

JUDGE BATTS

09 CIV 5386

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

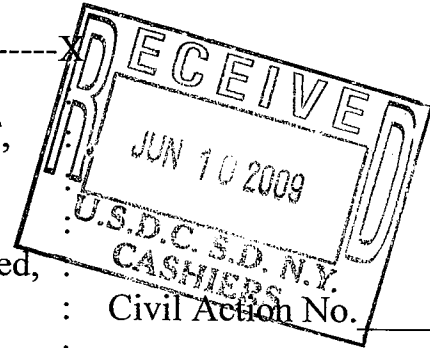
CRITERIUM CAPITAL FUNDS B.V., BBF TRUST,  
WALL STREET SECURITIES, S.A.,  
BANCA ARNER, S.A., and ALVARO CASTILLO,  
on behalf of themselves and all others similarly situated,

Plaintiffs,

v.

BERNARD L. MADOFF, KINGATE MANAGEMENT  
LIMITED, TREMONT (BERMUDA) LIMITED,  
FIM ADVISERS LLP, CITI HEDGE FUND  
SERVICES LTD., GRAHAM H. COOK,  
JOHN E. EPPS, SANDRA MANZKE,  
CHARLES SEBAH, KEITH R. BISH,  
CHRISTOPHER WETHERHILL, MICHAEL G.  
TANNENBAUM, PHILLIP A. EVANS, MARGARET  
EVERY, SHAZIEH SALAHUDDIN, JOHANN WONG  
and PRESTON M. DAVIS,

Defendants.



Civil Action No.

CLASS ACTION

JURY TRIAL  
DEMANDED

COMPLAINT

Plaintiffs, by and through their attorneys Boies, Schiller & Flexner LLP,  
hereby sue Defendants and allege, upon personal knowledge as to matters relating  
to themselves, upon information obtained during the course of their attorneys'  
investigation, and upon information and belief as to all other matters, as follows:

## NATURE OF ACTION

1. This suit arises out of the largest and longest-running “Ponzi scheme” in history, an enormous fraud orchestrated by defendant Bernard Madoff and facilitated by the reckless and grossly negligent conduct of the other Defendants, which cost investors many billions of dollars. This class action is brought on behalf of investors in Kingate Global Fund, Ltd. (“Kingate Global”) and Kingate Euro Fund, Ltd. (“Kingate Euro”), two of the so-called “feeder funds” that channeled billions of dollars into Madoff’s fraudulent operations. (References in this complaint to “the Funds” shall be to Kingate Global and Kingate Euro.)

2. Plaintiffs seek to recoup losses of some \$3.5 billion resulting from the Funds’ investment of class members’ assets in the Ponzi scheme conducted by Madoff and his firm, Bernard L. Madoff Investment Securities (“BMIS”). Plaintiffs and the class members were shareholders or equity holders in the Funds as of December 11, 2008, the date when Madoff’s fraud was revealed. (All references to “Plaintiffs” shall henceforth include the Class.)

3. Although Madoff operated the Ponzi scheme, Defendants solicited investments from Plaintiffs and oversaw, controlled, and managed those investments, which they turned over to Madoff after purportedly vetting and monitoring him and his operations. Defendants in fact did not properly vet or monitor Madoff and, instead, falsely reported steadily-increasing account values to

Plaintiffs while paying themselves hundreds of millions of dollars in fees based on those fictitious amounts. As a result, Defendants are responsible for Plaintiffs' massive losses.

4. Defendants directly owed duties to Plaintiffs, including fiduciary duties, to conduct due diligence and provide accurate and complete information about Plaintiffs' investments in the Funds and in Madoff's operation (both before and after the initial investments were made), to exercise care with Plaintiffs' investments, to monitor Madoff (who they designated to carry out the Funds' investment strategy), and to safeguard Plaintiffs' assets. Rather than complying with their representations and duties, the Defendants used the Funds as mere conduits to Madoff. The loss of Plaintiffs' assets in the Madoff Ponzi scheme is a direct and proximate result of Defendants' false representations and failure to fulfill their duties to Plaintiffs.

5. Defendants wrongfully collected millions of dollars in fees based on their purported management of Plaintiffs' investments, including fees based on the fictitious profits supposedly generated by Madoff for Plaintiffs. As a result of Defendants' wrongful actions, Plaintiffs' assets were stolen rather than invested. Because there were no profits on the non-existent investments, Defendants wrongfully collected the fees from the Funds. A constructive trust must be

imposed on those fees and against those who hold them, so that the fees can be returned to Plaintiffs.

## PARTIES

### Plaintiffs

6. Due to the acts alleged herein, the Plaintiffs identified below have lost their investments in the Funds as of December 11, 2008, and also have paid substantial investment, placement, management, and performance fees that were wrongfully charged based on fictitious investment returns.

7. Plaintiff **Criterion Capital Funds, B.V.**, is a Netherlands Antilles private limited liability company (“besloten vennootschap”) that invested assets in Kingate Global beginning on January 1, 1999.

8. Plaintiff **BBF Trust** is a trust formed under the laws of the Commonwealth of the Bahamas that invested assets in Kingate Global beginning in October 1997.

9. Plaintiff **Wall Street Securities, S.A.**, is a Panamanian corporation that invested assets in Kingate Global beginning in November 2008.

10. Plaintiff **Banca Arner S.A.** is a Swiss corporation that invested assets in Kingate Global beginning in July 1997 and Kingate Euro beginning in May 2000.

11. Plaintiff **Alvaro Castillo** is an individual residing in Switzerland who invested assets in Kingate Global beginning on October 30, 2008.

Defendants

12. Defendant **Bernard Madoff** (“Madoff”) orchestrated the Ponzi scheme into which the other Defendants funneled Plaintiffs’ investments and directed the fraudulent activities of BMIS. Madoff is a resident of New York. He is now incarcerated in the Metropolitan Correctional Center following his guilty plea to multiple counts of fraud and other crimes.

13. Defendant **Graham H. Cook** (“Cook”) is a Director of both Kingate Global and Kingate Euro and, in addition to his wrongful actions on behalf of the Funds, breached duties he owed directly to Plaintiffs. Mr. Cook is a resident of the British Virgin Islands. As a director of Kingate Global and Kingate Euro, Mr. Cook had knowledge of, and participated in, the Funds’ transaction of business within the state of New York, including maintaining of investment accounts in New York, consenting to the transactions related to those accounts, and otherwise by exercising control over the Funds.

14. Defendant **John E. Epps** (“Epps”) is a Director of both Kingate Global and Kingate Euro and, in addition to his wrongful actions on behalf of the Funds, breached duties he owed directly to Plaintiffs. Mr. Epps is a resident of Bermuda. As a director of Kingate Global and Kingate Euro, Mr. Epps had

knowledge of, and participated in, the Funds' transaction of business within the state of New York, including maintaining of investment accounts in New York, consenting to the transactions related to those accounts, and otherwise by exercising control over the Funds.

15. Defendant **Sandra Manzke** ("Manzke") was a Director of Kingate Global from 1995 until at least 2003. In addition to her wrongful actions on behalf of Kingate Global, Ms. Manzke breached duties he owed directly to Plaintiffs. Ms. Manzke was also Chairman and co-CEO of Tremont Advisers, Inc., the parent company of Tremont (Bermuda) Limited. As a director of Kingate Global, Ms. Manzke had knowledge of, and participated in, Kingate Global's transaction of business within the state of New York, including maintaining of investment accounts in New York, consenting to the transactions related to those accounts, and otherwise by exercising control over Kingate Global. Ms. Manzke is a citizen of New York.

16. Defendant **Charles D. Sebah** ("Sebah") was a Director of Kingate Global, from 1995 and until at least 2003. In addition to his wrongful actions on behalf of Kingate Global, Mr. Sebah breached duties he owed directly to Plaintiffs. As a director of Kingate Global, Mr. Sebah had knowledge of, and participated in, Kingate Global's transaction of business within the state of New York, including

maintaining of investment accounts in New York, consenting to the transactions related to those accounts, and otherwise by exercising control over Kingate Global.

17. Defendant **Keith R. Bish** (“Bish”) was a Director of Kingate Global, from 1995 to 2002. Bish is a citizen of the United Kingdom residing in the British Virgin Islands. In addition to his wrongful actions on behalf of Kingate Global, Mr. Bish breached duties he owed directly to Plaintiffs. As a director of Kingate Global, Mr. Bish had knowledge of, and participated in, Kingate Global’s transaction of business within the state of New York, including maintaining of investment accounts in New York, consenting to the transactions related to those accounts, and otherwise by exercising control over Kingate Global.

18. Defendant **Kingate Management Limited** (“Kingate Management”) is a corporation organized under the laws of Bermuda on February 24, 1994. Kingate Management manages capital and investments for Kingate Global and Kingate Euro, pursuant to “manager agreements” with each Fund. Kingate Management’s duties include managing all aspects of the investment advisory services provided to Kingate Global and Kingate Euro, including selection and evaluation of the Fund’s Investment Advisor, in this case Madoff’s company, BMIS. Kingate Management was also responsible for arranging for all accounting and administrative services for the Funds. Kingate Management was not registered with the SEC as an investment advisor under the Investment Advisers Act of 1940.

Kingate Management transacted business related to the Funds in New York, including maintaining of an investment account with a New York broker-dealer.

19. Defendant **Christopher Wetherhill** (“Wetherhill”) is a Director of Kingate Global, Kingate Euro, and Kingate Management. Wetherhill has been a Director of Kingate Global and Kingate Management since 1995 and a Director of Kingate Euro since the Fund’s inception. Mr. Wetherhill, a citizen of the United Kingdom, is a resident of Bermuda. As a director of Kingate Global, Kingate Euro, and Kingate Management, Mr. Wetherhill had knowledge of, and participated in, the Funds’ transaction of business within the state of New York, including maintaining of investment accounts in New York, consenting to the transactions related to those accounts, and otherwise by exercising control over the Funds. In addition to his wrongful actions on behalf of the Funds, Mr. Wetherhill breached duties he owed directly to Plaintiffs.

20. Defendant **Michael G. Tannenbaum** (“Tannenbaum”) is a Director of Kingate Management. In addition to overseeing and directing Kingate Management’s wrongful actions on behalf of the Funds, Mr. Tannenbaum owed duties directly to Plaintiffs. Mr. Tannenbaum is a United States citizen and domiciliary of New York. Mr. Tannenbaum transacted business related to Kingate Management in New York.



21. Defendant **Phillip A. Evans** (“Evans”) is a Director of Kingate Management. Mr. Evans is a resident of Monaco. As a director of Kingate Management, Mr. Evans had knowledge of, and participated in, the Funds’ transaction of business within the state of New York, including maintaining of investment accounts in New York, consenting to the transactions related to those accounts, and otherwise by exercising control over the Funds. In addition to his wrongful actions on behalf of the Funds, Mr. Evans breached duties he owed directly to Plaintiffs.

22. Defendant **Margaret Every** (“Every”) was a Director of Kingate Management. As a director of Kingate Management, Ms. Every had knowledge of, and participated in, the Funds’ transaction of business within the state of New York, including maintaining of investment accounts in New York, consenting to the transactions related to those accounts, and otherwise by exercising control over the Funds. In addition to her wrongful actions on behalf of the Funds, Ms. Every breached duties he owed directly to Plaintiffs.

23. Defendant **Shazieh Salahuddin** (“Salahuddin”) is a Director of Kingate Management. Ms. Salahuddin is a resident of Bermuda. Ms. Salahuddin is also a senior employee of the FIM group of companies. As a director of Kingate Management, Ms. Salahuddin had knowledge of, and participated in, the Funds’ transaction of business within the state of New York, including maintaining of

investment accounts in New York, consenting to the transactions related to those accounts, and otherwise by exercising control over the Funds. In addition to her wrongful actions on behalf of the Funds, Ms. Salahuddin breached duties he owed directly to Plaintiffs.

24. Defendant **Tremont (Bermuda) Limited** (“TBL”) is a corporation organized under the laws of Bermuda on November 16, 1988. TBL is a wholly-owned subsidiary of Tremont Group Holdings, Inc. (formerly Tremont Advisers, Inc.), a Delaware corporation registered as a foreign corporation in New York. TBL was a Co-Manager of Kingate Global through at least 2003. TBL’s duties included managing all aspects of the investment advisory services provided to the Kingate Global, including selection and evaluation of the Investment Advisor, in this case BMIS. TBL was further responsible for arranging for all accounting and administrative services for Kingate Global. TBL transacted business related to Kingate Global in New York, including maintaining an investment account with a New York broker-dealer.

25. Defendant **Johann Wong** (“Wong”) was President and a Director of TBL from 1994 to 2005. Mr. Wong is a Canadian citizen and a domiciliary of Connecticut. As a director of TBL, Mr. Wong had knowledge of, and participated in, the Funds’ transaction of business within the state of New York, including maintaining of investment accounts in New York, consenting to the transactions

related to those accounts, and otherwise by exercising control over the Funds. In addition to his wrongful actions on behalf of the Funds, Mr. Wong breached duties he owed directly to Plaintiffs.

26. Defendant **Preston M. Davis** (“Davis”) was the Accounting Manager for TBL from at least 1995 to 2003. As Accounting Manager of TBL, Mr. Davis had knowledge of, and participated in, the Funds’ transaction of business within the state of New York, including maintaining of investment accounts in New York, consenting to the transactions related to those accounts, and otherwise by exercising control over the Funds. In addition to his wrongful actions on behalf of the Funds, Mr. Davis breached duties he owed directly to Plaintiffs.

27. Defendant **FIM Advisers LLP** (“FIM”) is a limited liability partnership incorporated under the laws of the United Kingdom. FIM is an asset management company specializing in the management of hedge fund portfolios for institutions and private clients. FIM is regulated by the Financial Services Authority of the United Kingdom. Pursuant to a Consulting Services Agreement dated August 1, 2005, FIM rendered consulting advice and services to Kingate Management with respect to the Funds’ investment, operational, administrative, marketing, accounting, and legal matters. FIM is the successor-in-interest to FIM Limited, a limited liability company formed in 1980, under the laws of England and Wales. FIM acted in New York under the Consulting Services Agreement

through its agent, **FIM (USA) Inc.** (“FIM USA”), a Delaware corporation qualified to do business in New York.

28. Defendants Kingate Management, TBL, FIM, Cook, Epps, Manzke, Sebah, Bish, Wetherhill, Tannenbaum, Evans, Every, Salahuddin, Wong, and Davis are referred to collectively as the “Kingate Defendants.”

29. Defendant **Citi Hedge Fund Services Limited** (“Citi”), formerly known as BISYS Hedge Fund Services Limited, is incorporated under the laws of Bermuda. Citi is responsible for all matters pertaining to the administration of Kingate Global and Kingate Euro, including communications with shareholders and the general public, soliciting sales of the Funds’ shares, accepting subscriptions for share purchases, maintaining the Funds’ corporate records and accounts, distributing payments of dividends and fees, calculating and publishing the subscription and redemption prices and net asset values of the Funds, conducting meetings of the Funds’ shareholders and directors, and making redemptions from the Funds. Citi is an affiliate of Citigroup, Inc., and Citi Hedge Fund Services, Inc., a Delaware corporation registered to do business in New York. Citi is the successor-in-interest to Hemisphere Management Limited, the prior administrator of Kingate Global and Kingate Euro. Citi administered Plaintiffs’ investments in the Funds’ New York investment accounts by communicating subscription and redemption requests to Madoff.

## JURISDICTION AND VENUE

30. This Court has jurisdiction over this dispute pursuant to the Class Action Fairness Act of 2005, *codified at* 28 U.S.C. § 1332(d)(2)(B). The amount in controversy in this action exceeds \$5,000,000. The Class consists of more than 100 individuals; at least one Plaintiff is a citizen of a foreign state and at least one Defendant is a citizen of New York.

31. This Court has personal jurisdiction over all Defendants because all Defendants have maintained minimum contacts with New York related to Plaintiffs' claims by transacting business and engaging in continuous activity in the state of New York, including:

- a. Establishing investment accounts with BMIS in New York;
- b. Maintaining ongoing investment activity in BMIS accounts, including transferring all of Plaintiffs' investments to BMIS in New York as custodian of such assets;
- c. Making telephone calls, faxing and mailing documents and directing computer and internet communications to New York;  
and
- d. Receiving fees derived from the foregoing activity conducted in New York.

32. Venue is proper in this District pursuant to 28 U.S.C. § 1391(a)(3), as one or more of the individual Defendants reside in this District.

### **FACTUAL ALLEGATIONS**

#### **A. Madoff's Massive Ponzi Scheme**

33. Madoff founded BMIS in 1960, and eventually expanded the firm to a worldwide client base. Since at least 1990, Madoff perpetrated a massive Ponzi scheme through the investment advisory services of BMIS. Rather than investing assets in actual securities as represented by him and Defendants, Madoff fraudulently used those assets for his personal benefit (and the benefit of his family and associates) and otherwise distributed them to prior investors to create the illusion of profits. BMIS's account statements, which purported to set forth trades in equities and options using the assets turned over by the Funds, as well as trading gains and losses and securities holdings, including U.S. Treasury bills, were during the time the Funds existed entirely fictitious, and no trades of securities were executed for years.

34. The size of Madoff's global fraud has been estimated at \$64.8 billion, based upon the reported value of approximately 4,800 BMIS client accounts as of November 30, 2008. Madoff's fraudulent scheme unraveled in December 2008 when BMIS did not have sufficient funds to cover investors' redemption requests. On December 11, 2008, Madoff was arrested and charged in a criminal complaint

after admitting that his money management operations were “all just one big lie” and “basically, a giant Ponzi scheme.” On March 12, 2009, Madoff pleaded guilty to an 11-count criminal complaint, including fraud, perjury, theft from an employee benefit plan, and two counts of international money laundering. He is now incarcerated awaiting sentencing.

35. At his plea hearing, Madoff explained that he had been paying returns to certain investors out of the assets received from other investors. Madoff stated that BMIS was insolvent and had been for years. Madoff estimated the losses from his fraud to be approximately \$50 billion.

**B. Kingate Funneled Plaintiffs’ Assets to Madoff**

36. **Kingate Global** is an open-end investment company organized as an international business company under the laws of the British Virgin Islands. Kingate Global commenced operation in 1994. Shares in Kingate Global were first sold on March 1, 1995. Since its inception, all, or substantially all, of Kingate Global’s assets were invested with Madoff. Plaintiffs acquired shares or equity in Kingate Global when they turned over their assets to the Kingate Defendants, who in turn funneled them to Madoff.

37. **Kingate Euro** is an open-end investment company organized as an international business company under the laws of the British Virgin Islands. Kingate Euro commenced operations on May 1, 2000. Since its inception, all, or

substantially all, of Kingate Euro's assets were invested with Madoff. Plaintiffs acquired shares or equity in Kingate Euro when they turned over their assets to the Kingate Defendants, who in turn funneled them to Madoff.

38. Each member of the class invested in either Kingate Global or Kingate Euro. The investments were made outside of New York. Kingate Global, Kingate Euro, and Kingate Management, in turn, delegated all investment duties and custody of the investments to Madoff and BMIS, both located in New York, where they operated the Ponzi scheme.

39. The Funds used Madoff as their sole Investment Advisor from their inception. Madoff was described by the Kingate Defendants as a "New York based NASD registered broker-dealer employing approximately 350 people and acting primarily as a market-maker in listed and unlisted stocks and convertible securities." (Kingate Global Fund, Ltd. Amended and Restated Information Memorandum, October 6, 2008, at 14 [hereinafter KGF 2008 IM]; Kingate Euro Fund, Ltd. Amended and Restated Information Memorandum, October 6, 2008, at 15 [hereinafter KEF 2008 IM]; Kingate Global Fund, Ltd. Amended and Restated Information Memorandum, August 1, 2007, at 14 [hereinafter KGF 2007 IM]; Kingate Global Fund, Ltd. Amended and Restated Information Memorandum, May 1, 2006, at 14 [hereinafter KGF 2006 IM]; Kingate Global Fund, Ltd. Amended and Restated Information Memorandum, January 15, 2003, at 15 [hereinafter KGF



2003 IM]; *see also* Kingate Global Fund, Ltd. Information Memorandum, May 1, 2000, at 15 [hereinafter KGF 2000 IM].) Reportedly, over \$3 billion was invested in Kingate Global and Kingate Euro, and virtually all of those moneys were funneled to Madoff.

40. The losses that Plaintiffs suffered when the Funds collapsed would have been avoided if Defendants had fulfilled their duties to Plaintiffs, if they had lived up to their own representations, and if they had adequately investigated and monitored Madoff and BMIS. In failing to do so, Defendants breached their duties to Plaintiffs and the Class, and effectively wiped out the investments of Plaintiffs and the Class. At the same time, the fund managers of Kingate Global and Kingate Euro paid themselves millions of dollars in fees. For instance, Kingate Management's fees were approximately \$38 million in 2007 and \$35 million in 2006.

41. By virtue of their education, business experience and sophistication, and the dominant role that the Madoff relationship played in the business of the Funds, each of the Defendants either knew or should have known of the "red flags" associated with Madoff's operation and either knew or should have known the true facts alleged herein with regard to Kingate's false representations and lack of due diligence with respect to Madoff's operations.

**C. Kingate Defendants Falsely Represented the Funds' Investments With Madoff and the Absence of Due Diligence and Oversight of Madoff's Operations**

42. Beginning in 1995 and continuing to December 11, 2008, the Kingate Defendants marketed the Funds on the basis of false and misleading representations and omissions. The Information Memoranda issued by the Kingate Defendants consistently – and falsely – described the investment strategy of the Funds as seeking to obtain capital appreciation of assets principally through a “split-strike conversion” strategy. For example, according to the Information Memoranda, Madoff used a “non-traditional investment strategy” to achieve long-term capital appreciation “that is a variation of the traditional ‘option conversion’ strategies,” known as “split-strike conversion.” (KGF 2008 IM, at 2; KEF 2008 IM, at 1-2; KGF 2007 IM, at 2; KGF 2006 IM, at 2; KGF 2003 IM, at 2; KGF 2000 IM, at 2-3.) These representations were false, since Madoff did not use the split-strike conversion investment strategy or make any investments at all.

43. The May 1, 1996, Information Memorandum for Kingate Global (“KGF 1996 IM”), by which investments in the Funds were solicited, represented to investors that the Kingate Defendants would exercise care and due diligence in selecting and monitoring Madoff, that Defendants had transparency with respect to Madoff and his operations, and that they would exercise oversight over Madoff:

- a. “In selecting a particular Investment Advisor to which [Kingate Global] will allocate assets, the Co-Managers will be guided by” factors such as the “Investment Advisor’s past performance and reputation”; the “[s]ize and efficiency of assets managed”; the “[c]ontinued favorable outlook for the strategy employed”; and the “[a]bility of [Kingate Global] to make withdrawals or liquidate its investment.” (KGF 1996 IM, at 1.)
- b. “[T]he Co-Managers have agreed . . . to manage all aspects of the investment advisory services provided to the Fund, including the selection and evaluation of the Investment Advisors and the allocation of the Fund’s assets among the Investment Advisors.” (KGF 1996 IM, at 19.)
- c. “The Co-Managers, in their sole discretion, arrange for the investment of the Fund’s assets by the Investment Advisors.” (KGF 1996 IM, at 19.)
- d. “The Co-Managers have an international perspective regarding investments and believe that by allocating the Fund’s investment portfolio either directly or through one or more Sub-Funds among a limited number of above-average Investment Advisors having different investment styles and strategies and

emphasizing various techniques, products and geographic markets, the impact of any one such style, strategy or market on investment performance will be diluted.” (KGF 1996 IM, at 20.)

- e. “The Co-Managers collect, analyze and evaluate information regarding the personnel, history and background, and the investment styles, products, strategies and performance of professional investment management firms.” (KGF 1996 IM, at 20.)
- f. “FIM researches, screens and nominates of [sic] selection by Co-Manager Kingate investment advisors that may be appointed to manage the Fund’s assets. Based upon its analysis, FIM makes recommendations to Co-Manager Kingate concerning a proposed allocation of assets among asset classes and among investment advisors that it believes are suitable for the investment program of the Fund’s various Classes of shares.” (KGF 1996 IM, at 20-21.)
- g. “FIM continuously monitors the asset allocation made by the Fund among various asset classes and among investment advisors.” (KGF 1996 IM, at 21.)

- h. “Based upon its continuous analysis of the performance of the investment advisors, FIM will recommend changes in the allocation of the Fund’s assets among different investment advisors.” (KGF 1996 IM, at 21.)

These representations were false because, at the least, the Kingate Defendants did not conduct the represented due diligence and oversight of Madoff.

44. In later Information Memoranda from 2000 through 2008, the Kingate Defendants repeated representations regarding how assets in the Fund were invested:

- a. “The Fund seeks to obtain capital appreciation of its assets through the utilization of a non-traditional stock/options trading strategy,” i.e., the split-strike conversion. (KGF 2008 IM, at 2; KEF 2008 IM, at 2; KGF 2007 IM, at 2; KGF 2006 IM, at 2; KGF 2003 IM, at 2; KGF 2000 IM, at 2.)
- b. The split-strike conversion investment strategy “entails: purchasing a basket of forty-five (45) to fifty (50) large-capitalization S&P 100 stocks . . . which together account for the greatest weight of the Index . . . selling out-of-the money S&P 100 Index call options representing a dollar amount of the underlying Index equivalent to the dollar amount of the basket

of shares purchased;” and “purchasing out-of-the money or at-the-money S&P Index put options in the same dollar amount.” (KGF 2008 IM, at 2; KEF 2008 IM, at 2; KGF 2007 IM, at 2; KGF 2006 IM, at 2; *see also* KGF 2003 IM, at 2-3; KGF 2000 IM, at 2.)

- c. “The investment advisor is a New York based NASD registered broker-dealer employing approximately 350 people and acting primarily as a market-maker in listed and unlisted stocks and convertible securities . . . . The Manager has established a discretionary account with such Investment Advisor on behalf of the Fund for the management of the USD assets. The Investment Advisor utilizes a ‘split strike conversion’ strategy consistent with the strategy of the Fund. . . .” (KGF 2008 IM, at 14; KEF 2008 IM, at 15; KGF 2007 IM, at 14; KGF 2006 IM, at 14; *see also* KGF 2003 IM, at 15.)
- d. Kingate Management, pursuant to the Manager Agreement, “manage[d] all aspects of the investment advisory services provided to the Fund, including selection and evaluation of the Investment Advisor.” (KGF 2008 IM, at 13; KEF 2008 IM, at

14; KGF 2007 IM, at 13; KGF 2006 IM, at 13; KGF 2003 IM, at 14).

These representations were false because the represented investment strategy was in fact not followed and Defendants conducted no meaningful evaluation of Madoff; indeed, there was no investment of Plaintiffs' assets in any legitimate securities.

45. In their correspondence to Plaintiffs, Defendants repeated the misrepresentation that the assets in the Funds were legitimately invested and misrepresented the status of the investments. For example, as recently as October 2008, Kingate Management represented that Kingate Global's "portfolio [invested with Madoff] started the month 100% invested in US Treasury bills and ended the month with the same positions." (Kingate Global Fund, October 2008 Update.) Defendants had no reasonable basis for making that statement, which was false because the assets of the Fund were not invested in U.S. Treasury bills or in any other securities.

46. Through FIM, the Kingate Defendants consistently represented to Plaintiffs the high level of diligence and risk monitoring they conducted with respect to investment managers such as Madoff, including the following:

- a. “Regular reviews of markets, strategies, managers and peer groups on a qualitative and quantitative basis are used to evaluate and monitor changes in risk factors and profiles”:
- b. “[R]esearch specialists will . . . conduct in-depth analysis into every aspect of a fund, its manager and its service providers”;
- c. Members of the Investment Committee “review and analyse all aspects of the strategy, manager, risk and operational due-diligence to ensure completeness of process and suitability for investment”;
- d. “Each portfolio is subject to continuous analysis to ensure all risk factors are identified and controlled and all internal and external management portfolio policies are adhered to”; and
- e. “Strategy and manager conclusions are subject to active monitoring by the research teams, investment committee and risk management to ensure accuracy of analysis.”

FIM, Research & Investment, <http://www.fim-group.com/research.asp>. These representations were false because the Kingate Defendants did not conduct the represented due diligence, monitoring or oversight.

47. Although the Kingate Defendants represented that they would delegate “all investment management duties with regard to USD Shares to the



Investment Advisor,” in this case Madoff (KGF 2008 IM, at 5; KEF 2008 IM, at 6; KGF 2007 IM, at 5; KGF 2006 IM, at 5; KGF 2003 IM, at 5; KGF 2000 IM, at 5), Kingate Management explicitly retained control over Kingate Global and Kingate Euro: “All decisions with respect to the general management of the Fund are made by the Manager, who has complete authority and discretion in the management and control of the business of the Fund.” (KGF 2008 IM, at 4; KEF 2008 IM, at 5; KGF 2007 IM, at 4; KGF 2006 IM, at 4; *see also* KGF 2003 IM, at 5; KGF 2000 IM, at 5.) These representations were false because the Kingate Defendants in fact turned over to Madoff Plaintiffs’ investments in the Funds and abdicated their responsibility and discretion with respect to control of the invested assets.

48. Defendants sent periodic, false updates to the Plaintiffs regarding the performance of Kingate Global, representing, for example, the following:

- a. “Kingate USD performed well in November [2008] closing the month with a gain of +1.45% after fees” (Kingate Global Fund, November 2008 Update);
- b. Three year returns of 30.78% (Kingate Global Fund, October 2008 Update); and
- c. Five year returns of 51.94%.

These representations were false, and Defendants had no reasonable basis for making them. The Fund in fact did not “perform well” in November 2008 or any other month, nor did it ever achieve the represented returns.

49. Defendants likewise sent periodic updates to the Plaintiffs regarding the purported performance of Kingate Euro, representing the following:

- a. “Kingate Euro performed well in November [2008] closing the month with a gain of +1.34% after fees” (Kingate Euro Fund, November 2008 Update);
- b. Three year returns of 25.06% (Kingate Euro Fund, October 2008 Update); and
- c. Five year returns of 43.53%.

These representations were false and Defendants had no reasonable basis for making them. The Fund did not in fact hold the represented assets or achieve the represented investment return.

50. By making these false representations alleged above, by failing to act with diligence, and by failing to confirm the accuracy of the information disseminated to Plaintiffs, the Kingate Defendants were grossly negligent, breached their duties to Plaintiffs and did not act in good faith.

**D. Defendants Ignored Red Flags That Madoff Was Operating a Ponzi Scheme**

51. In addition to making false representations, the Kingate Defendants failed to react to or to disclose, in the Investment Memoranda or elsewhere, the existence of numerous “red flags” regarding the conduct of Madoff’s business, which should have put them on notice that Madoff was not operating a legitimate investment fund. These red flags included the lack of any transparency into Madoff’s actual operations, the lack of segregation of duties with respect to the trading and custody of assets, Madoff’s reporting to Defendants of purported securities trades at prices outside the actual trading ranges, inadequate auditing of Madoff’s operations, and the consistently profitable returns for a fund pursuing the stated strategy, which were not attainable.

52. The Kingate Defendants ignored the warning flag of Madoff’s use of Friehling & Horowitz (“F&H”), an unknown accounting firm that was plainly unequipped to audit a company of BMIS’s size. The firm had only three employees – a retired partner living in Florida, a secretary, and one active certified public accountant. While F&H was a member of the American Institute of Certified Public Accountants (“AICPA”), it had not been subjected to a peer review since 1993 – a requirement of membership of AICPA – because F&H represented to the AICPA, in writing, that it did not perform any audits. This information was ignored by the Kingate Defendants.

