%	0.35%	1.15%	0.77%	1.50%	1.37%	0.16%	11.86%
Index	3.46%	-9.23%	-6.42%	7.68%	0.51%	-2.50%	-1.08%	-6.41%	-8.17%	1.81%	7.52%	0.76%	-13.04%
<u>2002</u>													
Fund	-0.14%	0.58%	0.71%	0.97%	2.76%	0.24%	3.43%	0.37%	0.12%	0.77%	0.04%	0.02%	10.26%
Index	-1.56%	-2.08%	3.67%	-6.14%	-0.91%	-7.25%	-7.90%	0.49%	-11.00%	8.64%	5.71%	-6.03%	-23.37%
<u>2003</u>													
Fund	-0.47%	-0.10%	2.45%	-0.01%	0.93%	1.32%	1.69%	0.20%	1.13%	1.66%	-0.25%		8.84%
Index	-2.74%	-1.70%	0.84%	8.10%	5.09%	1.13%	1.62%	1.79%	-1.19%	5.50%	0.71%		20.28%

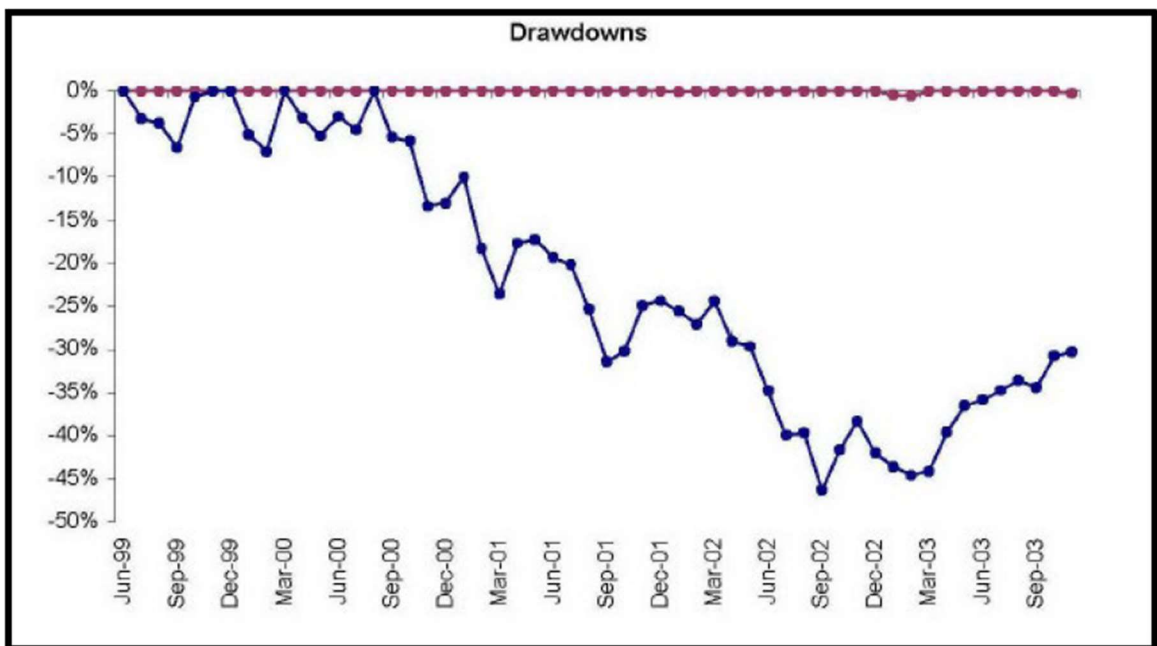
Molina Decl., Ex. 56 (Summary Report, July 1989 to Nov. 2003 (SQO000003952)) at SQO000003955.

186. The Estenne Study also included a “Drawdowns” graph which further demonstrates the lack of correlation between BLMIS’s performance (the red line) and the S&P 500 Index (the blue line):



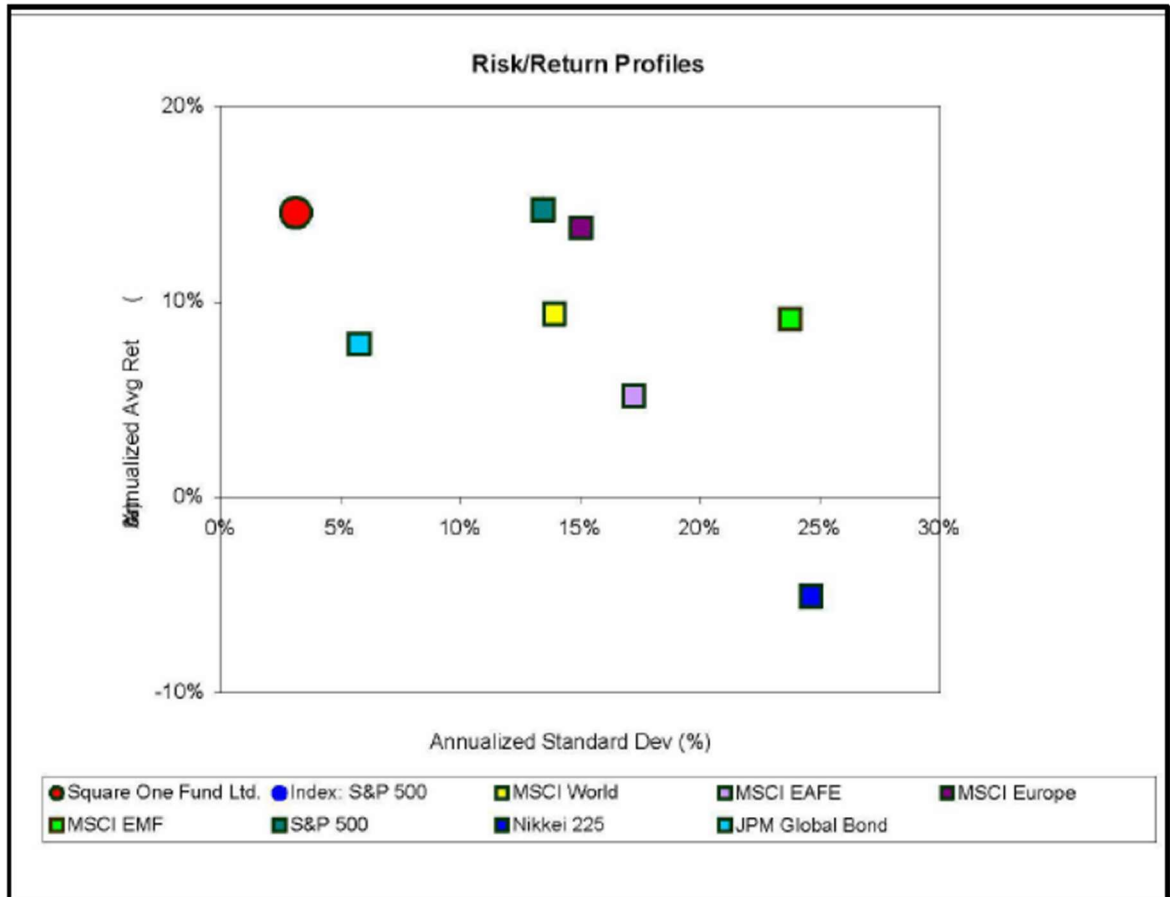
Molina Decl., Ex. 55 (Partners Advisers Summary Report, July 1989 to Oct. 1999 (FADSAI0005930)) at FADSAI0005934.

187. The drawdowns graph in the subsequent studies showed similar lack of correlation:



Molina Decl., Ex. 56 (Summary Report, July 1989 to Nov. 2003 (SQO000003952)) at SQO000003956.

188. The Estenne Study also analyzed the correlation between investment performance and investment risk for the SSC Strategy and seven different indices. The red circle represented Square One, which had a lower risk profile and larger return profile than any of the other indices:



Molina Decl., Ex. 55 (Partners Advisers Summary Report, July 1989 to Oct. 1999 (FADSAI0005930)) at FADSAI0005931.

189. In the June 2000 Investment Manager Information report on BLMIS, Square One concluded that there was a “mystery about [Madoff’s] abilities to generate such consistent returns with such a simplistic strategy.” Molina Decl., Ex. 53 (Partners Advisers Investment Manager Information on BLMIS (SQO000011351)) at SQO000011355.

190. When looking at one of the analyses that tracked Square One's performance from February 1999 through August 2003, Müller testified that the S&P performance from 1999-2003 "wasn't very good"—"negative, actually," which covered "the bursting of the tech bubble, so the markets were in a bear market." Molina Decl., Exs. 27 (Müller Tr.) at 302:1-7; and Ex. 40 (Email from Müller to Estenne, Sept. 30, 2003 (SQO000016006)) at SQO000016007.

191. Müller stated that despite the poor market conditions and lackluster performance of the S&P 500, Square One's performance was "pretty steady" with no downward returns. Molina Decl., Ex. 27 (Müller Tr.) at 302:11. Regarding the correlation factor, Müller testified, "there was no way we could explain Madoff's return." *Id.* at 304:18.

192. Müller further testified that it would have been "impossible" for Madoff or anyone else to time the market this well for so long, concluding that the only possibility was that Madoff was cheating in some way. *Id.* at 126:08-127:05.

193. Partners Advisers had a Julius Bär due diligence report on Fairfield Sentry. This report was unable to reconcile BLMIS's purported execution of the SSC Strategy with the returns:

- i. "a timing risk may occur if the long put and long stock positions are not put on or unwound at the same time."
- ii. "If all the strategy's assets are invested at the same time, exposures to single stocks can become very sizeable, causing a liquidity risk."

Molina Decl., Ex. 60 (Julius Bär Due Diligence Report, Mar. 28, 2000 (SQO000012465)) at SQO000012466, SQO000012469.

D. Partners Advisers Becomes Concerned that BLMIS Was a Fraud

194. In 2002, Partners Advisers, conducted a diligence review of two BLMIS feeder funds on behalf of the Absolute Return Target ("ART") Fund, a Luxembourg investment fund that Partners Advisers created and managed to offer their customers a portfolio of investments that

Partners Advisers had hand selected and in which Estenne and Partners Advisers' customers were invested. Molina Decl., Ex. 27 (Müller Tr.) at 227:8-25, 228:1-11, 254:19-25, 255:1-3.

195. During a 2010 interview with OpalesqueTV, Estenne explained that the partners at Partners Advisers were co-invested in all Partners Advisers investments, explaining that “the idea is putting our money where our mouth is and gain credibility by investing together and investing better on behalf of our core investors.” OpalesqueTV, *Luc Estenne: Family Offices and Hedge Funds*, YouTube (October 18, 2010), <https://www.youtube.com/watch?v=nXo9Yo5xjTU>); see also Molina Decl., Ex. 27 (Müller Tr.) at 66:22-67:1.

196. From 2000 to 2002, the ART Fund's investment portfolio included Square One, which was one of the portfolio's best-performing funds. Müller Tr. at 289:5-19.

197. In or around August 2002, Partners Advisers conducted due diligence on two other BLMIS feeder fund to identify potential new investments and to inquire further into its concern—from its oversight of Square One's performance, that BLMIS's purported returns did not correlate with the market. *Id.* at 254:19-255:1-3.

198. During this time, there was a bear market in the wake of the burst in of the dot.com bubble and the 9/11 attacks, yet BLMIS purported to post consistently positive returns. Molina Decl., Ex. 56 (Summary Report, July 1989 to Nov. 2003 (SQO000003952)) at SQO000003955.

199. Partners Advisers' diligence employee, Jérôme Müller, was tasked to carry out this diligence into BLMIS feeder funds. One of these feeder funds was Fairfield Sentry, which is apparent based on an itinerary from Fairfield Greenwich Group's Stephane Muuls. The itinerary includes a meeting between Muuls and Müller on August 29, 2002:

Geneva 29/08/02 0830: Equitas Charles Ioas 21, rue du Rhône 1204 Geneva T: 41 22 318 59 34
1000: Partners Advisers Jérôme Müller 12, rue François Bonivard 1201 Geneva T: 41 22 716 00 60

Molina Decl., Ex. 61 (Meeting Itinerary, FG-05223996).

200. In his email summarizing the meetings in Switzerland, Muuls states he met with Müller. Molina Decl., Ex. 62 (Stephane Muuls Email, Sept. 10, 2002 (FG-05223991)).

201. The other BLMIS feeder fund with which Müller met was Kingate Global. Molina Decl., Ex. 27 (Müller Tr.) at 235:11-13.

202. The BLMIS feeder fund representatives that he consulted told Müller that BLMIS's consistently positive returns were generated by random market-timing, which concerned Müller because he understood that "[m]arket timing doesn't work" given that it is "impossible to forecast where the market is going, repeatedly." *Id.* at 126:6-18.

203. Müller was not able to explain why Madoff had good market timing, he had never "seen a manager who was successful in predicting what the markets would do on a regular basis." *Id.* at 126:08-18; 126:19-127:05.

204. Müller came away from this diligence convinced that BLMIS was not executing the SSC Strategy because "there was no way to explain how the returns were generated" under that Strategy. *Id.* at 283:10-17.

205. Müller understood that the SSC Strategy was supposed to correlate closely with the S&P 500 but, in reality, BLMIS's reported returns had little-to-no correlation with that index. *Id.* at 238:20-240:23; 304:13-25.

206. Müller tested his conclusions with trusted investment professionals within his network, who agreed that BLMIS's purported strategy and returns that BLMIS's operations were likely illegal. *Id.* at 234:09-23; 214:04-243:04.

207. Some of these individuals told Müller they believed that BLMIS was "front-running" by using nonpublic information from its market-making business to assist the trades made by its IA Business; a practice that Müller understood to have been "illegal" in the United States. *Id.*

208. According to Müller, "the belief in Geneva was that [Madoff] was using information from his market-making business, to take position in the hedge fund with, sort of, the knowledge of where the market was going because he saw the volume in the option business, right. So that was sort of the common belief in Geneva back in the day, and everybody was sort of . . . thinking that this was the case." *Id.* at 241:9-17.

209. One of these investment professionals in Müller's network was Albert Collette, a Geneva-based investment manager. Collette stated that "[y]ou could not have a conversation of more than one minute on the subject of Madoff without people talking to you about fraud." Molina Decl., Ex. 63 (Transcript of Examination of Albert Collette ("**Collette Tr.**")) at 16:6-8, 7:30-37.

210. Collette likened investing in Madoff to the Tour de France: "There were teams that were doped and teams that weren't. Madoff was the doping." *Id.* at 7:30-37. Müller agreed with Collette's analogy. Molina Decl., Ex. 27 (Müller Tr.) at 251:3-7.

211. When Collette and Müller spoke, they discussed “how to explain the returns, since we were all having that discussion and no one had an answer to that question.” Molina Decl., Ex. 63 (Collette Tr.) at 7:36-37.

212. Müller came away with these discussions convinced that BLMIS’s IA Business’s “return stream was impossible to explain” unless BLMIS had been engaging in illegal activity. Molina Decl., Ex. 27 (Müller Tr.) at 259:18-19.

213. Based on his diligence, Müller ultimately concluded that BLMIS’s investment advisory business was “*too good to be true*.” Molina Decl., Ex. 64 (Emails between Timothée Henry and Masha Johnson (SQO00000)); and 27 (Müller Tr.) at 272:1-273:4.

214. There were concerns among Partners Advisers personnel that Madoff was front-running. According to Müller, Estenne was not very concerned about the possibility of the illegal activity of front-running because it would have created criminal liability only for Madoff, not for Estenne. Molina Decl. Ex. 27 (Müller Tr.) at 256:7-25.

215. Estenne corroborated Müller’s testimony and admitted that he did not list the potential for front-running as a cause for concern in due diligence reports or notices that were sent to investors. Molina Decl., Ex. 13 (Estenne Tr.) at 275:9-16.

E. Jérôme Müller Confronted Luc Estenne with His Concerns about BLMIS

216. Following his review, Müller reported his conclusion that BLMIS’s purported investment strategy could not generate BLMIS’s purported returns and that none of what BLMIS reported appeared to add up. Molina Decl., Ex. 27 (Müller Tr.) at 254:22-255:1-3; 272:13-273:04.

217. Müller also recommended to Estenne that, based on those opinions, Partners Advisers should remove Square One from its portfolio (in which Estenne and Müller personally invested). Molina Decl., Exs. 26 (Lloyds Bank Due Diligence Questionnaire (SQO000018127)) at

SQO000018130; 28 (Müller Tr.) at 65:9-66:8; and 13 (Estenne Tr.) at 49:25-50:6, 228:5-8, 285:14-21. Additionally, Partners Advisers was Estenne’s corporate brand, and he wanted to shield it from potential harm. *Id.*, Ex. 17 (Partners Advisers Website (PUBLIC0622535)).

218. Müller also recommended that Estenne should implement a “no Madoff policy” at Partners Advisers. Molina Decl., Exs. 27 (Müller Tr.) at 257:14–262:25; and 13 (Estenne Tr.) at 222:02–228:12.

219. This was not the first time that Estenne had been warned that Madoff was a fraud. In the late 1990s, Fletcher repeatedly warned Estenne that BLMIS was “a fraud.” Molina Decl., Exs. 65 (Emails between Estenne and Peter Fletcher, Dec. 12, 2008 (SQO000007155)); and 66 (Transcript of Examination of Peter Fletcher (“**Fletcher Tr.**”)) at 85:22-86:2.

220. Peter Fletcher is a Canadian national who worked in Geneva as the CEO of Parly Company, a company that shared office space with Partners Advisers. *Id.* at 33:2-9; Molina Decl., Ex. 27 (Müller Tr.) at 38:4, 39:1-5.

221. Fletcher spoke regularly with Estenne and Müller in the late 1990s and early 2000s on potential investments. Molina Decl., Ex. 66 (Fletcher Tr.) at 77:14-25, 81:5-13.

222. Fletcher testified that he believed since the 1990s that Madoff was involved in more than simply front-running. *Id.* at 41:2-6, 69:3-11, 70:18-20. Fletcher reviewed information on BLMIS Feeder Funds, Fairfield Sentry and Kingate, concluding that the information “didn’t look right.” According to Fletcher, it “didn’t take much to figure out” that “their strict split-strike conversion just didn’t work.” *Id.* at 41:2-6, 69:3-11, 70:18-20.

223. Fletcher opined that Madoff was doing something to “jack up” the returns, especially when the market was performing poorly. *Id.* at 69:15-21.

224. Fletcher identified issues with BLMIS including:

- i. that it would have been impossible for BLMIS to trade the size of assets that it was purporting to trade, concluding that “they couldn’t have done the trades . . . because there wasn’t the volume on the stock exchange There’s no way in hell [that BLMIS could have done those trades.]” *Id.* at 44:24-47:10.
- ii. that “[s]egregation of assets is the most important thing to [him]” because investors want “an independent custodian third party to monitor the investments.” Yet with BLMIS “[a]nybody[with] half a brain” would be able to confirm that BLMIS held all the assets without any meaningful third-party supervision. *Id.* at 27:17-28:1-18, 55:7-11.
- iii. that it was concerning to him that the feeder funds’ documents “strip[ped] Madoff’s name from” their offering materials because it meant auditors would not have the ability to look into BLMIS’s operations. *Id.* at 59:23-60:5.
- iv. that he had never seen a manager charge no fees, so it was suspicious for an “investment manager in New York” not to do so. *Id.* at 41:7-10.

225. Estenne acknowledged in his deposition that Fletcher had shared these concerns with him during the relevant period. Molina Decl. Ex. 13 (Estenne Tr.) at 291:9-12.

226. Following the exposure of BLMIS’s fraud, Fletcher emailed Estenne saying “[a]lways knew this is a fraud, is [*sic*] only taken 15 years.” To which, Estenne replied “Yes, patience is a virtue!” Molina Decl., Ex. 65 (Emails between Estenne and Peter Fletcher, Dec. 12, 2008 (SQO000007155)).

F. After Learning of Müller’s Concerns, Estenne Directed Partners Advisers to Divest Its Holdings from Square One

227. The ART Fund included Square One in its portfolio in December 2000 until the position was redeemed in the fall of 2002. Molina Decl., Ex. 67 (ART Fund Quarterly Review, Oct. to Dec. 2002 (SQO000000906)) at SQO000000909.

228. During that time, Square One was one of the ART Fund’s best-performing investments. Molina Decl., Exs. 68 (Portfolio Performance Rankings, Jan. 1999 to Sept. 2003

(SQO000004214)); and 69 (Portfolio Performance Rankings, Jan. 1999 to Sept. 2003 (SQO000004222)).

229. The ART Fund redemption was ordered on October 31, 2002, approximately two months after Müller conducted due diligence on BLMIS. Molina Decl., Exs. 70 (Various ART Fund Documents (10-04330_ART_0000375)) at 10-04330_ART_000039.

230. While Square One was performing well for the ART Fund during the bear market of the early 2000s, the ART Fund divested from Square One because “there are important conflicts of interests [with respect to BLMIS], as the manager is his own custodian and values the portfolio himself. To avoid any other blow ups, the position has been redeemed.” Molina Decl., Ex. 71 (ART Fund Quarterly Review, Oct. to Dec. 2002 (SQO000000995)) at SQO000000999.

231. When asked about his and Estenne’s decision to drop Square One from the ART Fund portfolio in 2002, Müller testified that he was concerned with the irregular operations at BLMIS, explaining that “Madoff was the custodian of his own assets, which was a lack of segregation of duties, which was also an issue with the firm.” Molina Decl., Ex. 27 (Müller Tr.) at 283:10-17.

232. Estenne agreed with Müller’s assessment, testifying that “Partners Advisors [*sic*]— had decided to redeem from its investment in Square One through ART because of the lack of segregation of these different functions.” Molina Decl., Ex. 13 (Estenne Tr.) at 246:3-11.

233. Estenne testified that Partners Advisers decided to drop Square One from the ART Fund portfolio in 2002 following Bristol’s “fraudulent activity” and “blow up.” Additionally, “[i]t was decided by Partners Advisers that Partners Advisers would refrain from investing in funds where the – there was a significant what’s called fat tail, meaning that there was a possibility of a

very significant loss due to either, you know, leverage or the behavior of the instrument included in the strategy. That would be one.” *Id.* at 220:11-223:2.

234. Once the ART Fund redeemed its investment in Square One, there were no investments in BLMIS for or on behalf of Partners Advisers. *Id.*

G. Estenne Blacklisted Any Partners Advisers Investment Into BLMIS

235. Estenne decided to blacklist any investments in Madoff at Partners Advisers and imposed a “no Madoff policy” due to the perceived concerns:

Q: And after you became the head of research, you had more—I think you said earlier you had more of a voice?

A: Yes.

Q: So your opinion had more significance?

A: Yes.

Q: And at that point, what was your – as head of research, what was your policy with respect to investing in Madoff or Madoff feeder funds?

A: Well, the policy was that he wasn’t going to get into our portfolios.

Q: With respect to this, is it fair if I call it – refer to it on the record, for the purpose of this, a “no Madoff policy”? Is that fair?

A: Yeah. As far as I was concerned, yes.

Molina Decl., Ex. 27 (Müller Tr.) at 259:12-260:9.

236. In response to a questionnaire from a potential investor, Partners Advisers reply that the ART Fund “is not and never will be invested in Madoff.” Molina Decl., Ex. 26 (Lloyds Bank Due Diligence Questionnaire (SQO000018127)) at SQO000018156.

9. Is the fund invested in Madoff? If so, please provide percentage per fund.

No. The fund is not and never will be invested in Madoff.

237. Partners Advisers’ decision to not invest in BLMIS was reiterated in a March 16, 2006 email from Jérôme Müller to Luc Deblue, stating that Partners Advisers would “absolutely

not!” invest in a Madoff feeder fund. Molina Decl., Ex. 72 (Emails between Estenne and Müller, Mar. 16, 2006 (SQO000013895.C0001) at SQO000013895.0002.

238. Following Madoff’s arrest, Henry sent emails confirming Partners Advisers’ “no Madoff” policy:

- i. December 15, 2008 email to Masha Johnson stating that “Jerome consistently refuted any proposal to invest in Madoff. He always said it was too good to be true.” Molina Decl., Ex. 64 (Emails between Timothée Henry and Masha Johnson (SQO000006939)).
- ii. December 16, 2008 email to Philip Craig stating that “Jerome our CIO always refused to invest in Madoff. He always believed there were too many risks involved.” Molina Decl., Ex. 73 (Emails between Timothée Henry and Philip Craig, Dec. 16, 2008 (SQO000015057)) at SQO000015057.
- iii. December 17, 2008 email to Otto Nilssen stating that “Jerome was always against it and we were not invested.” Molina Decl., Ex. 74 (Emails between Timothée Henry and Otto Nilssen, Dec. 18, 2008 (SQO000015045.C0001)) at SQO000015045.0001.
- iv. Undated letter to Partners Advisers co-investors stating “none of the hedge fund portfolios we manage or advise have any holdings in any funds related to Bernard Madoff. We were prevented from considering an investment by the lack of transparency and certain conflict of interests present at Madoff Securities.” Molina Decl., Ex. 75 (Partners Advisers Letter to Co-Investors (SQO000007277)).

H. Estenne Memorialized His Concerns Surrounding Madoff in Emails to Other Investment Professionals in His Network

239. In March 2003, Estenne emailed Carlo Luigi Grabau of Alena Financial Services, attaching the 2001 articles from MarHedge and Barron’s which detail the secrecy surrounding Madoff and skepticism towards Madoff’s performance. Molina Decl., Ex. 76 (Email from Estenne to Carlo Luigi Grabau, Mar. 14, 2003 (SQO000000836)).

240. In May 2003, Estenne asked an unrelated investment professional, Theo Nijssen, a series of due diligence questions for Madoff in advance of Nijssen’s meeting with BLMIS:

Dear Theo,

Please find here the questions for Madoff:

Could you confirm to me that the strategy you implement is exclusively a split strike convergence strategy?

Professional money managers specialized in index and volatility trading do not understand how you can produce such a regular and smooth performance.

Could you explain to me what are your competitive advantages which would explain this regularity?

How can you assure us that there is a Chinese wall between your asset management and market making activities?

What is the structure of depositaries used i.e. do you use any sub-custodian and who ultimately holds the assets that are deposited with you?

What is the best answer you could give to someone who is uncomfortable about the non segregation of functions between, the manager, the market-maker, the administrator and the depositary?

Molina Decl., Ex. 77 (Emails between Estenne and Theo Nijssen, May 9, 2003 (SQO000004980)).

241. In October 2008, a friend of Estenne, Catherine Lemaitre asked him about the risks of investing with Madoff. Estenne responded:

The main risks are as follows:

- Investment professionals do not understand how with such a simple strategy, such a stable track record can be generated,
- No separation between asset management, brokerage, custodian and administration functions,
- Asset size unknown but in theory sufficient to significantly influence the equity derivatives market,
- Potential risk of front running?
- No access to management teams or on-site due diligence capacity to fully understand the strategy.

Please do not send this email in its written form.

Molina Decl., Ex. 78 (Emails between Estenne and Catherine Lemaitre, Dec. 12, 2008 (SQO000007076.C0001)) at SQO000007076.0001.

242. Two months later, after BLMIS's fraud became public, Lemaitre replied to Estenne "we can say that you had warned me" *Id.*

I. Estenne Continued Funneling Institutional Investors into Square One, Despite the No Madoff Policy at Partners Advisers

243. Despite the "no Madoff" policy at Partners Advisers, Estenne continued soliciting investments into Square One up until 2008, when the fraud was exposed. Molina Decl., Ex. 13 (Estenne Tr.) at 264:5-23.

244. Estenne did not share his BLMIS-related concerns with the Square One investors because he believed that they already "were aware of the positives and the negatives of the strategy, and were ready to take the risks related to these positives and these negatives." *Id.* at 264:5-23.

245. Estenne's solicitations included representations that Square One "is the kind of fund that should be in every fund of funds" and that BLMIS's SSC Strategy "is almost risk free investing." Molina Decl., Ex. 79 (Partners Advisers Investment Manager Information for BLMIS (SQO000004728)) at SQO000004729, SQO000004732.

246. Despite the concerns raised by Müller and Estenne, and Estenne's decision to blacklist any Partners Advisers investment in BLMIS, Estenne was reaping the benefits—collecting 1.25%-2% annualized fees on Square One's investments—with no personal exposure. Molina Decl., Ex. 18 (Square One Summary Confidential Memorandum (FADSAD0005900)) at FADSAD0005910-11.

VI. The Trustee's Red Flags Expert, Dr. Pomerantz, Concluded that the Red Flags Would Have Prompted a Reasonable Investor in Square One's Shoes to Divest from Square One or, at a Minimum, Conduct Additional Due Diligence on BLMIS

247. Dr. Steve Pomerantz, an economic and financial expert, was retained by the Trustee as an expert witness in this matter. Dr. Pomerantz conducted numerous analyses from which he

concluded that due diligence performed on, and information otherwise available regarding BLMIS and Madoff revealed numerous red flags relating to Square One's BLMIS account 1FR048. Pomerantz Report ¶ 2.

248. Dr. Pomerantz reviewed and analyzed: (i) documents exchanged between the Trustee, the Defendant and third parties related to this proceeding; (ii) customer statements, trade confirmations, and other related BLMIS documentation and data; (iii) the purported trading activity in the Square One BLMIS Account; (iv) testimony obtained through discovery in this proceeding; and (v) publicly available information including market data and fund databases. *Id.* ¶ 5.

249. Dr. Pomerantz stated that the primary goal of any investment is “to maximize reward while simultaneously limiting risk, including the risk of theft or fraud. In order for market participants to achieve that goal, they must perform due diligence.” *Id.* ¶ 37.

250. Dr. Pomerantz's analysis concluded that Square One had information and documents sufficient to perform due diligence analyses to confirm that Madoff could not have generated the returns he claimed using the Madoff SSC strategy. *Id.* ¶ 34.

251. Dr. Pomerantz concluded that Square One performed and reviewed contemporaneous due diligence analysis of Square One's BLMIS account while invested with BLMIS that revealed numerous red flags or “doubts or concerns regarding the investment opportunity” concerning Madoff and his purported strategy. *Id.* at ¶ 34.

252. In the investment industry, a “red flag” means “information that raises doubt or concern regarding an investment opportunity and can include: (i) any inconsistencies with industry customs and practices; (ii) any indications that the advisor is not executing the strategy; (iii) any inconsistencies with the stated strategy; (iv) any potential changes in the advisor and/or his

organization, investment process, or philosophy; (v) any situations that create an opportunity for fraud; (vi) any indicia of fraud or changes to the risk profile of the invested assets; and (vii) any impossibilities where the only reasonable explanation is fraud.” *Id.* ¶ 59. When a red flag is uncovered, it is industry custom to conduct additional diligence to further investigate. *Id.* ¶¶ 64-65, 70.

253. According to industry custom, if the only reasonable explanation is fraud the custom is to end the inquiry and refuse to invest:

When a red flag is an indicia of fraud or creates an opportunity for fraud, it is industry custom and practice for the fund manager to perform additional due diligence to ferret out whether the indicia of or opportunity for fraud leads to another red flag. Similarly, when red flags are uncovered that indicate the advisor is not executing or is operating inconsistent with the stated strategy, it is industry custom and practice to perform additional due diligence to determine whether the information leads to another red flag. If due diligence identifies a significant red flag where the only reasonable explanation is fraud, a fund manager would typically stop the due diligence process and not invest or redeem their investments. It is not necessary to perform each and every due diligence activity if a single activity reveals a significant red flag where the only reasonable explanation is fraud

Id. ¶ 70.

254. Based on Dr. Pomerantz’ review of the documents and information available to Square One and in the record, Dr. Pomerantz’ analyses and experience, and industry customs and practices, there were numerous quantitative and qualitative red flags that would have tipped off Square One—had Square One properly been conducting due diligence and looking into Madoff consistent with industry customs and practices. *Id.* at Sec. VI, ¶¶ 342.

255. To the extent that Square One sought to salvage its investment in BLMIS, Dr. Pomerantz concluded that Square One should have at a minimum performed additional due

diligence including confronting BLMIS about the apparent red flags that suggested fraud. *Id.* at ¶¶ 64-70.

A. Process: Due Diligence on Madoff's SSC Strategy Identified Numerous Red Flags

256. Dr. Pomerantz reviewed BLMIS's purported investment strategy, the SSC Strategy, including the purported use of a collar. "By way of the collar, the put option should have created a floor for the returns and the call option should have created a ceiling. The put options would create a floor on losses but could not turn losses into gains." Pomerantz Report ¶¶ 98-104, Figs. 3, 4.

B. Process: Due Diligence on Madoff's Service Provider Identified Numerous Red Flags

257. BLMIS served as investment advisor for the Square One Account, as well as operating as its own broker-dealer, custodian, and administrator. *Id.* ¶ 108.

258. Square One was aware of BLMIS's numerous roles as broker-dealer, investment advisor, custodian, and administrator. This was raised by Square One, and Estenne agreed that the more checks and balances on a manager, the lower the likelihood that the manager would conduct fraud on an investment. *Id.* ¶¶ 108, 111, 114, 116.

259. Dr. Pomerantz concluded that Madoff serving as his own broker-dealer, custodian, and administrator was a red flag since it was inconsistent with industry customs and practices. Further, the lack of independent verification created an opportunity for fraud. *Id.* ¶ 109, 116.

260. BLMIS's auditor, Friebling & Horowitz was a firm with one active accountant that did not have adequate audit support for a firm the size BLMIS purported to be. *Id.* ¶¶ 117-18.

261. In 2001, BLMIS publicly estimated an assets under management ("AUM") of as much as \$7 billion. According to Dr. Pomerantz, it is a red flag for a fund this size to not have a well-known, well-established, and well-equipped auditor. It is inconsistent with industry customs and practices and created an opportunity for fraud. *Id.* ¶ 119.

C. Process: Due Diligence on the Implementation of Madoff's SSC Strategy Identified Numerous Red Flags

a. No Downside Risk

262. In Madoff's SSC Strategy, Madoff purported to select a basket of stocks from the S&P 100. As a result of this stated strategy, Madoff's position should have moved with the overall S&P 100. However, Square One's returns did not move in the same direction as the S&P 100—instead it consistently outperformed the market. *Id.* ¶ 120.

263. Square One was aware of, and raised on multiple instances, the issue of consistent positive returns. *Id.* ¶ 124. This concern was also raised by a 2001 Barron's article titled "Don't Ask, Don't Tell: Bernie Madoff is so secretive, he even asks investors to keep mum," which Estenne forwarded following his decision to implement a "no Madoff" policy at Partners Advisers. *Id.* ¶¶ 125-26.

264. Dr. Pomerantz concluded that it would have been mathematically impossible for anyone implementing the Madoff SSC strategy to eliminate downside risk, as Madoff did, while generating returns in excess of default risk-free Treasury returns over any significant period of time because of the pre-determined range defined by the strike prices. *Id.* ¶ 126 & n.160.

265. Dr. Pomerantz concluded that "[t]he inability to match the Madoff SSC strategy with the reported returns for the Square One BLMIS Account was a red flag that Madoff was not executing the purported strategy." *Id.* ¶ 126.

266. Dr. Pomerantz further concluded, that as noted by Partners Advisers in the Lloyd's Bank due diligence questionnaire, Square One's performance, and deviations from the SSC Strategy, should have been an "alert factor," and that "unusual performance given the strategy and risk profile of a manager, is usually a warning sign." *Id.* ¶ 126 & n.162.

b. Unexplained Exposure to Market Risk

267. Madoff's SSC Strategy was stated to be designed to reduce risk for investors. Under the strategy, equity purchases are hedged using an option collar created through the purchase of puts and the sale of calls. When the purported hedges are not adjusted based on changes in the value of the equity position, the result is inconsistency with the Madoff SSC Strategy, and it leaves the Square One Account exposed to market risk. *Id.* ¶ 127.

268. Dr. Pomerantz's analysis found that on 30 occasions, Square One Account statements reflected changes to the basket of equities purportedly purchased for the Square One BLMIS Account but failed to reflect corresponding changes to the options used to hedge the equity position. BLMIS's actions on each of these occasions was inconsistent with the Madoff SSC Strategy and inexplicably exposed Square One to additional market risk. *Id.* ¶ 128-30.

269. Square One Account statements also showed instances in which there were delays in putting on part of the option collar—at least five separate instances during 1999 with timing issues around the purchase and sale of the options collar. *Id.* ¶ 131.

270. These types of "speculative" option transactions were not used to hedge any equity transactions. Instead, these option transactions were used independently of any equity positions for the sole purpose of generating a profit and were therefore a deviation from the Madoff SSC strategy. The use of options to generate returns represents an example of style-drift as the profits are not being driven by any part of the Madoff SSC Strategy—they are being driven by speculative options. Over this time period speculative options represented 6.9% of the returns in the Square One BLMIS Account. Importantly, not all of these option transactions were successful as the example above reflects. These speculative option trades were suspicious, inconsistent with the Madoff SSC Strategy and should have prompted Square One to perform additional quantitative

due diligence on the purported execution of the strategy. The additional due diligence would have been to conduct performance attribution, reverse engineering, and alpha analysis. Dr. Pomerantz concluded that due diligence in these areas would have revealed the only reasonable explanation for these red flags was fraud. *Id.* ¶¶ 132-41; Pomerantz Report ¶ 138.

c. Atypical Frequency of Dividends

271. BLMIS's SSC Strategy purported to invest in U.S. Treasuries when "out of the market." Money market funds declare dividends daily and pay them monthly. However, upon analyzing the Square One Account statements, Dr. Pomerantz found instances where dividends were paid multiple times in a single month—in contravention of typical industry standards and norms. *Id.* ¶¶ 107, 142-45.

272. Square One Account statements reflected as many as seven purported dividends in a single month, and 25 times where at least three purported Fidelity Fund dividends were reflected on the Square One BLMIS Account statements in a single month. Purported money market dividend payments reflected on the statements for the Square One BLMIS Account that did not match the dates or the frequency of the actual Fidelity Fund dividend payments were suspicious and should have prompted Square One to perform additional due diligence to make sure there was no other suspicious activity on the customer statements. In accordance with industry customs and practices, this due diligence could include a comparison of purported equity, option, and U.S. Treasury Bill prices to the daily high and low market prices, as well as analysis of option volume. *Id.* ¶¶ 143-45.

d. Impossible Option Volumes

273. Dr. Pomerantz's analysis of Square One Account statements against a review of total daily volumes on the CBOE Exchange confirmed it was not possible that BLMIS was trading

the number of options indicated on the customer statements. From February 1999 through November 2008, BLMIS purportedly traded in 171 different call options on 360 days in 455 unique transactions for Square One. *Id.* ¶ 146-47, Fig. 9. Similarly, as it relates to put options, BLMIS purportedly traded 178 different put options on 332 days through 408 unique transactions from 1999 through 2008 in the Square One Account. *Id.* ¶ 148-49, Figs. 10, 11. Looking specifically into the transactions that traded above the daily market volume, Dr. Pomerantz found that the number of shares transacted by Madoff greatly exceeded the total share volume transacted on the exchange. *Id.* ¶150-51.

274. If Square One was following industry norms, Square One should have done additional quantitative due diligence on the purported execution of the strategy, including performance attribution, reverse engineering, and alpha analysis given the fact that the volume reflected in the Square One BLMIS Account was in excess of the total market volume. In the securities market, this should not happen even once since one instance of trading more than the market is impossible, and due diligence in these areas would have revealed significant red flags where the only reasonable explanation was fraud. *Id.* ¶ 151.

e. Impossible Out-of-Range Trades

275. Due diligence on Madoff's execution of the SSC Strategy would have revealed impossibilities related to out-of-range trades. *Id.* ¶ 152.

276. Had Square One done a comparison of pricing information between BLMIS trade confirmations and publicly available pricing data—like Dr. Pomerantz did—it would have revealed the out-of-range equity and options transactions as well as out-of-range t-bill trades. *Id.* ¶¶ 152-163.

277. Based on his analysis, Dr. Pomerantz concluded that BLMIS could not have been making the trades that were reported on the trade confirms or customer statements for the Square One account, and the only reasonable explanation for the impossible out-of-range equity transactions, out-of-range options transactions, and out-of-range U.S. Treasury Bill trades was fraud. *Id.* ¶¶ 157, 160, 163.

D. Process: The Lack of Scalability Was a Red Flag

278. Square One was aware that, by 2001, Madoff was managing at least \$7 billion of AUM. *Id.* ¶ 165 & n.203, 204.

279. Coupled with Square One's knowledge of the SSC Strategy, Square One should have been aware of the fact that the volume of put and call options necessary to execute the strategy would have been impossible under the purported strategy—because if Madoff was managing approximately \$7 billion in AUM, he would have needed approximately \$7 billion in call options in terms of notional value. *Id.* ¶¶ 164-168, Fig. 15.

280. The fact that Madoff was operating between \$7 to \$17 billion under the SSC Strategy with the reported returns was a red flag with fraud being the only reasonable explanation. *Id.* ¶ 169.

E. Process: Industry Customs and Practices Would Have Found BLMIS's Investor Communications as a Red Flag

281. BLMIS's exclusive use of paper statements, and non-standard trade confirmations and customer statements were atypical and inconsistent with industry customs and practices. According to industry customs, customers should have access to their total beginning and ending balances on all statements—which would not be possible with the customer statements for the Square One BLMIS Account. Madoff's non-standard customer statements were a red flag. *Id.* ¶ 170-91.

F. Portfolio

282. Dr. Pomerantz analyzed portfolio-related due diligence, including alpha analysis, reverse engineering, and volatility analysis—all of which reflected industry customs and practices. *Id.* ¶ 192.

283. The Estenne Study illustrated linear correlation analysis as well as regression diagnostics that could be used to interpret the analysis. This information was standard in the industry, and the regression analysis in the Estenne Study, as well as the t-statistic calculated from it, indicated that Square One's returns did not comport with the stated SSC Strategy. *Id.* ¶¶ 192-98.

284. The Estenne Studies include a regression analysis, titled "Linear Correlation Analysis," which plots the monthly return of the S&P 500 against BLMIS monthly returns from January 1991 through October 1999. For example, the regression analysis in the October 1999 Estenne Study shows that only 5% of the change in BLMIS's returns was explained by the change in the S&P 500. *Id.* ¶ 196-98, Fig. 21; Molina Decl., Ex. 55 (Partners Advisers Summary Report, July 1989 to Oct. 1999 (FADSAI0005930)) at FADSAI0005932.

285. The Estenne Studies showed that, on average BLMIS was generating a risk-adjusted return of 2.3% regardless of the performance of the stocks in which it was investing. Pomerantz Report ¶ 200-01, Sched. 5, Figs. 22-24.

286. Had Square One performed a regression analysis, like Dr. Pomerantz performed, the outcomes would have been a red flag that Madoff was not executing the strategy he purported to implement, "or indeed any strategy." The only reasonable explanation was fraud. *Id.* ¶¶ 199-202.

287. Dr. Pomerantz further analyzed the Square One Account through a common technique employed in due diligence referred to as “reverse engineering.” The goal of reverse engineering is to replicate, as closely as possible, the investment strategy that is being pursued.

288. When reverse engineering Madoff’s SSC strategy, Dr. Pomerantz found that the volatility of the market risks in the purported strategy did not match up with the actual volatility produced by BLMIS’s returns. *Id.* ¶ 203-07, Fig. 25.

289. When Dr. Pomerantz performed due diligence on the Madoff SSC Strategy—with less information than was available to Square One—he was able to conclude the stark difference between expected and actual BLMIS volatility as a significant red flag where the only reasonable explanation was fraud. *Id.* ¶ 208.

G. People: BLMIS’s Excessive Concentration of Duties, Lack of Credentials, and Lack of Transparency Were Red Flags Known to Square One that Should Have Been Investigated Further

290. Square One was aware that BLMIS had an excessive concentration of duties—as Madoff acted as the investment advisor, custodian, and counterparty broker. On multiple occasions, Square One raised these concerns. Dr. Pomerantz confirms that, according to industry customs and norms, this was a major red flag. Knowledge of Madoff’s excessive concentration of duties should have prompted Square One to investigate further. *Id.* ¶¶ 210-15.

291. In addition to Madoff’s excessive concentration of duties, Estenne raised concerns related to the “[p]otential risk of front running” given Madoff’s role as the market-maker as well. *Id.* ¶ 215 & n.264; Molina Decl. Ex. 78 (Email from Luc Estenne to Catherine Lemaitre, PAM Global Investments re: Madoff, October 14, 2008 (SQO000007076.C00001)).

292. Luc Estenne’s Book Chapter identified organization risk questions such as whether there is “a back office made of experienced people, how long they have the different principals worked together, etc?” Molina Decl., Ex. 21 (PUBLIC0615798).

293. Due diligence includes reviewing the ADV forms—in BLMIS’s SEC Form SDV it listed no more than five employees working on the IA business. *Id.* ¶ 217.

294. Dr. Pomerantz concluded that, due diligence performed consistent with industry customs, would have revealed that BLMIS had a limited number of personnel, with no advanced education or training who were purportedly implementing a multi-billion-dollar investment strategy. *Id.* ¶ 218.

295. BLMIS lacked typical disclosures and operational transparency—something that Square One raised as early as 1999—According to Dr. Pomerantz BLMIS’s lack of disclosures and operational transparency was a red flag because it was suspicious and inconsistent with industry customs and practices. *Id.* ¶¶ 219-25.

H. Performance

296. The quantitative analyses Dr. Pomerantz performed on the Square One Account included peer analysis, performance analysis in times of market stress, correlation analysis and performance attribution. These analyses are customary in the industry to help safeguard against fraud, misappropriation, or other deceit by an investment advisor. *Id.* ¶¶ 226-28.

a. Performance in Times of Market Stress

297. Dr. Pomerantz’s analysis found that Madoff’s anomalous performance during times of market stress would only have been explained by fraud. *Id.* ¶¶ 229-40.

298. When comparing Square One’s stated returns to the returns of the S&P 100 and S&P 500 during times that the market exhibited significant stress—the S&P 100 and S&P 500 both fell substantially, yet BLMIS’s returns were positive. *Id.* ¶ 230-31, Fig. 26. Similarly, the end of 2002 saw the end of a three-year period during which the stock market fell dramatically while the Square One BLMIS Account reported returns of over 45%. Between 1999 and 2002, the S&P

100 fell 43.9%, while the Square One BLMIS Account showed returns of 45.9%. *Id.* ¶¶ 233-39, Figs. 27-29.

299. Dr. Pomerantz concluded that the consistent returns, that are not correlated to the S&P 100 and S&P 500, should have prompted additional quantitative due diligence on BLMIS's purported strategy, and that due diligence in these areas would have revealed that the only explanation was fraud. *Id.* ¶¶ 232, 238, 240; Sections VI.D.2, VI.B.2, and VI.B.1.

b. Performance Attribution

300. Dr. Pomerantz performed a performance attribution on the Square One Account. Performance attribution is an industry standard analysis to identify the source of excess performance (relative to a benchmark) delivered by an investment advisor. The results of Dr. Pomerantz's performance attribution identifies the sources of return for the purported profits of the Square One BLMIS Account into four major categories for the years 2000 through 2008 including: equity pricing, market timing, dividends, and option pricing. *Id.* ¶¶ 241-42, Fig. 30.

301. Dr. Pomerantz's peer analysis showed that of the four major categories, 58.3% of Square One's purported trades were due to the consistent purchase and sale of stocks at most favorable prices. The comparison of trading records for the Square One BLMIS Account against the Volume Weighted Average Price Analysis (VWAP) for the respective stocks of the period February 1999 to November 2008, shows that 84.7% of purported buy transactions by the share volume were executed below VWAP while 78.8% of purported sell transactions by share volume were executed above VWAP. Further, the analysis showed that, on average, BLMIS purportedly bought shares \$0.39 below VWAP and sold shares \$0.30 above VWAP. These deviations from VWAP are significant in an industry where the industry norm is to target trade execution at VWAP (meaning that one would expect 50% of shares would be above VWAP and 50% would be below

VWAP). The only reasonable explanation for BLMIS's purported ability to buy and sell at these levels with such consistency was fraud. *Id.* ¶¶ 241-47, Figs. 30, 31.

302. After analyzing BLMIS's purported trades, Dr. Pomerantz concluded that Madoff's purported success at timing the market "does not appear to be any better than if he had flipped a coin to determine when to enter and exit the market." *Id.* ¶ 248, Fig. 30.

303. Consistent with Partners Adviser's conclusion that "[m]arket timing doesn't work" and Müller's testimony that it is "impossible to forecast where the market is going, repeatedly," Dr. Pomerantz's analysis illustrates a lack of any market timing skill on behalf of BLMIS. A contemporaneous analysis by Square One would have found the same. *Id.* ¶¶ 248-55, Figs. 31-33.

c. Peer Analysis

304. It is customary to continually evaluate the performance of an investment advisor in the context of peer groups—i.e., other funds, benchmarks, and general market movements. Dr. Pomerantz completed peer analysis using information publicly available from third-party providers, incorporating the evaluation of widely recognized market events and comparing the Square One BLMIS account to different peer groups, including hedge funds, mutual funds, world-class investment advisors, and indices. *Id.* ¶¶ 256-59.

305. Dr. Pomerantz performed peer analysis using six performance metrics: (i) Sharpe Ratio; (ii) Sortino Ratio; (iii) number or percent of positive months; (iv) number or percent of negative months; (v) maximum drawdown; and (vi) number of months in drawdown). *Id.* ¶¶ 260–65.

306. Dr. Pomerantz concluded that across all six industry-standard metrics, that were also used in the Estenne studies, all peer groups (such as hedge funds, mutual funds, world-class

investment advisors, and indices), and for all time periods considered, BLMIS outperformed its peers to a degree of statistical improbability, if not impossibility. *Id.* ¶¶ 266-67; Sec. VI(D)(3).

307. It is highly unlikely for an investment advisor to outperform, and often by a significant amount, every peer group, across these performance metrics, across lengthy periods of time. These results should have prompted additional qualitative due diligence by Square One, which would have revealed the only reasonable explanation was fraud. *Id.* ¶¶ 267, 316.

d. Correlation Analysis

308. Dr. Pomerantz performed a correlation analysis of Square One's purported returns against the S&P 100. *Id.* ¶¶ 317-25. Per Dr. Pomerantz's reverse engineering analysis, BLMIS's returns should have displayed a correlation coefficient of more than 0.49 from February 1999 through November 2008. However, the returns for the Square One BLMIS Account displayed a correlation coefficient of 0.23 during that period. *Id.* ¶ 319. The returns for the Square One BLMIS Account were entirely unrelated to what happened with the S&P 100 over Square One almost 10-year investment history with BLMIS, contradictory to the purported strategy. *Id.* ¶ 321. The lack of correlation with the S&P 100 was indicia of fraud demonstrating that Madoff was not implementing the strategy he said he was implementing based on the returns he reported and should have prompted additional quantitative due diligence on the purported execution of the strategy, including performance attribution, reverse engineering, and alpha analysis. The only reasonable explanation for the lack of correlation was fraud. *Id.* ¶ 325.

I. Price: BLMIS's Operational and Fee Structures Were Atypical

309. BLMIS's operational structure was atypical, suspicious and inconsistent with industry customs and practices. BLMIS utilized managed accounts, despite the fact that Madoff purportedly implemented the same investment strategy across multiple accounts. It was highly

inefficient for an investment advisor following the same investment strategy across multiple accounts to implement the strategy using managed accounts instead of a pooled account or fund structure. BLMIS incurred significantly more administrative costs than if it had been structured as a fund.

310. Dr. Pomerantz concluded that, because of how the strategy was purportedly executed, BLMIS incurred significant additional operational costs (including printing and sending tens of thousands of documents each year) that were unnecessary. *Id.* ¶¶ 327-30.

311. Conversely, BLMIS's fees were significantly lower than those that would have been charged in a traditional fund structure. A common industry fee structure for an investment advisor is the "1-and-20" structure, consisting of a management fee of 1% of AUM and a performance fee of 20% of profits. Where a typical investment advisor would charge both management and incentive fees, BLMIS only charged transaction fees. Dr. Pomerantz concluded that BLMIS's fee structure was a red flag because it was an extreme departure from industry customs and practices. *Id.* ¶¶ 331, 336.

312. Under BLMIS's atypical structure, Square One paid \$440 thousand less per year than they would have paid under a typical 1-and-20 structure. The fact that BLMIS passed on approximately \$4.4 million in fees from Square One alone was suspicious and a red flag because it was inconsistent with industry customs and practices. *Id.* ¶¶ 337-41.

J. Additional Quantitative Due Diligence Would Have Revealed Significant Red Flags Where the Only Reasonable Explanation Was Fraud

313. Dr. Pomerantz concluded that due diligence consistent with industry customs and practices would have revealed numerous red flags relating to the Square One BLMIS Account because:

- i. There were certain transactions that were impossible and the only reasonable explanation was fraud. *Id.* at ¶ 342.

- ii. There were also numerous red flags relating to the Square One BLMIS Account that were by their nature indicia of fraud, inconsistent with industry customs and practices, and/or inconsistent with Madoff's purported strategy, requiring additional qualitative and quantitative due diligence. *Id.* ¶ 342.
- iii. Over the life of Square One's investment with Madoff, a number of examples where information was shared regarding BLMIS and the Madoff SSC strategy that, consistent with industry customs and practices, would have caused a fund manager invested with BLMIS to perform additional due diligence. *Id.* ¶ 342.

VII. Square One Was Sanctioned for Spoliative Conduct

314. During fact discovery, Square One produced documents from a data set it curated in 2011 using limited search terms and without input from the Trustee (the "**2011 Data Set**").

315. Outside of the 2011 Data Set, Square One did not preserve any other documents or data.

316. In June 2023, the Trustee moved for sanctions against Square One for spoliation.

317. On August 27, 2024, Discovery Arbitrator Judge Frank Maas issued spoliation sanctions against Square One under Rule 37(e) of the Federal Rules of Civil Procedure as a result of its failure to preserve metadata. *See* Order Regarding Trustee's Motion for Spoliation Sanctions, ECF No. 311.

318. Square One has refused to pay any of the sanctioned amounts to the Trustee.

319. On March 27, 2025, the Trustee filed a motion with Judge Maas seeking to hold Square One in contempt and requesting coercive sanctions (the "**March 27 Sanctions Motion**"). *See* Molina Decl., Ex. 80 (Trustee's Letter Requesting Sanctions).

320. As of the date of this filing, the Trustee's March 27 Sanctions Motion remains unresolved. *Id.*

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