EXHIBIT 1
MR. MADOFF: Obviously, first of all, this conversation never took place, Mark, okay?

MR. VIJAY: Yes, of course.

MR. MADOFF: All right. There are a couple of things that, you know, could come -- well, I don't know if they'll come up or not but let me just tell you how we -- information that we have given out in the past whenever we're asked about our relationship, our relationship with any of these funds is, number one, we really have never seen any of your documentation, you know, like the stuff that you send out to your clients, you now, any of that stuff because we never want to be looked at as the investment manager or that we are out, you know, soliciting or doing any marketing for the fund and so on, so in the past if we've ever been asked about what our role is with any of these types of funds, it has always been that we are the executing broker for these transactions and that you use a
proprietary trading model that we -- that is ours that basically sets the -- that, you know, has certain parameters built into it which have been approved by you and then that's part of the trading directive that you've seen.

MR. VIJAY: Right.

MR. MADOFF: Okay, the, now the -- so -- and by the way, on the trading directives, the one that you have -- Mark, the one that you sent me a copy of, which is an old one, all right: -- we're going to send you up -- actually, we'll messenger it up to you, Mark, today, a new trading authorization directive that we had actually a couple of years ago, which basically is the same thing except it took the -- they said the other day the options are no longer part of the model. The options are separate and there are standing instructions for the models. They have the same parameters built into it but it has been broken off as part of the model a few years -- a couple of years ago, actually fairly soon after we gave you this other one, and
the reason we did that was because the intellectual property that's in the equity piece of it, the first piece of it, is stuff that we feel and that our lawyers feel is our property and we could always claim it was our property from a -- so that nobody else can use that but the options piece of it really is too broad that we would never be able to actually successfully claim that that's a, our own intellectual property if somebody else wanted to use that, so we basically split it off from the model, so the equity is a part of the model. The options are not part of the model. It's important, so the -- but you have to have -- we have to have standing instructions on the model -- I mean on the option side as well so that we're not deemed to be, you know --

MR. VIJAY: Right.

MR. MADOFF: Okay, so, if you ever get into any conversations about the model, it's for the equities. The options are not part of the model. That's just -- there are standing instructions of what the parameters
of the options are, and then basically
they're identical pretty much but they're not
-- as I say, it's not part of the model and
that's important, okay. So I'll send you up
the new trading instructions today and also
the standing instructions for the option
side.

MR. VIJAY: Okay, good.

MR. MADOFF: They'll only respond to that
if for some reason they ask you what -- they
ask you about how the, you know, strategy
gets implemented and so on. The other thing
that is on the allocation as to how, you
know, we know how much monies to allocate,
basically the response that we've always
given in the past is the fund allocates a
certain amount of monies to us that says
okay, this is how much we want to invest and
it has been pretty much, you know, the same
amount, all right, and then when we liquidate
-- so if we have for argument sake $4 million
that we're -- that's been allocated to us or
whatever -- $1 million has been allocated to
us and the -- and we liquidate the
transactions, okay, so now we go from fully
invested to now we're sitting in fashion, all
right. That amount -- we log that amount and
we know that the next time we see a -- we see
a -- we decide that we want to go into the
market we start to work with that -- with
that -- what the last amount was, all right,
and the only time that would change would be
if you -- if the fund gets, you know, a
redemption or whatever it is and then they --
what would typically happen is the investment
manager calls us and says, okay, we want to
-- you know, we need -- we're taking a
million dollars away from the allocation
because we have redemptions, or whatever it
is, and then we adjust the figure and we're
working with the million dollars less. So,
you -- and the same thing would work if in
fact you wanted to send in additional monies.
Again, the investment manager is the one that
tells us how much to add to the strategy or
subtract from the strategy, and that's done
basically by a phone call. Okay?

MR. VIJAY: Okay.
MR. MADOFF: Because that's the way we've always responded to any of those questions. Let me just see if there's -- I doubt they'll get into that, but they -- you never know with these guys, so it's basically that, you know, that Madoff uses whatever the last amount that he liquidated for the fund and that's the new amount that he would invest unless money is brought in and taken out and then that's -- we get a phone call from the investment manager and change the allocation. Okay, so I think that's that. Let me look at my notes, okay. The -- okay, okay.

MARK: Who makes that phone call on it? Is that Dan calling over to Madoff or do you?

MR. VIJAY: I think at this point it's Jeffrey making that phone call.

MARK: When we're going to take money out?

MR. VIJAY: Yeah, when we -- exactly, when the contributor or redeem. I mean I'll actually send the written instructions. It will be a wire request.

MARK: Okay, good.
MR. MADOFF: The best thing to do is not get involved with what you said, written instructions, if possible because any time you say you have something in writing they ask for it.

MR. VIJAY: Okay.

MR. MADOFF: So, the best thing to do is just say it's a phone call. That's what we said it is, we get contacted by somebody at Fairfield, somebody -- the investment manager or Jeff Tuck or whatever it's called but that's the way it has basically been done for the most part, at least for the time that we -- you know, if we answered this question, you know, a year or so ago, and that's basically the way pretty much everybody operates. You know, they make a phone call and say, we need to withdraw a certain amount of money and we want to add a certain amount of money and that's it, because typically if you're adding money, you know, we'd have to okay it. We may not take it or we may take it. So, you know, that's basically -- you know, also when you speak to these guys, by
the way, you’re not supposed to, you know, sort of -- you don’t have to be exact on this stuff because it’s not -- you know, no one pays attention to these types of things or who calls or who doesn’t or who remembers who calls. It’s basically, you know, more casual. I mean, the idea is that it’s -- is that we’re not the one that’s making that decision how much to -- I mean, you know -- you know, we’re not the one that’s operating the fund. That’s the issue that they always try and determine as to what the role of the various parties are, is the broker controlling the fund is the investment manager controlling the fund.

MR. VIJAY: All right. If they get into the question of these trading authorizations and these operating guidelines, you know, it’s a model that you develop that we’ve reviewed and approved and that should be the stance rather than -- you know, than anything else.

MR. MADOFF: Yeah, I mean, it’s you know, they have seen trading author -- you know,
they have seen trading authorization. They saw the -- when they were in to do our examination a year -- you know, I don’t know when that was, nine months ago or whatever, they saw the -- they saw that there’s -- that the trading -- the new one that I’m sending you, the trading authorization that doesn’t have the options as part of the model.

MR. VIJAY: Mm-mm.

MR. MADOFF: Because we -- you know, we had said that the options were part of the model years ago, but it’s now not part of the model, and you know the reason we took it out they were twofold. Number one, it was that we didn’t want it to be part of the model because we didn’t want it -- we didn’t want the options to be -- to taint the intellectual property of the equity piece, but just as importantly as the model on the option -- the model was designed really for the equity side, not for the options and the options the problem with the model with the options is it didn’t give us all the data -- it didn’t have all the data that we needed to
determine some of the -- when it came to executed because it didn’t have certain factors in that -- in the model, like liquidity and so on and so forth, so that’s done -- so the options are done separately. And the options, by the way, you know your documents you put down that they’re down simultaneously. They’re really not done simul -- even if you look at the trading authorization, the beginning, it says an attempt to establish the options. The options get put on, you know, relatively, you know, close to when we do the equities, but they’re not -- you know, it’s not like it’s a simultaneous thing, because option contracts aren’t negotiated that way.

MR. VIJAY: So it will be -- I mean, it will be at some point throughout the day if --

MR. MADOFF: Well, yeah, yeah. Well, those -- they saw that because they have the -- they got your confirmations and so on.

MR. VIJAY: And so that could conceivably be a few hours between the completion of the
MR. MADOFF: Yeah, right.

MR. VIJAY: -- (inaudible) and the options. Is it true that your -- you know, you're attempting to secure the put hedge prior to actually executing options? In other words, you're going out to your eight to twelve or so counter parties and trying to say that, okay if --

MR. MADOFF: No, no, because this is the thing you always have to understand that they -- that you guys are not -- are not part of the execution piece of this -- of this strategy and that's important. In other words, the -- because they -- the concern that they have with any strategy that is implemented for another party, like a fund from the executing broker is their concerns are is there informa -- do you know when -- when the strategy is going to be employed ahead of time or does anybody know it ahead of time because then there's the issue of is there a possibility for somebody to front run an order. So if -- so we basically -- the
only ones that know when we’re going to execute the strategy and whether it be going in or going out is us, is Madoff, all right. That you’ll get the information -- you know when you’ve -- you know when the strategy has been implemented or exited when you get the confirmation because if we -- and it’s the same thing with the counter parties, you know. They -- we have an -- we know that we’re going to be able to put on a column, which is what this is because you can always put on a column. It’s just a matter of determining the price. You’re either going to pay or you’re going to pay less, but eventually we’re going to be able to establish that --

(Phone Rings.)

MR. MADOFF: Hold on one second. -- Yeah, hold on one second. Sorry. So the issue is, look, as far as you’re concerned, the fund has allocated certain amount of money to go into a specific strategy. You know what the -- you’ve approved the parameters of the strategy and I’ve agreed to
follow those. That's the trading
authorization directive is it says, okay,
these are the strategies -- this is the
strategy. The model sets the size of the
order, the stock and the price and that's it,
and then once you get that execution then
your job is to, as an investment manager I
guess, is just to monitor that the -- that
there were in fact the right securities in
there that, you know, it followed the
instructions or the model that you didn't buy
gold, you bought IBM and General Motors and
to track the performance of the strategy, but
the -- if in fact you were involved in -- I'm
sorry, just hold on because I'm the only one
here, okay?

(Phone Rings.)

MR. VIJAY: Okay, no worries.

(On Hold.)

MR. MADOFF: Okay, I'm sorry. Can you
just hold on for one second so I can take one
other another call?

MR. VIJAY: Sure, I'll wait here.

(On Hold.)
MR. MADOFF: I'm sorry, if I get anymore solicitations for charity I'm going to kill myself. Okay, I'm sorry, so what I was saying was that the -- I mean, that's the rule. We're the executing broker. It's our strategy. You guys are just monitoring monitoring what the effect is because the question is always revolving -- always come up about -- and the concern of the commission or any regulator as it relates to hedge funds and executing brokers is that there -- is there an opportunity for the fund or one of their other funds or entities to front run an order. Like if they know that we're getting into the market are they transmitting that information to somebody else or are they are they using it themselves. So the -- and even though that would obviously be counter productive to the fund overall, but their concern is is maybe the fund is -- but are some of the employees of the fund if they get that information. It's the same thing with us. We have to be very careful that nobody in our organization sees any of the trading
that we do, whether it be for the firm’s own account, whether it be for clients’ own accounts and so on. So the -- you know, the question probably will come up is -- does does Madoff call you and tell you he’s going into the market or getting out of the market or that he started getting into the market and so on. Now obviously there have been transactions taking place over a series of days which it does, you’ll know eventually, but basically you’re given the confirmations to it -- by the time you’re getting the confirmation two or three days we’re basically finished anyhow.

MR. VIJAY: Mm-mm.

MR. MADOFF: Okay?

MR. VIJAY: Okay.

MR. MADOFF: So that’s the issue. Now and all of this is -- is the case. It’s not like you’re telling them something that’s not the case, but as I say that’s -- that’s the major concern that these people have and probably why they want to know who is it that’s implementing the strategy. Is it us
implementing the strategy? Is it you
implementing the strategy? And obviously
we're the ones that have to be -- you know,
we have the time and a price discretion, you
just the -- you know, you've -- you've --
this model actually, you know, picks the
number of shares and the stock if that's the
case because it's a very tight parameter, so
you know that -- that's -- that's part of the
-- that's part of the exemption for the
discretionary issue from the SEC regs. So it
used to be years ago that, you know, you had
to give a particular order and a particular
security, but then they've changed that and
they've -- to now -- so that -- because
everybody was using basket strategies and
like would it be index arbitrage or anything
else like that where there are actually
formulas and models that are generating these
trading strategies, and this is not -- we're
not the only one that does this type of
strategy. So the brokers have to have -- you
know, to have these what they call not held
order, these working orders, they have to
have the flexibility to execute a basket of
securities and the baskets are going to be
different denominations based upon -- based
upon models.

MR. VIJAY: Right.

MR. MADOFF: By the users of these
things. So basically the issue from them,
and probably the most important issue is that
Madoff is the one that implements the
strategy. Yes, we know that he has certain
parameters that he can only buy certain
securities and certain amounts based upon a
model. The time and price of when he
executes the strategy is his decision, and we
don't find out about it until after the fact.
And you don't have to actually go out say so
there's no front running possibility.

MR. VIJAY: It will be understood, yeah.

MR. MADOFF: Yeah, but you don't want to
plant any seed in their head -- but they'll
know that. That's -- if they know, yes, we
-- we only -- we don't get any information
ahead of time then that's really what they --
what they want -- they want to know.
MR. VIJAY: I mean, if as part of their larger inquiry if they're interested in just the control of that or is it a matter of protecting that information, not that it -- I mean, whether it goes out to FCG in advance or even internally, I mean, it would be good to understand some of the controls that are (inaudible) that you have in place, but also separates, you know, the information flow from your kind of managed account.

MR. MADOFF: Basically -- you could basically -- you know, as I say if that -- they know that already because they've looked at -- when they come in to do exams for us, all right, they've -- they make sure that there are Chinese walls -- that we have Chinese walls established between our market making side and our -- and our proprietary side of the room and be -- and also from the institutional orders. So they know that we have Chinese walls. Every brokerage firm has to have Chinese walls established between the various lines of their business. All right, so they know that because, you know, that's
it. All right, what they don't know is what Chinese walls you have, all right, in your organization which is -- but that you're okay because you're not -- to my knowledge in any of your funds you're not executing any transactions and you're getting your -- you know, well, first of all in your other funds you probably have no idea what they're buying and selling period, you know, as far as individual securities, but you -- you know, although I don't know. But you -- but there's probably nothing you could do with these funds to run in front of their orders. One of the reasons that these funds never disclose or at least the old line funds never disclosed to their investors what they're buying and selling until after the fact is they don't want them -- you know, they don't want them having any of this information. Part of the problem in this whole area with these -- with these new style funds that are out, these one -- these guys that claim they give them transparency all the time so that they -- they, you know, it's basically the
small or new funds where they -- where they
told their investors, you know, what they’re
buying, what they’re selling. They look at
that as being, you know, very transparent and
they look at that as an advantage to their
clients and that’s true that the client knows
that what he’s buying and selling so he’s not
all of a sudden going to find out he bought
potato futures when he thought the fund was
investing in equities or something. The
problem with that is that the flow of
information, all right, leads -- you know,
puts the funds in a position where they’re
getting information too soon and that that
information, you know, makes it possible for
the fund to be -- you know, to do -- to get
front run or the investment manager to front
run. So, you know, whereas in the old days
you would never -- you had no idea -- even
like if you’re an investor of Paul, Tudor,
Jones you get a two page sheet once a quarter
that tells you what your equity is, but you
have no idea what the hell he bought or sold.
So one of the concerns that the commissioner
has, as I said, is you know -- is had over the -- over the recent years now is -- is the concern of do -- do the -- do the investors in the fund know what the fund is doing. Like do you -- would you call up your investors even in Fairfield and say Madoff is getting into the market, you know, and it would be the same thing with the derivative dealer. You know, you call up the derivative dealer says, okay, I'm going to enter the market tomorrow and they can go -- and they know that we buy typically the S&P, they go out and run in front of it. So, you know, the secrecy as to information is a key issue for everybody and from your standpoint yours should be basically I don't know about -- I don't know about these trades until after the trades are executed and my job is then just to monitor and see what the performance of it is and to make sure that the securities that we -- that was -- that was supposed to be in the model are in the model.

MR. VIJAY: Understood, that makes sense. And Bernie, is there any issue in your mind
about -- about information getting out to
clients after we've already been invested but
prior to an exit?

MR. MADOFF: No, not with you -- not with
you it is because everybody knows basically
that the strategy involves buying the top 50
stocks in the S&P.

MR. VIJAY: Right.

MR. MADOFF: Okay, so they know it -- you
know, they know the stocks that we're going
to buy, we're in the S&P, you know, and they
-- they know that eventually we're going to
come out of the market, but you know we will
never tell them -- you know, I mean, you
don't know when we're going in -- out of the
market or when we're coming into the market,
you never do.

MR. VIJAY: Right, right.

MR. MADOFF: You know -- you know, the --
so that's -- we don't -- we don't have a
concern about it because as far as we're
concerned there's nothing that any of your
clients could do, you know, that would hurt
us or hurt, the strategy because they just
don't -- don't have the information, you know.

MR. VIJAY: Understood.

MR. MADOFF: In the situation. Yeah, they may know that you're in the market because you've told them you were in the market or because you sent out some stuff to them, but the reality of it -- you know, so they know they're in the market and they know eventually they're going to come out of the market. They don't know if we're going to come out of the market in one week or in two months. You just don't -- you know, they just don't know that. So the -- let me just go a little further, but feel free to ask anything.

MR. VIJAY: Sure. I mean, that's the main concern that seems to come up from the commission over the last few times that they met you. Are there any other concerns that maybe are secondary or -- I should also know?

MR. MADOFF: Oh, I mean, I think that and these are concerns that necessarily aren't ours or, I mean, issues that the SEC
had with us. It's -- it's knowledge that I
know because of my relationship with the
regulators and also because of -- you know,
common sense would tell you, you know, these
issues and that this would be -- this would
be the concern. It's the same -- it's the
same concern that they have with the -- with
the proprietary trading desks of firms. In
other words, you know, and the institutional
desk. I mean, Merrill Lynch -- this is from
the beginning of time. Merrill Lynch gets a
hundred thousand share order in IBM from
their institutional desk and the
institutional broker who got the order, you
know, and working the order tell the
proprietary trading desk at Merrill Lynch,
listen, I got a large buyer or order in IBM,
do they -- you know -- you know, do
something.

MR. VIJAY: Right.

MR. MADOFF: So this is -- you know, this
is -- you know, this is an old problem. It's
be -- it's more exacerbated now because of
the fact that you have so much hedge fund
activity. It's like 50 percent of the market
place and the hedge funds operate in totally
different ways than they used to. You know,
you have all these funds. You have -- it's
just it's changed the landscape and the
commission has no idea what the hell is going
on and of course they always think the worst,
which is what they're supposed to do. So
they always -- you know, they always assume
that somebody is sharing information and
giving it -- and what used to be, as I say,
basically, they just had to worry about the
brokerage firms running in front of a client
or they used to worry, for example, we -- our
market making orders, you know, department
gets orders, all right, so -- from A.G.
Edwards, Merrill Lynch or whatever. Does --
do we give that information to our
proprietary desk. Now the reality of it is
there's stupidity of -- and we answer those
questions all the time, every time we get an
exam, and the issue that is -- our market
making desk, the information that we get from
our orders is meaningless. I mean, they're
-- they're, you know, five hundred, eight hundred thousand share orders. We're not getting hundred thousand share orders. So that is -- it doesn't -- even if we told the proprietary guy that, yeah, we just got a five hundred share order and they come in every three second, less than three seconds, what the hell they going to do with it? Even when we had these -- a larger orders, our time slicing orders, those -- those -- we have automatic lock out procedures in our -- where our system locks out the firm from trading at the same time that we're working those orders and so on and so forth, and the orders that we get that we think -- the people that execute the orders for, let's say for Fairfield, are totally, you know, aside and separate. They never see -- no one in my organization ever sees an order that we get from Fairfield.

MR. VIJAY: So those people are they -- they're separate and Chinese walled away from the rest of the market making business, okay.

MR. MADOFF: Yes.
MR. VIJAY: And how many people are on that team right now?

MR. MADOFF: Okay, there's really only -- I'm the only one that can make the decision in our organization as to when to get in and out of the market. We have one other person, all right, that would make decision when I'm (inaudible). There are a number of us that discuss, you know, when we should get in and out of the market, but I'm the only one that pulls the trigger.

MR. VIJAY: Okay.

MR. MADOFF: Or if I'm not there, someone else, but I'm always there. But these -- this is type of -- this kind of information is not information that you would have any reason to have.

MR. VIJAY: Okay.

MR. MADOFF: And you don't -- you don't want to -- you don't want to have that information because -- and so -- and what they do is, you know, the Commission when they ask questions they try and draw out information. You know, that's what they try
and do. Even though they should -- they have no reason to have it -- just hold on one second.

(On Hold.)

MR. MADOFF: Hi, hello?

MR. VIJAY: Yeah, we're here.

MR. MADOFF: So the -- you know, the less that you know about how we execute, and so on and so forth, the better you are other than, yes, you could -- you know, you could -- you know, if they asked do you know that Madoff -- do you know if Madoff has Chinese walls, and you say, yes, look -- you know, your position is say, listen, Madoff has been in business for 45 years, you know, he executes, you know, a huge percentage of the industry's orders, he's -- you know, he's a well known broker. You know, we make the assumption that he's -- he's doing everything properly.

Yes, we know he has -- you know, as part of our normal relationship, we know that he has Chinese walls between the various business lines of his firms, but as to who executes the orders in our organization, how we
execute the orders --

MR. VIJAY: That's not going to come up.

MR. MADOFF: So then other than the fact that you know that we use a model to execute those -- to execute your strategy with them, that's really all that you really want to know because you don't want to have a relationship with us that is more than it is, and that that's -- and that's why we designed it that way, that's why we, for example, never see your clients. We have in the past, you know, on occasion but we never really saw the individual clients, we would see some of the -- we used to see some of the banks that you used to deal with, you know, and I used to -- that's why I never anybody because one of the concerns -- the other concern the commission has is do -- do the executing brokers -- and we're not even a prime broker. I know you refer to us as a prime broker, but a prime broker like Morgan Stanley is basically these guys do capital introduction. They do margin lending. They do all sorts of other things. They give you free rent. They
give you all of these things. We don't do that. We're -- we -- our role has always been defined as the executing broker for our clients, whether it be A.G. Edwards or whether it be Fairfield Century that we're working on on orders from them. We never execute any other orders that you have, for example, in any of your other fund business. We -- you know, our relationship is strictly execute the split strike conversion orders that -- that we execute for you and that's it. So it is -- it's not -- you know, we you know are not out -- one of the other concerns they used to have is does the executing broker get directed brokerage. You know, like do you -- you know, do you -- do we execute other trades for you be compensated in that, and you know that way. Is there any soft dollar arrangements? There's none of that. Do we do any marketing for you? Do we do -- do we provide you with any other research, any of that? We do not do that. Other prime brokers do all of that stuff and all of those things, relationships are -- are
concerns for the commission. So we -- we have a very defined role and function in how we operate for -- for you or anybody else, and that is we are the executing broker.

Yes, you know, we're the -- it's our strategy, it's our motto and our compensation is strictly the commissions that we generate from the orders, and that is -- that's it.

There's no other relationship involved. So any questions that they would ask you about, you know, how we execute the transactions and this and that, that's not something that we've ever shared with you nor would we have any reason. We don't market you. We don't -- we don't -- you know, we don't know who your clients are. We don't discuss anything with your clients. We don't speak to them. You know, let me just see if there's any other questions. I'm trying to cover a lot with you. We don't know who your clients are. If they ask you, you know, do you know who else we execute these trades for, you say, well, we know we got -- the strategy is used by other funds, but you don't -- you
know, you don’t know the amounts, you don’t know who because we don’t discuss that with -- we’ve never discussed that with you and we don’t intend to. So you can say, yeah, we know -- you know, there are other funds that execute this strategy through Madoff, but you don’t know the size, you don’t know the arrangement, you don’t know the thing -- you know, you assume is basically the same as yours are, which it is.

MR. VIJAY: What if the question comes up whether we -- we’re comfortable or we can verify that we’re getting sort of a pro rata allocation based on our assets, other particular execution in or out --

MR. MADOFF: You can say that you -- that we’ve -- that we’ve told you, which is the case, that everybody gets a pro rata allocation.

MR. VIJAY: Okay.

MR. MADOFF: How do you know that? You don’t, okay, but that’s -- you know, that’s what we’ve told you.

MR. MADOFF: That’s the arrangement.
MR. MADOFF: That's the way it is, so if we -- if we have, you know, eight billion dollars to go out and put to work, and we go into the market and we only buy two million the first day, then everybody gets 20 percent of the allo -- you know, it's your fair share of allocations. All you have to know is that -- that -- that everything is allocated on a pro rata basis based upon all of our clients, and that's -- that's the way all brokers work. So and again, you know, they don't -- you know, you don't have to be too brilliant with these guys because you don't have to be, you're not supposed to have that knowledge and, you know, you wind up saying something which is either wrong or, you know, it's just not something you have to do. So -- and I'm not -- I'm not telling you to conceal anything. I'm telling you, you know, that there are things that you don't -- one of the problems we've had in the past is people go out and they -- they, you know, even -- I'm talking about like with you where guys write things in a document or say things which is
not really -- which is not a hundred percent
the case, and I’ll get into that in a little
while when I go through your notes. I’m just
trying to cover the stuff that I --

MR. VIJAY: Sure.

MR. MADOFF: First, okay, so we don’t
market. You don’t know the exact amounts on
what we trade for others. We’re the
executing broker. We don’t do any other
business with you. There are terms and
conditions on the options just like there are
on the equity. Yup, and the options are not
part of the model anymore. I went over the
allocation. Okay, let me just get into the
notes that you guys put together. Ross, you
can leave the law profession now, you’ll be a
money manager.

UNIDENTIFIED MALE: Well, that’s where
the guy trained, right, he was on the options
floor.

MR. MADOFF: Right, okay, the fund
strategy is -- that’s fine. The relationship
that’s all fine. Okay, the guidelines --
yeah, okay, we covered. That’s fine. I told
you don't have to make the statement
there's no front running possibility, that's
assumed. Okay, on the -- the split strike
strategy objective, okay. The objective of
the fund is to achieve capital appreciation,
okay, I would take out -- yeah, it's
submitting it anyhow, but don't say --
consistent monthly returns.

MR. VIJAY: Okay. You can delete that,
yeah.

MR. MADOFF: By identifying any profiting
from (inaudible) of large cap fund, that's
okay. You know, it's basically because, you
know, the consistent monthly returns is not
necessarily --

MR. VIJAY: Our objective as such.

MR. MADOFF: A consistent, and it's again
it's, look, this strategy -- and I've had
conversations with the commission two years
ago when they sent around inquiries on how
all -- you know, executing brokers, broker
dealers were dealing with funds and what the
strategies they use for the funds and what
the role is and so on and different types of
strategies and so on, and they’re aware of the fact that we do this -- that we do this strategy for you and for others, right, and basically, you know, the way we describe the strategy, which is the case, is it’s a strategy that is -- that, you know, involves putting on a bas -- buying a basket of securities that replicate the S&P, all right, one hundred. And, you know, according to a -- the pre-defined parameters and models, and that’s -- that’s (inaudible) that takes care of the discretionary issue. And the purpose of the strategy is to take advantage of an upward move in the market, all right, that’s -- and the -- you’re buying the securities that are basically going to move with the S&P, all right, and that that -- that strat -- that basket of securities can be hedged using broad based index options, all right, to -- you know, to put a collar to limit the risk of the strategy, all right, by hedging it. You know, these basket strategies, you know, are not unique to us. The model is unique to us, but some people will buy the
whole S&P, you know.

MR. VIJAY: Can I ask you, is it part of the model, is there any sort of decision between stock A and stock B and the overall purpose is obviously to replicate the performance of the index and to track it very closely, but you know is it -- is it a pre-standard if the market capital were to index that your really just looking for the largest market caps and going down that list?

MR. MADOFF: In other words, it is -- it's important that the -- that we buy -- what our model defines of just, you know, certain types of securities and certain capitalization. So it's not that we can -- we do not care whether we think IBM is going to move up more than General Electric and so on. This is a market strategy that is based upon the overall movement of the market. So we are basically -- if we wanted to do a pure play we would buy all 100 S&P securities, but the problem with doing that the more you buy the more your commission costs are and the more cumbersome the strategy is. So the idea
is to basically buy a basket of securities
that's going to have a 95 percent correlation
and so the model dictates -- and, again,
they've seen these parameters, so they know
what the parameters are. All right, they --
they -- so we're not trying to pick General
Electric because we like General Electric.
We're trying to -- to, you know, if the
market -- if the market's going to move two
percent in a particular day and we -- we want
to be able to have a basket that's all --
that's going to follow that move as closely
as possible, and the reason -- because we --
we're not trying to -- we're not trying to
pick one stock that's going to out perform or
possibly under perform the market. So, yes,
it's basically the same securities all the
time because those are -- those cap waitings
are built into -- are built into the S&P.

MR. VIJAY: Right.

MR. MADOFF: All right, and you can --
you can either hedge it or not hedge it. If
you wanted to be open ended both on the
upside and the downside, you cannot hedge it.
We -- we don’t believe in not hedging, and so we’ll -- we’ll hedge it with -- with the -- with a broad base -- with a broad base index with certain parameters below the market, they have to be out of the money, you know, on both sides and so on and so forth. But, again, that is not something, so you understand, that they -- you know that you have to -- yeah, if you have -- you know, you’re not the one that’s implementing the strategy and you’re not even the one that’s determined that this is a great strategy or not. I mean, this fund has been using this strategy for 15 years.

MR. VIJAY: Right.

MR. MADOFF: You know, so this is -- you know, this strategy was put on long before you even showed upon the scene. You know, and this is a -- you know, this is not a strategy that is a unique strategy. It’s a market index strategy and the skill of us, the skill of Madoff is knowing when to get into the market and get out of the market. That’s the role we play. I mean, that’s the reason you
choose us as opposed to some other guy.

    MR. VIJAY: That is the interesting question, but I understand that it’s not going to be -- I mean, wouldn’t anticipate that will be something that the SEC is interested in or at least with this discussion with us. So, I mean, it’s fair to leave that out or if it comes up, you know, to simply --

    MR. MADOFF: Look, you’re not --

    MR. VIJAY: Hotline our role and defer that question to you if --

    MR. MADOFF: I mean, exactly. That’s not a -- as I say, you know, look you never know what they’re going to ask because these guys they thought -- it’s a fishing expedition.

    MR. VIJAY: Right.

    MR. MADOFF: That’s what they do, okay.

So, you know, they typically -- you know, we run through this all the time. The guys come in to do a books and records examination and they -- they whatchamacallit -- you know, they ask you a zillion different questions and we look at them sometimes and we laugh,
and we say are you guys writing a book? And we say, you know, and they know that brokers -- you know, because these guys they work for five years at the commission then they become a compliance manager at a hedge fund now.

MR. VIJAY: Right.

MR. MADOFF: Or they -- they go work for proprietary trading desk. Nobody wants to stay there forever. So nobody wants to give them that information, and you know it's none of their business. That doesn't prevent them from asking it, and they'll say, you know, well, we just want to know -- you know, about the strategy. They know about the strategy. You know, they should. You know -- you know, the issue -- I'm telling you the issue here is strictly of -- this is a front -- my guess would be, I don't know for sure, but I -- you know, my guess would be this is an issue of front running. Is there a relationship between Madoff -- you know, in your situation and some of the other funds? Does he participate in the other funds? Is he an investor of yours? Does he share in any
other profits? You know, all of those types of things. So the -- when the -- but if they ask questions about the strategy, the
strategies are -- you know, they know the answers that -- you know, maybe these girls, these lawyers don't know it, but someone there knows it. The -- you know, and again it's not -- look, you have to remember that if you're a typical -- I don't know how you work with your other funds, these other seedling funds or relationships that you have with these people, but the -- typically -- I mean, you'd be shocked at the lack of knowledge of the typical investment manager or fund manager of the fund or funds based upon the primary fund they invested. You know, they look at a fund, they know the basic concept of the fund. You know, they know, you know, if the guy's a -- but if you think that somebody that's an investor with in Sachs Capital knows what the hell his strategy is, it changes everyday, you know, and what he's investing in. They don't. They're basically just -- they're
chasing performance and they're looking at a track record of a particular strategy and they're going in -- into that strategy. I mean, so -- I mean, when we -- when asked what our role is with these various funds in the past, we said the same thing a hundred times, you know -- you know, we're the executing broker. Yes, we're the one that, you know, put on the strategy and we are rollers, we're good market timers. Nobody likes to use the term market timing anymore because it got tainted because of the mutual funds --

MR. VIJAY: Right.

MR. MADOFF: But trading in and out of the market is timing, okay, so what the -- if they ask, you know, how does Mad -- do you know how Madoff decides when he's going to go in the market and out of the market, which is a question people always ask me, not only -- and I'd say, you know, I'm not going to share that information with you, there's all sorts of -- we have -- you know, obviously, a lot of black box technology, momentum models and
all sorts of things that tell us when to get
in and out of the market. A regulator would
say is part of your information coming from
orders that you get from other brokerage
firms or institutions or -- the answer is,
no, that's illegal. No, we don't -- that's,
you know, in case we -- should we -- in case
someone never told you guys, you know, that's
-- you know, that's not something you're
allowed to do. So how do we determine how we
get in and out of the market, whether this is
a good time to put the strategy on, it's
based upon our feeling that the -- that the
market is going to move up, and that this is
a, you know, a time to be in the strategy and
the strategy is going to follow the market.
As to when we -- how we exit the market, by
the way, the model determines that. You
know, we don't get out of the market when we
think the market is -- is necessarily going
to go lower. That's a fallacy that some
people think. Basically the model is
programmed -- this is not something you have
to --
MR. VIJAY: No, this is just us, yeah.

MR. MADOFF: But the model is programmed that once certain parameters are broken it automatically generates, you know, a sell order to exit the market. So we -- we’re going to stay in the market as long as the parameters -- the model does what it’s supposed to do.

MR. VIJAY: Even if we’re, you know, like two strikes above -- above the call strikes?

MR. MADOFF: Right, so there are certain triggers that are built into the model.

Again, none of which you have great knowledge of, but the model determines when we get into the market, you know, and determines when we get out of the market. You have various models that determine that or various systems that determine that. So let me just finish this thing. So there’s no consist -- we took off.

MR. VIJAY: Yeah.

MR. MADOFF: On the split strike strategy E, okay, the simultaneous purchase. I know you keep saying that in your documentation,
but again that was -- you just have to -- you don't have to say simultan -- you just say the purchase of S&P put options. This is -- I have no idea what the last is or not. The rest of it -- it's a -- okay, on F, the market risk --

MR. VIJAY: Right.

MR. MADOFF: Okay, you -- where you go onto say in brackets, which may benefit the fund in rising markets, you see where --

MR. VIJAY: Yeah, I'm with you on that point.

MR. MADOFF: That should be taken out, the whole thing after that. The minimum correlation levels be breach, remedial action --

MR. VIJAY: Right.

MR. MADOFF: Because that's --

MR. VIJAY: That was all something in the prior trading authorization, right --

MR. MADOFF: Right. You basically -- all you have to basically just, you know, say is that the market risk is obviously that the correlation -- that the -- that the basket --
the market risk is the fault that we -- that
number one put on -- these are -- you know,
we put on a position and the market goes down
and it's a bullish -- you know, we're looking
for the market to go up and the market goes
down. So if -- if -- if the strategy is put
on -- is put on and you long the market
because you're basically always long in the
market even though you're limited -- you're
by the puts and by the calls. Basically if
-- the strategy is implemented because the
market -- because the -- Madoff thinks the
market is going up, and the market goes the
other way, you know, you're going to lose to
the difference of the strike price of the
put, and --

UNIDENTIFIED MALE: And the second --

MR. MADOFF: And, you know, so that's --
and the second is that the correlation
somehow or other breaks down the 95 percent
correlation breaks down, but then you'll --
the strategy is going to be sold, it's going
to be exited, but there's still going to be
some -- you know, some basic -- look, as far
as they're concerned, the -- any market
strategy has a certain degree of risk, even
if you have puts on it you have a -- you
know, as they say, the correlation cannot --
cannot hold and by the time you exit the
strategy you're going to lose the difference
between the correlation. It's never going to
be major, but you know it's not -- it's a
hedge strategy so therefore, you know, the
market risk is not that issue, and they're
not even going to get into that. They
shouldn't be getting into that because, you
know, as I mentioned to, I guess, Mark, when
I spoke to him last -- you're still there,
Mark, right?

MARK: I'm here, Bernie.

MR. MADOFF: Okay, is that you know one
of the -- one of the concerns that everybody
had with the SEC looking at all of these --
you know, the regulation of hedge funds was
that they were -- that they were going to go
too deeply into the strategies and that they
were going to inhibit everybody from using
the strategies, and they swore to everybody,
I mean not literally, but basically they assured Greenspan and the industry that they were not interested in the strategies, that that wasn’t what they wanted. They just wanted to be able to -- to make sure primarily that what they were telling clients in their documentation was the case, that they weren’t saying they were in the stock market strategy when they were in commodities, and that they were -- the valuations were correct that they were reporting their performance was accurate and things of that sort. They said they really did not have any business going into a -- or weren’t going to judge what people’s strategies were or whether they were -- strategies made any sense or not, but they’re full of shit, to describe it. Because as you can see, if that was really the case, then they wouldn’t be -- they wouldn’t ask you anything about a strategy. They would just say, okay, you know, this is the -- you know, the strategy we use, it’s an equity strategy and we’re buying equities, we’re not buying
soybeans. So, you know --

MR. VIJAY: I know it likely won’t come up and this is just more for our own background, but have you ever been asked or have you ever considered, you know, given --
given your models and your knowledge in 15 plus year history of sort of inverting it and putting on a bear spread, would it work or would it not?

MR. MADOFF: You could. I mean, you could do -- you could do -- you know, what we call a back spread.

MR. VIJAY: Right.

MR. MADOFF: You know, you could do that. You could also over weight the strategy with puts.

MR. VIJAY: Right.

MR. MADOFF: There’s lots of different things that you can do, but basically we found over -- and we used to do that years ago, but we found that the best way to avoid market risk is to be out of the market.

MR. VIJAY: Right, rather than --

MR. MADOFF: Rather than to try and --
rather than try and make money in a down
market because that's too -- it's just too
difficult.

MR. VIJAY: Mm-mm.

MR. MADOFF: There's not enough liquidity
when you want to do that, so basically the
strategy is when we like the market we're in
the strategy. When we don't like the market,
we're out of the market.

MR. VIJAY: Right.

MR. MADOFF: You know, the -- I think --
let me just see. I think -- I don't -- I
think I pretty much covered everything. Do
you have --

MR. VIJAY: One thing we didn't include
on the sheet because I -- you know, we
thought we're just here to talk about it
verbally, if the conversation with the
commission goes in this direction, we'll say
about, you know, what sorts of activities or
oversight do we actually, you know, conduct
based on the trade tickets, you know, the
sorts of things we talk about would be, you
know, the risk monitoring. We do feed the
positions into arithmetics --

MR. MADOFF: Fine?

MR. VIJAY: Risk reporting service and so, you know, we do monitor the exposure by -- by sector, the Greeks, you know, sensitivities in the data as well as (inaudible). That's all I think safe stuff, the standard stuff. We do monitor on a daily basis the trading activity against -- or the positions against, you know, the thresholds that we've outlined in the operating agreement or the trading authorization, so that's why it's good to have this updated one, and any time, in fact, that you know you're updating that document it would be great to get a copy.

MR. MADOFF: We should have -- nothing changed in the -- the reason -- the reason you probably never got one, and we did send them out, I wasn't sure whether you got one or not, but your stuff goes different places, but the parameters are identical. You'll see if you look at the two documents nothing is changed in them, it's just it was there -- in
other words the parameters of the options are the same and the parameters of the equities are the same. That hasn't changed at all. It is just, as they say, the -- it really should not -- it really never should have been part of a model document because the purpose of this document was twofold. Number one, to establish what the parameters are, and so that we did not have discretion that, you know, we've agreed these are the pre-set parameters and we've agreed to --

MR. VIJAY: Abide by them.

MR. MADOFF: To abide by them, and it's -- and when you see the ones for the -- what we call the terms and conditions for trading the -- trading the options, those parameters are the same, but the issue would be -- or made -- the other issue that we had was wanting to assure ourselves that if all of a sudden somebody gave this -- we found another fund or another broker that was -- that was not our client executing the same strategy using our model, and again as to what the value is or not, who the hell knows because
the reality of it it's our timing that's really the issue and our execution capability that's the advantage that we have, but we wanted that. But the -- so the document -- the model will hold up to intellectual property as it is to the equity side, but they said if you put the options in there, you know, that would not hold up, that's too broad and then what happens is it sort of -- it changed the intellectual property of the (inaudible), so we just broke it -- we broke it out and there's two -- two separate -- two separate documents. And also the reason why we couldn't make the option model or the parameters of the model were exact was when it comes to executing them it was because it didn't have certain liquidity issues in there which we use -- we use when we make that determination. From their standpoint they're not going to give a damn about one way or another. You have a trading authorization that tells you what your parameters are for the equities and what -- you wouldn't use the term trading authorization on the models.
because they're what's known as standing
instructions, terms and conditions. I think
we label it -- yeah, terms and conditions for
option hedging strategies. You'll see that.

MR. VIJAY: Right.

MR. MADOFF: That you have -- as far as
they're concerned, you can say you have
standard -- you have standing parameters that
Madoff has to follow when he executes the
option trade and you also -- you have certain
directives that he has in trading the equity
-- the equity piece.

MR. VIJAY: I know the options are still
-- I mean, they are all OTC at this stage, so
--

MR. MADOFF: Yes, yeah.

MR. VIJAY: So liquidity is important on
the listed counterparts when you're
transacting the OTC -- OTC options contracts
and --

MR. MADOFF: Yeah, those are done with --
those are done with derivative -- with
derivative dealers.

MR. VIJAY: Dealers, okay.
MR. MADOFF: That basically European Bank
and derivative banks, dealer banks. I'm just
trying to think. What else. And, you know,
I guess -- who's going to be on the call
Amit, just you and Mark?

MR. VIJAY: I think Mark will be on it.
Both of us will be on it.

MR. MADOFF: Yeah, I mean, you know with
these guys basically anything you can't
answer you basically just say I -- you know,
don't answer. You know, you just say -- you
know, I'm just not knowledgeable in that
aspect of it. You know, if again, if they
wanted to know more about the strategy, you
know, they know they can call me.

MR. VIJAY: Right.

MR. MADOFF: They know I'm the executing
broker. They know that you're not making the
decisions, so you don't have to be -- what
you basically said just recently about how
you monitor the risk and you monitor all of
that stuff, that's important. That's what
your job is and that's what you do and that's
what -- that's what today quite frankly what
investment managers do in all of these fund or funds. I mean, that’s what they do. They don’t -- they’re not -- they’re not making a decision when you invest whether or not the strategy is a good strategy. I mean, Mark, are you -- do you guys do that with your other funds?

MARK: Yeah, we do and Amid is heavily involved in all those risk calculations for --

MR. MADOFF: No, I mean -- I know the risk calculations, but I mean you’re not determining whether or not this strategy, other than from a performance standpoint you’re not involved in the execution aspects of any of these strategies.

MARK: Almost all of our funds are managed outside, and we have a sub advisory relationship. We have one small group at the end of the hall that run Arlington for us and that’s two portfolio managers running on one strategy.

MR. MADOFF: Good, right. So, whatever.

I mean, you know, look they say -- this --
this strategy -- the relationship that we have is been an established relationship for a long time. The commission knows how we -- how we operate, and even if they act stupid on the phone call with you like they're just trying to find out all of this information, you know, they basically -- they should know all of this unless it's just, you know, some people that don't know anything, but I would doubt it. You know, because they -- and they may not know anything when they speak to you tomorrow, but if they wanted to -- but I think, as they say, I -- my guess would be from what I think is going on here is basically that they are -- they're trying to establish the relationship between us, and us could be any broker, you know, and the funds and the -- whether there's any sort of cross dealing, any sort of sharing of profits that they're not aware of, all of those things because they -- the question that went around on a number of occasions through every broker that does business, you know, and I've seen them. Just like when they sent that sweet
questionnaire, Mark did -- you sent me a long
time ago.

MARK: Yeah.

MR. MADOFF: And they sent others out,
you know, to people in general terms. The
questions they all asked were do you invest
in any of these funds, are you a limited
partner in any of them, do you get
(inaudible) any of this stuff, is there any
information sharing -- all of this type of
stuff is they want to know -- and you see the
reason why you got a follow up call about
wanting to have this call on Wednesday is --
and even the questions, like you know is
there -- is Madoff -- you know, are there
other funds that are involved and is he --
what's his relationship with the funds, with
Fairfield, you know, and all of this stuff is
-- is there some other way that we could
benefit from the performance that we give you
outside of getting the commissions on the
transactions, the -- are the penny a share
and the dollar a contract on that sort of
stuff, is there anything else that he can
get? You know, does he get any sort of performance fee, is there any sort of other issue like, you know, like that, you know, that sort of thing? Even if you go back to, you know, the issues like -- that other people have raised questions about with this whole fund area, that's what they're looking at in here, and when they -- they -- when they did an examination for us, they asked all those questions, which is standard -- standard questions and the answer that I gave them, which are the case, are exactly what I'm -- I'm giving you and basically what you should respond to them. Obviously, not that we had a -- we didn't have a conversation on all of this stuff, but that's basically -- that's what they expect to hear and but they want to hear it with their own -- and I tell you, they just -- it's a typical fishing expedition that brokerage firms go through all the time and now you guys are going to wind up going through as a matter of routine.

MR. VIJAY: Okay, and so -- yeah, the Commission's charged they might ask if we
feel that they're fair and reasonable and of course at the levels that we talked about. I think it was up to four cents, right, that's what they are?

MR. MADOFF: Four cents a share, but that's what we get on the equity transactions, a dollar a contract on the --

MR. VIJAY: Okay.

MR. MADOFF: On the options and the treasury bills are -- there's no fee on those. Those are just cash management.

MR. VIJAY: This is a -- I mean, it's useful because it does -- I mean, this information is already known to us. There's nothing new, it just -- it just clarifies and put into context what the substance of their inquiry might be, and I see that it’s about, you know, establishing the relationship and the role that we each serve and -- you know and --

MR. MADOFF: Have any opportunity for -- to misuse any information, and that -- you know, as I say, that’s why when the first question you’re asked, I mean, do we call you
up and tell you what's going to get into the strategy or out of the strategy, that answer should be clearly no.

MR. VIJAY: Absolutely no.

MR. MADOFF: I have to send you up the new -- you know, the -- which is not really new, but the -- the other trading -- modified trading authorization directive and the terms and conditions for the options, and as I say, that's not something that you have to offer to give them. They've seen it anyhow, but as I say with them you don't offer anything unless they --

MR. VIJAY: Unless they ask.

MR. MADOFF: You know, unless you have no choice. Mark, is there anything else that you --

MARK: No, Bernie, I should let you know the call's now at 2 o'clock on Wednesday. Amit will be up here in New York. We'll have the binders in front of us, and I'll be able to, you know, pass him an note or he can write a question to me if we have any issues that come up on the call, but we'll be --
we’ll be together for that.

MR. MADOFF: Who changed the time; you
did or they did?

MARK: We did. I wanted to give Amit
time to get up here just so we could --

MR. MADOFF: Okay.

MARK: I have talked to him, it is a
voluntary call. It’s not going to be
recorded. They may --

MR. MADOFF: I’m sorry, I didn’t hear
you. What?

MARK: It’s a voluntary call.

MR. MADOFF: Right.

MARK: It isn’t testimony. They’re not
-- it’s not going to be -- there won’t be a
transcript. There won’t be a recording of
it. They may take notes, that’s about it.

MR. MADOFF: Who told you that; they did
or you asked them?

MARK: They did. I asked him questions
about it.

MR. MADOFF: Oh, okay. Okay, as far as
you know it’s just going to be -- did they
tell you who’s going to be on the call or
they didn’t?

MARK: They didn’t. I’m -- I’ll touch base with her one more time and see who this -- if this examiner’s on and what role he plays along with Simona and Melissa, the two staff attorneys.

MR. MADOFF: Okay, well it’s not going to matter. You might as well wait until they do it because I guess --

MARK: Okay.

MR. MADOFF: You don’t want them to think that you’re concerned about anything. With them you should -- your best off you just be, you know, casual.

MARK: We’re trying. We’re trying to be cool and to just cooperate and get it over with and get them out of here. You know, answer the question and move on.

MR. MADOFF: Okay, all right, so you’ll give me a call after it’s finished?

MARK: Yeah. Amit and I will probably let you know how it went.

MR. MADOFF: Okay, and it’s going to be 2 o’clock on Wednesday, okay. What else, what
else, what else. Okay. Okay, I'm going to
send that stuff up to you and I'll check --
onece you get it, walk, if you can give me a
call on my cell phone just to let me know
that you got it.

MARK: Sure.

MR. MADOFF: All right?

MARK: Okay, Bernie.

MR. MADOFF: Okay, great. Amit, take
care.

MR. VIJAY: Thank you, Bernie. Take care
then.

MR. MADOFF: Bye.

(Recording stops)