

# Exhibit 1

*Picard v. Katz*, No. 11 Civ. 3605 (JSR)  
Expert Report of John Maine

**I. Introduction**

I have been retained by Davis Polk & Wardwell to provide expert testimony in the litigation known as *Picard v. Katz*. I have been asked to testify regarding topics including private wealth management practices in the financial industry, how brokers operate with regard to client assets and the customer's ability to do due diligence with respect to broker operations, and the nature of securities brokerage accounts, including those in this case.

This report presents my observations and conclusions.

**II. Summary of Qualifications and Compensation**

Attached to this report, as Exhibit A, is my curriculum vitae, detailing my qualifications as an expert in the securities industry. Also attached, as Exhibit B, is a list of cases in the last four years in which I have testified as an expert. I am compensated at the rate of \$385 per hour.

**III. Facts and Data Relied Upon**

In forming my opinions as presented in this report, I relied upon my years of experience in the financial industry, which includes involvement in over fifteen hundred arbitrations and court cases between customers and brokers, in which I usually represent the broker. I reviewed sample account documents issued by Bernard L. Madoff Investment Securities ("BLMIS"), including trade confirmations, monthly statements and 1099s. I also reviewed the Broker Check Report regarding BLMIS prepared by the Financial Industry Regulatory Authority ("FINRA"), which is available on FINRA's website. Finally, I reviewed the

amended complaint, the memoranda of law submitted with respect to Defendants' motion to dismiss the amended complaint, and the Court's opinion thereon dated September 27, 2011.

#### **IV. Summary of Opinions**

##### **A. Investment Management Vehicles**

An individual or entity that wishes to invest in securities may consider doing so in various ways. Two of the most common include using the services of a broker-dealer and investing in some type of pooled fund.

A "broker-dealer" is, among other things, engaged in the business of buying or selling securities for customers. In this regard, the broker-dealer functions as a securities intermediary that maintains securities accounts for customers, *i.e.* a broker. In addition to operating as an agent, the broker-dealer may operate as a dealer, *i.e.* buying or selling for its own account. Because broker-dealers buy and sell securities directly for specific customers, they are different from hedge funds or mutual funds. Hedge funds and mutual funds also trade in securities, but they are not "middle men" acting for customers. Instead, they sell investors percentage interests in the funds themselves and distribute investment returns proportionately to each interest holder.

When a customer invests through a broker-dealer, the customer provides funds to the broker for the purchase of securities that will be held for the benefit of the customer. After purchasing a security the customer is entitled to the benefits of owning that specific security. In addition, the customer can give the

broker specific instructions about the operation of his account, *i.e.*, what securities to buy or hold.

When a customer invests in a pooled fund such as a hedge fund or a mutual fund, he is not buying a specific security—he is buying a portion of a pool of assets, and he owns a percentage of that fund. The investor will receive his proportional share of the investment results generated by that fund. He cannot buy or sell any security that is part of the pool, he can only buy and sell an interest in that pool.

Broker-dealers may also invest in a functionally similar manner for customers. They can pool client assets and trade blocks of securities on behalf of multiple customers. All of the customers are then given the average price paid or received on those trades. Bulk transactions of this type are very typical in private wealth management accounts. Based on my experience, I would estimate that nearly 95% of private wealth managers use this technique to trade on behalf of customers. I understand that BLMIS used this technique, buying and selling baskets of securities that were then allocated to customers.

**B. Investment Advice**

In my experience, most wealthy individuals hire professionals to manage their investment securities, whether they invest through a broker or in a fund. There are several reasons for this. First, successful people are generally busy doing whatever has made them successful. Monitoring the markets requires an enormous investment of time, time that a successful person normally does not

have. Retaining an experienced professional permits a busy customer to use his time to engage in his own area of expertise while still participating in the market.

Second, while wealthy investors may have sophisticated knowledge of their own career specialty, this does not mean that they have sophisticated knowledge of the financial markets. Even if they did take the time to manage their own investments, it is unlikely that customers who are not financial market experts will achieve as good a return as will a professional. To be in the best position to be successful, an investor should have a high level of expertise and sophistication regarding securities and markets. Investment markets are complex, and increasingly dominated by investment professionals. Moreover, the markets are increasingly global. While in the past an individual investor might have been able to focus primarily on investment opportunities in domestic companies with which they were personally familiar, in today's global economy, evaluating investment opportunities requires consideration of global market trends and industry changes.

Third, as securities markets have become increasingly sophisticated, so have investment strategies. Many of the new techniques used in investing, such as employing securities options to hedge investments, are normally carried out by specialists. A non-professional investor would likely be unable to achieve results that could compete with those attainable by such specialists.

Therefore, to save time and in the hope of achieving better returns, wealthy investors generally turn to professionals, whose careers are devoted to analyzing investment opportunities and strategies. To accomplish these goals,

investors often open a private wealth management account with an investment professional. Nearly all brokerage firms have private wealth management groups, and it is one of the fastest growing parts of the financial industry.

Such professionals are often “registered investment advisors,” persons registered with the Securities and Exchange Commission (“SEC”) who manage the investments of others. An investment advisor with more than \$100 million under management must register with the SEC. Such professionals are generally compensated in one of three ways. They can charge clients a fee, they can generate commissions on trades, or they can employ some combination of the two methods.

**C. Discretionary vs. Non-Discretionary Accounts**

Brokerage accounts fall into two categories: non-discretionary and discretionary.

In non-discretionary accounts, the customer retains decision-making authority, and the broker must obtain the customer’s consent prior to making any trades. A person who wants to be responsible for the management of his account will likely have a non-discretionary account so that he can invest according to his own strategy.

In a discretionary account, the customer delegates all investment decision-making authority to the broker. The customer gives the broker the right to decide on the investment strategy, which will guide the broker’s decisions as to which securities to buy or sell, and when to buy or sell them. In a discretionary account, the broker does not need to obtain the client’s consent prior to making trades.

In my experience, the majority of private wealth management accounts are discretionary. This is because, as discussed, most wealthy investors do not have the time or sophistication to make their own investment decisions. Acting with discretion, a broker can act quickly, using his professional judgment to invest in today's fast-paced markets, without waiting for consent to each and every trade.

In fact, most private wealth managers will not accept non-discretionary accounts. Their performance is judged on their the rates of return. When trading on behalf of hundreds of customers, it would take an enormous amount of time to obtain informed consent from each customer. This could hinder their ability to implement strategies in fast-moving markets, and possibly impair their ability to obtain the desired returns. Therefore, both the broker and the customer benefit if the broker is given discretion.

However, brokers with discretion understand that they have great responsibility to their customers. Within the financial industry, discretionary accounts are considered to impose a higher level of duty, and allow an investor to hold his advisor accountable for his performance.

**D. Customer Reports**

Regardless of whether an investor's account with a broker is non-discretionary or discretionary, that investor will receive the same standard documents detailing the activity conducted in his account. These documents include confirmations, which are sent after each purchase and sale to notify the customer as to what was bought or sold. The confirmation confirms that a security has been bought or sold, pursuant to an agreement between the broker-

dealer and his customer. For example, a trade confirmation might show that a customer purchased one share of IBM stock at \$48 per share on a particular day.

A brokerage statement is issued monthly or quarterly. It is a “snapshot” of the status of the brokerage account at the end of the period, and shows all transactions made during the statement period as well as the customer’s position at the end of the period—how many shares of stock or other securities are held for the customer at that time. In the example above, the statement would reflect the purchase of the IBM stock for \$48 on the trade day, and the current value of the IBM stock on the day as of which the statement was issued, and any other positions in the account at the end of the period.

Brokers also issue 1099 forms on an annual basis. 1099 forms reflect income generated by dividends and interest on investments and are used by the Internal Revenue Service (“IRS”) to calculate an investor’s tax liability. They also reflect the gross proceeds of all the year’s sale transactions.

#### **E. The Importance of the Confirmations and Statements**

The reports issued by broker-dealers are critically important because, in the modern securities markets, they represent the customer’s only evidence of ownership.

The modern world of securities trading is quite different from that of fifty years ago. Securities trading is based on individual purchases and sales at agreed prices. In past decades, this process took place at a physical location such as a stock exchange, and brokers would exchange tangible paper stock certificates



representing a stake in the issuing company. Investors would receive these paper certificates and rely on them as representing the securities they purchased.

Now, stock trades happen digitally, with a computer system matching up the bid and ask prices. Electronic trading has greatly increased the pace and volume of trading in today's market. This increased volume has made the issuance of paper documentation for each and every share an impossibility. Therefore, brokers now employ centralized custody of securities through entities such as the Depository Trust & Clearing Corporation ("DTCC"). The DTCC maintains a central depository of securities and allows for electronic transfer of shares between brokers, eliminating the trade of paper stock certificates.

Investors no longer receive paper certificates. Instead, investors now rely upon their confirmations and brokerage statements, which represent that investor's entitlement to ownership of the securities listed, in the amounts identified. Brokers issue confirmations and brokerage statements in electronic or hard copy form, or use some combination of the two. There is nothing unusual about a broker issuing trade confirmations and brokerage statements in paper form only.

These documents can be analogized to a statement issued with respect to a checking account at a bank. A bank customer receives a statement showing funds held in his name at the bank. The customer "owns" and is able to request those funds at any time. The customer cannot, however, go the bank and see "his" money. Similarly, a brokerage statement represents the broker's debt to the customer for the securities listed on the statement. The customer "owns" the

stock on the statement. The customer cannot, however, go to his broker and see “his” stock. Therefore, like the bank customer, the brokerage customer must instead rely upon his statement.

A brokerage customer is also entitled to rely on the accuracy of a broker’s statement primarily because the financial industry is one of the most heavily regulated industries in our economy. A host of governmental and non-governmental organizations play a role in this regulation, including the SEC, FINRA, and state regulatory agencies.

The SEC is a government commission created by Congress to protect investors. The SEC is responsible for administering all major federal legislation governing the securities industry. Brokers are required to file extensive information about their financial condition on a periodic basis with the SEC. Federal securities laws and regulations impose strict requirements on brokers when dealing with customer funds and securities held for customers. The SEC staff regularly performs inspections and examinations on all registered brokers to monitor their compliance with the applicable law and regulations. Through its Enforcement Division, the SEC investigates violations of the securities rules, including rules prohibiting fraud and false or misleading statements in materials distributed to investors. The SEC is empowered to bring lawsuits and enforce penalties against entities that violate the federal securities laws.

FINRA is the largest self-regulatory organization overseeing the financial industry. All companies who wish to sell securities in the U.S. are required to register with FINRA. FINRA has regulatory oversight over all securities firms

that do business with the public, and aims to protect investors by ensuring the integrity of the securities industry. FINRA licenses individuals and enforces rules governing their behavior, and is authorized by the SEC to discipline registered representatives and member firms that fail to comply with the laws or with FINRA's rules. Like the SEC, FINRA also performs examinations and inspections of member brokers to monitor their compliance with the law and regulations. FINRA also maintains the Central Registry Deposit ("CRD"), a database maintaining extensive records of the activities of every member firm and representative, including that member's disciplinary record.

FINRA-registered firms and employees are subject to extensive reporting requirements, including the requirements of reporting any customer complaints and submitting annual financial statements to the Authority.

In addition to the SEC and FINRA, brokers are subject to regulation in each of the states. In New York, where BLMIS operated, the Investor Protection Bureau protects investors from frauds perpetrated by brokers, dealers, salesmen and investment advisors by investigating any customer complaints.

Because there is no need to do so, due in part to the extensive regulatory schemes overseeing brokers, most brokerage clients do not review their statements to make sure they accurately reflect, for example, the then-current market price or trading volume for specific securities bought or sold by the broker. The customer is entitled to assume that the broker has done, or will do, whatever is necessary to perform the obligation he has undertaken to the customer. If the broker has taken the customer's money in return for an obligation to buy a

particular stock at a particular price, the customer need not do anything else to make sure that the broker actually buys the stock. In the securities industry, the issuance of a trade confirmation binds the broker to fulfill whatever was memorialized in the confirmation. The customer has no way of policing the broker's internal operation, and consequently is not required to be concerned about it.

Thus, most customers receive their statements, look at the bottom line stating the value of their portfolio to determine whether the value increased or decreased, and then file the statement away to give to their tax preparer. There is no need to do any more investigation and, in my experience, most customers do not.

**F. Opinions Regarding BLMIS Accounts**

Based on my many years of experience in the financial industry and exposure to thousands of trade confirmations and account statements, it is my opinion that the confirmations and statements issued by BLMIS were entirely standard, and that there was no substantive basis, from the point of view of an investor, to distinguish a BLMIS brokerage account from any other brokerage account.

The trade confirmations issued by BLMIS were typical of those issued by any brokerage house. The trade confirmations identified the trade date when the transaction was entered into, and the settlement date, reflecting the date when the transaction closed. The confirmations specifically identified the number of shares bought and sold of a certain stock, and included a CUSIP number, which stands

for “Committee on Uniform Securities Identification Procedures” and reflects a number assigned to U.S. and Canadian registered stocks and U.S. government and municipal bonds. The confirmations were standard, and looked similar to confirmations issued by any broker.

Like all monthly brokerage account statements, the BLMIS statements were dated, identified the name and address of the broker, included a specific account number corresponding to the named account holder, reflected the purchase and sale of specifically identified securities and stated the price at which they were bought and sold. The statements also provided a summary statement of the market value of all securities held in the account, and a year-to-date summary of cash transactions, income, and sales proceeds. These are the same types of standard details found on any monthly brokerage account statement. The BLMIS statements looked similar to statements issued by any broker.

The 1099s issued by BLMIS also correspond to standard 1099s issued by any bank or broker. Moreover, the fact that BLMIS issued these 1099s was another basis for a customer to feel comfortable that the information they received from BLMIS about their investments was accurate, because 1099s are submitted to and reviewed by the IRS. It would be counter-intuitive to think that that a fraudulent broker would submit false 1099s to the IRS for its review.

It is also my expert opinion that the following facts about BLMIS and Bernard Madoff himself would justify an investor in relying on both the trade confirmations and monthly account statements.

First, the trade confirmations and statements reflected that BLMIS was a member of FINRA, NSX, SIPC, NSCC and DTC. FINRA, discussed earlier, is the largest self-regulatory agency overseeing the financial industry. NSX is the “national stock exchange,” the nation’s first all-electronic stock exchange, and was formerly known as the Cincinnati Stock Exchange. SIPC, the Securities Investor Protection Corporation, is a non-profit corporation that protects customers of member broker-dealers by compensating them when a brokerage firm is closed due to bankruptcy or other financial difficulties and customer assets are compromised. NSCC is the National Securities Clearing Corporation, providing clearing, settlement, risk management and general counterparty services for broker-to-broker trades. DTC, the Depository Trust Company, also provides settlement services for clearing securities trades.

BLMIS’ membership in each of these entities would be expected of a broker-dealer that cleared its own trades. Membership in these organizations conveys that BLMIS was, in fact, a broker-dealer, and would entitle a customer to expect that his trade confirmations and account statements were accurate.

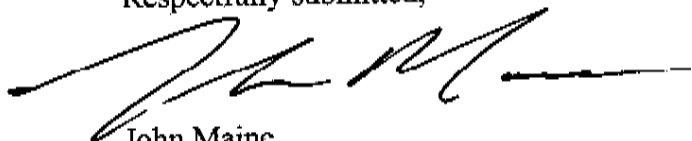
Mr. Madoff’s stature in the financial community was another factor on which investors might legitimately rely when considering whether their trade confirmations and account statements are accurate. Mr. Madoff was a former chairman of the NASDAQ stock market and vice-chairman of the board of governors of the National Association of Securities Dealers. He had many highly sophisticated investors. His prominent place in the financial industry would

further justify a customer's expectation that his confirmations and statements accurately represented his investments.

Moreover, by the time the Madoff fraud was revealed, BLMIS had been in operation for many decades. I have frequently been involved in cases in which a broker was engaged in a Ponzi scheme, and I have never seen one last more than a few years. Obviously, in this case, BLMIS appeared to be performing its obligations to customers for a very long time—apparently buying securities after taking customer funds, recording purchases and sales, and returning funds upon demand. The longevity and apparent normality of BLMIS' business model provides yet another reason for an investor to trust that BLMIS was a legitimate enterprise and that its confirmations and statements were accurate and reliable.

This report sets forth only a summary of the testimony I expect to provide at trial. I reserve the right to supplement or amend this report should additional information become available.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'John Maine', with a long horizontal flourish extending to the right.

John Maine

November 22, 2011



# EXHIBIT A

**JOHN MAINE**  
**EXPERT WITNESS & CONSULTANT – SECURITIES**

**EDUCATION**

B.A. Magna Cum Laude  
Dartmouth College

**INDUSTRY EXPERIENCE**

- Retail Stockbroker
- Institutional Salesperson
- National Institutional Sales Manager – responsible for recruiting and managing a nationwide sales force
- Resident Sales Manager of a 100 person branch office
- Regional Director for a 1,000 person region with revenues in excess of 200 million
- Member of the Board of Directors of Smith Barney and Executive Vice-President of the Firm

**EXPERT WITNESS CREDENTIALS**

- Retained approximately 1700 times, given testimony on approximately 700 occasions in over 40 states.
- Testified in State and Federal courts in various jurisdictions, in arbitration proceedings, in mediations and in SRO disciplinary hearings.

**TOPICS**

Alternative Investments

Among the topics qualified to present expert testimony:

Annuities

Auction Rate Securities

Back office procedures

Broker forgivable notes

Churning and excessive trading

Commissions and mark-ups

Damages

Employment issues

Hedge Funds

Hedging strategies for concentrated positions

High Yield Bonds and other complex debt instruments

Inter-firm hiring disputes and raiding

Limited Partnerships

Managed Money

Municipal Bonds

Mutual Funds

Options trading

Private Equity/Private Placements

Registered Investment Advisor issues

Regulatory disciplinary matters

REITs & TICs

Retirement strategies

Rule #144 and other control stock issues

Suitability

Supervision and Compliance

Trading away

U-4 and U-5 filings

*This is meant to be a representative list but is not all inclusive*

**PAST LICENSES HELD**

NYSE-Registered Representative

NYSE-Branch Office Manager

ASE, CBT, NASD, NYSE-Registered Options Principal

NASD-General Securities Principal

National Futures Association-Associated Person

References available on request

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# EXHIBIT B

## **JOHN MAINE**

### **CASES AND ARBITRATIONS IN WHICH I HAVE TESTIFIED AS AN EXPERT WITHIN THE PAST FOUR YEARS**

#### **Court Cases**

Vargas v. Kearney  
State Court, Placer County, California 2009

Eastburn v. Cole  
State Court, Marin County, California 2009

Roberts v. Bisno  
State Court, Alameda County, California 2009

Stephens v. Kellett Capital Management  
State Court, Marin County, California 2010

State of Colorado v. E\*Trade Securities  
State Court, Denver, Colorado 2011

#### **Arbitrations**

Charter v. Hakim  
Dodell v. Tannenbaum  
Pelosi v. Barretto  
Crowder v. Wells  
Swerling v. Stringer  
Torina v. Piro  
Wagenhals v. Dwyer  
Abel v. Lou  
Pinazzi v. Norman  
Den-Mat v. Zihailo  
Simon v. Miller  
Dobson v. Clayton  
King v. A.G. Edwards  
Ludvigson v. Schwarz  
Holzberg v. Cameron  
Boys v. Buckley  
Crusing v. Aldis  
Allalouf v. Torvala  
Garrett v. Escudero  
Moffatt v. Stanford Group  
Waldrop v. UBS PaineWebber  
Batemen v. Forster  
Schultz v. Smith Barney  
Chodorow v. Safavi

Stratton v. Richmond  
Benci v. Rudningen  
Kellman v. Moskowitz  
Edward v. UBS  
Hayden v. Robertson Stephens  
Orourke v. Baylin  
Hoover v. Foreman  
Weiss v. Berk  
Hale v. Horwitz  
Brady v. Ygenlasis  
Riciputo v. UBS  
Wong v. Smith Barney  
Stoyanoff v. Leary  
Postiglione v. CSFB  
Turmon v. Smith  
Arner v. UBS  
Clark v. Sussman  
Hong v. Mullen  
Chamberlain v. McMahon  
Sage v. Bear Stearns  
Weinreb v. Winter  
Fitzwilson v. Andrew Chase  
Gilliland v. McGeorge  
Stroehmann v. Peloquin  
Adler v. Selig  
Richards v. Forster  
Guinn v. Meidell  
Colucci v. Burns  
Miller Johnson v. Northland  
Sessaman v. Easterday  
Kramer v. Poutre  
Eansor v. Calderone  
Benezra v. Chamberlain  
Musser v. Vick  
Ventura v. Baum  
Silva v. Morgan Stanley  
Muir v. PSI  
Scher v. BofA  
McCubbins v. Flanagan  
Maltz v. Virnoche  
RLR Management v. Garrity  
Herta v. Hartwyck  
Mayne v. Burke  
Hunt v. Jackson  
Paul v. Wilmot  
Grant v. Wilhite  
Elzarka v. Kromholt  
Kennedy v. Leach  
McElhatton v. Kuhne

Van Hoose v. Markow  
Perloff v. Hallman  
Micha v. Bank of California  
Zuk v. Margolla  
DeHaven v. Jackson  
Sunde v. Clark  
Cohen v. Haas  
Tsui v. Bailey  
Dickerson v. Bar Lev  
Bostian v. Gallo  
Spencer v. Santoro  
Hokk v. AG Edwards  
Winstead v. UBS  
Gale v. Stocklan  
Jone v. Lee  
Palmer v. Coulter  
Ramsey v. Bohland  
Van Muyden v. Springer  
Goldsberry v. Dunas  
Berkowitz v. Maegher  
Parziale v. Ohanian  
Schwab v. Raymond James  
Madrid v. Lancaster  
Van Order v. Bagocus  
Welkom v. Cole  
Money Concepts v. ProEquities  
Cathcart v. Zinolli  
Arenson v. Clark  
Weinreb v. Garabedian  
Blitz v. Kabarín  
Eastburn v. Cole  
Beesemeyer v. A.G. Edwards  
Melton v. Deutsche Bank  
Beesemeyer v. Barniyak  
Quinault v. Hoheimer  
Reiter v. Weaver  
Bloom v. Ross  
Thompson v. Urbolic  
Brown v. JP Morgan  
Sardis v. Frankel  
Riverside v. Frankel  
Waks v. Goodenough  
Roberts v. Jerger  
Nielsen v. Schwab  
NYSE v. Poock  
Smith v. Citigroup  
Grymkowski v. Grossblatt  
Bernik v. Shemano  
Smith v. Schwab

Misha v. Lowi  
Brezden v. SunAmerica  
Paulson v. Bear Stearns  
Nopuenta v. Choy  
DeLaura v. Peter  
Postigo v. Schwab  
Glenn v. UBS  
Strand v. Morgan Stanley  
Ross v. Schwab  
Archer v. Schwab  
Greenberg v. Cole  
Thompson v. Wesson  
A.G. Edwards v. Raymond James  
Brown v. Schwab  
Kelly v. Schwab  
Wilfong v. Morgan Keegan  
Lerman v. Daifotis  
Edwards v. Shah  
Rivkin v. Schwab  
Applbaum v. Stone & Youngberg  
Robeson v. Schwab  
Leone v. WMFS  
Goldstein v. Piper Jaffray  
Sherman v. Citi  
Schweiterman v. Schwab  
Neves v. WaMU  
Biomemedics v. DB  
Mauny v. Schwab  
Pelley v. Schwab  
Garcia v. Gilford  
Erickson v. Schwab  
Lovins v. UBS  
Hayes v. Schwab  
Wachovia v. Stifel  
Abramson v. Citi  
Virginia Lake v. RBC  
Brown v. Finestone  
Intervac v. Citigroup  
McCray v. Wachovia  
Phelan v. KCM  
Hougie v. Schwab  
Oathout v. Schwab  
Matracaria v. Jefferies  
Hill v. Schwab  
Cooper v. Morgan Keegan  
Tripp v. UBS  
Aucoin v. UBS  
Wells Fargo v. Stifel  
Chapman v. Citigroup

Lichtenberg v. JPM  
Gordon v. PFS  
Empire v. Stockcross  
TGS v. Merrill  
Cogan v. U.S. Bancorp  
Vollstedt v. Schwab  
Manley v. Deutsche Bank  
Gritz v. Royal Alliance  
Wells Fargo v. Stifel Nicholas  
Joslen v. Akiyama  
Neel v. OPCO  
Citigroup v. Perry  
Smolensky v. Neuberger Berman  
Stirling v. Wells Fargo  
Madhok v. Schwab