

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

09 CIV 3708

MERIDIAN HORIZON FUND, LP, MERIDIAN  
HORIZON FUND II, LP, MERIDIAN DIVERSIFIED  
FUND, LP, MERIDIAN DIVERSIFIED FUND, LTD.,  
MERIDIAN DIVERSIFIED ERISA FUND, LTD.,  
MERIDIAN DIVERSIFIED COMPASS FUND, LTD.,  
and MERIDIAN ABSOLUTE RETURN ERISA FUND,  
LTD.,

No. \_\_\_\_\_

**COMPLAINT**

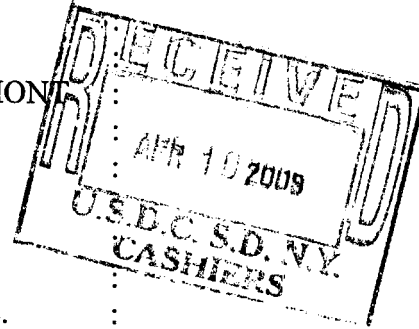
**Jury Trial Demanded**

Plaintiffs,

- against -

TREMONT GROUP HOLDINGS, INC., TREMONT  
PARTNERS, INC., TREMONT (BERMUDA)  
LIMITED, OPPENHEIMER ACQUISITION  
CORPORATION, KPMG LLP, and KPMG  
(CAYMAN),

Defendants.



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Plaintiffs Meridian Horizon Fund, LP, Meridian Horizon Fund II, LP,  
Meridian Diversified Fund, LP, Meridian Diversified Fund, Ltd., Meridian Diversified  
ERISA Fund, Ltd., Meridian Diversified Compass Fund, Ltd., and Meridian Absolute  
Return ERISA Fund, Ltd., by their undersigned attorneys, for their complaint against  
defendants Tremont Group Holdings, Inc., Tremont Partners, Inc., Tremont (Bermuda)  
Limited, Oppenheimer Acquisition Corporation, KPMG LLP, and KPMG (Cayman),  
allege the following:

**NATURE OF THE ACTION**

1. Plaintiffs invested and lost more than \$116 million in the Rye  
Select Broad Market XL Fund, LP (the "Onshore XL Fund") and the Rye Select Broad

Market XL Portfolio Limited (the “Offshore XL Fund,” and together with the Onshore XL Fund, the “XL Funds”). These funds were sold and managed by defendants Tremont Group Holdings, Inc. (“Tremont Group Holdings”), Tremont Partners, Inc. (“Tremont Partners”), and Tremont (Bermuda) Limited (“Tremont Bermuda”) (collectively, the “Tremont Defendants”), and their returns were derived from leveraged investments in other funds that were also sold and managed by the Tremont Defendants (the “Reference Entities”). Oppenheimer Acquisition Corporation (“Oppenheimer Acquisition”) is the parent of Tremont Group Holdings, and provides legal, compliance, and other support to the Tremont Defendants.

2. The Reference Entities were single-manager investment vehicles. The Tremont Defendants served as investment manager to these funds, but delegated all investment decisions to Bernard L. Madoff (“Madoff”) and/or Bernard L. Madoff Investment Securities, LLC (“BMIS”). Madoff, through BMIS, purportedly executed all trades on behalf of the Reference Entities, and also was the custodian for their securities.

3. Plaintiffs invested in the XL Funds because the Tremont Defendants – in, among other things, offering materials, responses to due diligence questionnaires (“DDQs”), and direct conversations – gave their assurance that they were intimately familiar with Madoff’s and BMIS’s operations, and that they closely monitored Madoff’s and BMIS’s transactions, internal controls, and operational risk. Moreover, the Tremont Defendants – through, among other things, monthly performance reports and yearly financial statements, and direct conversations – also represented that the assets Madoff and BMIS claimed to hold for the XL Funds existed and were

appreciating, and that the trades Madoff and BMIS claimed to have made for these funds actually occurred.

4. The Tremont Defendants thus purposefully positioned themselves as the gatekeepers of all Madoff-related information, and, in exchange for the substantial “management” fees they charged plaintiffs, promised that they had sufficiently vetted and monitored Madoff and BMIS. Plaintiffs relied on these representations in making and retaining their investments in the XL Funds, in particular because the Tremont Defendants limited, and later cut off entirely, plaintiffs’ direct access to Madoff and BMIS.

5. In fact, it now appears that Madoff, who pled guilty on March 12, 2009 to all eleven counts in the criminal information prosecutors filed against him, misappropriated the funds he received and purportedly invested for the Reference Entities’ (and, thus, for the XL Funds’) benefit. In December 2008, it was revealed that Madoff had for years been running a massive Ponzi scheme, and that the Reference Entities he purportedly managed held little or no assets. As part of his plea allocution, Madoff admitted to perpetrating this fraud since at least the early 1990s (prosecutors charge the fraud began at least as early as the 1980s), and admitted that he never invested his investment advisory clients’ assets in securities. Instead, he simply deposited client funds in an account at Chase Manhattan Bank, and paid redemptions from that account.

6. If the Tremont Defendants actually had conducted the due diligence and monitoring they claimed they had, they would have been aware of these facts. The Tremont Defendants either failed to perform the due diligence or monitoring they claimed to have performed, or they uncovered evidence of Madoff’s Ponzi scheme,

and knowingly or recklessly misrepresented to plaintiffs' representatives that the XL Funds' assets existed and were appreciating – all in order to continue collecting substantial fees from plaintiffs.

7. In addition to the representations of the Tremont Defendants, plaintiffs also relied upon unqualified audit opinions sent to them by KPMG LLP and KPMG (Cayman) (together, "KPMG"). Because the Reference Entities, and thus the XL Funds, relied on BMIS for virtually all portfolio management, trade execution, and custodial services, generally accepted auditing standards ("GAAS") required KPMG to obtain sufficient appropriate audit evidence to support the existence of the assets Madoff and BMIS claimed to hold and invest for the benefit of the Reference Entities, and the occurrence of the purported trades that generated the income reported in these funds' financial statements.

8. Given the concentration of functions at BMIS, and the resulting need for heightened professional skepticism, KPMG should have determined whether a reputable auditor conducted adequate procedures to satisfy itself as to the effectiveness of BMIS's internal controls, or as to the existence of assets and the occurrence of trades.

9. BMIS's auditor, Friehling & Horowitz, C.P.A., P.C. ("F&H"), failed to perform such procedures, and its reputation and the inadequacy of its work made its reports unreliable. F&H was a three person firm, with only one active accountant (David Friehling), who worked out of a small storefront office, had not been "peer-reviewed," and who reported to the American Institute of Certified Public Accountants ("AICPA") that he did not conduct audits. Moreover, as alleged by the SEC in its complaint against Friehling and F&H, and as KPMG would have discovered if it had

asked to review F&H's work papers, F&H's audits of BMIS were a sham, and not supported by any meaningful documentation. Thus, F&H's "audit" work on BMIS was unreliable.

10. Without assurance from a reputable auditor as to the existence of the assets and occurrence of trades, KPMG should have obtained additional audit evidence some other way – either by having BMIS engage a reputable auditor, or by performing audit procedures itself. No evidence has been reported to suggest that KPMG obtained such appropriate audit evidence. Moreover, because Madoff held none of the assets he claimed to hold for his investment advisory clients, and made none of the trades, KPMG would not have been able to obtain corroboration from sources independent of BMIS that the assets existed or trades occurred.

11. Under these circumstances, KPMG knew or was reckless in not knowing that issuing unqualified audit opinions on the financial statements of the Reference Entities, the XL Funds, and other Madoff-managed funds sold by the Tremont Defendants would violate GAAS. Nevertheless, KPMG sent to plaintiffs unqualified audit opinions for these funds. These audit opinions were false and misleading, and their issuance to plaintiffs by KPMG was reckless. KPMG knew that investors in the XL Funds would rely on its audit opinions on each of these funds – all of which purportedly derived returns from the same investment strategy the Tremont Defendants claimed Madoff and BMIS employed. Had KPMG issued anything other than an unqualified audit opinion with respect to any of these related funds, plaintiffs would not have invested in the XL Funds, and immediately would have redeemed any existing investments.

12. As a result of the wrongful conduct described herein, plaintiffs lost more than \$116 million, for which the defendants are liable.

## **PARTIES**

### **The Plaintiffs**

13. Plaintiffs Meridian Horizon Fund, LP, Meridian Horizon Fund II, LP, and Meridian Diversified Fund, LP (collectively, the “Onshore Plaintiffs”) are limited partnerships organized under the laws of the State of Delaware, with partners in, among other places, New York.

14. Plaintiffs Meridian Diversified Fund, Ltd., Meridian Diversified ERISA Fund, Ltd., Meridian Diversified Compass Fund, Ltd., and Meridian Absolute Return ERISA Fund, Ltd. (collectively, the “Offshore Plaintiffs”) are exempted companies incorporated with limited liability under the laws of the Cayman Islands.

15. Plaintiffs were managed from and within the State of New York.

### **The Madoff and BMIS Non-Parties**

16. Non-Party Madoff is the founder and owner of BMIS.

17. Non-Party BMIS is a securities broker-dealer and investment advisor registered with the SEC, with its principal office in New York, New York. BMIS purportedly engaged in investment advisory services, market making, and proprietary trading. According to the Tremont Defendants, BMIS served as custodian of the Reference Entities’ purported assets.

18. Non-party F&H is an accounting firm that operated out of a 238-square foot storefront office in Rockland County, New York. F&H had only three employees, one of whom was 80 years old and lived in Florida. Friebling, F&H’s only

active accountant, reported in writing to the AICPA that he does not conduct audits. F&H was engaged by Madoff and BMIS to perform professional services, including auditing BMIS's financial statements for 2002 through 2007. On March 18, 2009, Friehling was charged in a six-count criminal complaint that accused him of securities fraud, aiding and abetting investment advisory fraud, and making false filings to the SEC in connection with his false certification that he had audited BMIS's financial statements in accordance with GAAS. Friehling and F&H also have been named as defendants in a related civil lawsuit filed by the New York regional office of the SEC on the same day, alleging that F&H's audits of BMIS were a sham.

#### **The Rye Funds Non-Parties**

19. Non-Party Onshore XL Fund is a limited partnership organized under the laws of the State of Delaware. Its stated investment objective is to provide investors with long-term capital growth and a return based on a three times levered exposure to the economic performance of the Rye Select Broad Market Fund, LP (the "Onshore Reference Entity"), whose assets purportedly were managed by and custodied with Madoff and BMIS. Leverage on the Onshore Reference Entity's returns was to be achieved by the Onshore XL Fund entering into swap transactions with one or more designated counterparties. In addition to its investment with a swap counterparty, the Onshore XL Fund also had direct investments in the Onshore Reference Entity.

20. Non-Party Offshore XL Fund is a Cayman Islands exempted company. Its stated investment objective is to provide investors with long-term capital growth and a return linked to a three times levered exposure to the economic performance of Rye Select Broad Market Portfolio Limited (the "Offshore Reference Entity"), whose

assets purportedly were managed by and custodied with Madoff and BMIS. Leverage on the Offshore Reference Entity's returns was to be achieved by the Offshore XL Fund entering into swap transactions with one or more designated counterparties.

**The Defendants**

***The Tremont Defendants***

21. Defendant Tremont Group Holdings is a corporation organized under the laws of the State of Delaware, with its principal place of business at 555 Theodore Fremd Avenue, Rye, New York 10580. Tremont Group Holdings is a wholly owned subsidiary of defendant Oppenheimer Acquisition.

22. Defendant Tremont Partners is a corporation organized under the laws of the State of Connecticut, with its principal place of business at 555 Theodore Fremd Avenue, Rye, New York 10580. Tremont Partners is the chief operating subsidiary of defendant Tremont Group Holdings. Tremont Partners serves as (i) general partner of the Onshore Reference Entity and the Onshore XL Fund; (ii) sub-advisor to the Offshore Reference Entity; and (iii) investment manager of the Offshore XL Fund.

23. Defendant Tremont Bermuda is a company organized under the laws of Bermuda. Tremont Bermuda is the investment manager of the Offshore Reference Entity.

***Oppenheimer Acquisition***

24. Defendant Oppenheimer Acquisition is a corporation organized under the laws of the State of Delaware, with its principal place of business in New York, New York. Oppenheimer Acquisition acquired defendant Tremont Group Holdings in

2001. Tremont's annual revenue of approximately \$100 million comprises approximately 7% of Oppenheimer Acquisition's annual revenue.

*The Auditor Defendants*

25. Defendant KPMG LLP is a limited liability partnership organized under the laws of the State of Delaware, with its principal place of business in New York, New York. KPMG LLP sent to partners of the Onshore XL Fund (including the Onshore Plaintiffs) unqualified audit opinions on that fund's 2006 and 2007 financial statements. KPMG LLP also sent to partners of the American Masters Broad Market Prime Fund, LP (the "Prime Fund") (including the Onshore Plaintiffs) an unqualified audit report on that fund's 2005 financial statements. The returns of the Prime Fund, the Onshore XL Fund, and the Onshore Reference Entity, as reported in these funds' financial statements audited by KPMG LLP, were purportedly derived from the investment strategy that the Tremont Defendants claimed Madoff and BMIS employed.

26. Defendant KPMG Cayman is a Cayman Islands partnership. KPMG Cayman sent to shareholders of the Offshore XL Fund (including the Offshore Plaintiffs) unqualified audit opinions on that fund's 2006 and 2007 financial statements. KPMG Cayman also sent to the Offshore Plaintiffs unqualified audit opinions on the Offshore Reference Entity's 2006 and 2007 financial statements. The returns of the Offshore XL Fund and the Offshore Reference Entity, as reported in these funds' financial statements audited by KPMG Cayman, were purportedly derived from the investment strategy that the Tremont Defendants claimed Madoff and BMIS employed.

**PLAINTIFFS' LOSSES**

27. Plaintiff Meridian Horizon Fund, LP invested \$25 million in the Onshore XL Fund on October 1, 2006; \$10 million on March 1, 2007; and \$5 million on May 1, 2007.

28. Plaintiff Meridian Horizon Fund II, LP invested \$6.2 million in the Onshore XL Fund on August 1, 2007; and \$55,962 on May 1, 2008.

29. Plaintiff Meridian Diversified Fund, LP invested \$9.8 million in the Onshore XL Fund on August 1, 2007; and \$6 million on March 1, 2008.

30. Plaintiff Meridian Diversified Fund, Ltd. invested \$17 million in the Offshore XL Fund on October 1, 2006; \$10 million on January 1, 2007; \$20 million on March 1, 2007; and \$8 million on September 1, 2007.

31. Plaintiff Meridian Diversified ERISA Fund, Ltd. invested \$7 million in the Offshore XL Fund on October 1, 2006; \$10 million on November 1, 2006; \$5 million on January 1, 2008; and \$10 million on August 1, 2008.

32. Plaintiff Meridian Diversified Compass Fund, Ltd. invested \$6.55 million in the Offshore XL Fund on August 1, 2007; \$160,346 on May 1, 2008; and \$3 million on July 1, 2008.

33. Plaintiff Meridian Absolute Return ERISA Fund, Ltd. invested \$1.6 million in the Offshore XL Fund on July 1, 2007; and \$400,000 on January 1, 2008.

34. On January 14, 2009, Rye Investment Management (“RIM”), a division of Tremont Group Holdings that managed, sold, and administered the Tremont Defendants’ platform of single-manager funds, told partners in the Onshore XL Fund (on behalf of Tremont Partners) that it had concluded that this and related funds had “lost substantially all of their value,” and that the net asset values for these funds as of

November 30, 2008 were being calculated to “reflect a total loss of assets which were held at Madoff Securities.”

35. Plaintiffs have written off 100% of their investments in the XL Funds. The following table shows the amount of capital invested in the XL Funds, net of redemptions received from the XL Funds, that each plaintiff lost:

<b>XL FUND</b>	<b>PLAINTIFF</b>	<b>INVESTED CAPITAL LOST</b>
Rye Select Broad Market XL Fund, LP	Meridian Horizon Fund, LP	\$25,000,000
	Meridian Horizon Fund II, LP	\$4,255,962
	Meridian Diversified Fund, LP	\$13,800,000
Rye Select Broad Market XL Portfolio Limited	Meridian Diversified Fund, Ltd.	\$30,000,000
	Meridian Diversified ERISA Fund, Ltd.	\$32,000,000
	Meridian Diversified Compass Fund, Ltd.	\$9,710,346
	Meridian Absolute Return ERISA Fund, Ltd.	\$2,000,000
<b>TOTAL</b>		<b>\$116,766,308</b>

## **JURISDICTION AND VENUE**

### **Subject Matter Jurisdiction**

36. This Court has original and/or supplemental subject matter jurisdiction over all claims in this action pursuant to 15 U.S.C. § 78aa and 28 U.S.C. §§ 1331 and 1367. Some of the claims asserted herein arise under the federal securities laws, and the state-law claims are so related to the federal claims as to form part of the same case or controversy.

### **Personal Jurisdiction**

37. Each of the defendants has subjected itself to the personal jurisdiction of this Court by way of their regular transaction of business within the State of New York; dissemination to plaintiffs' representatives of offering materials, financial disclosures, audit reports, and/or other written materials from and/or in the State of New York; and communications with plaintiffs to, from, and/or in the State of New York. In addition, the Tremont Defendants, Oppenheimer Acquisition, and KPMG LLP have their principal places of business in New York.

**Venue**

38. Venue is proper in this District pursuant to 15 U.S.C. § 78aa and 28 U.S.C. § 1391, because a substantial part of the events and omissions giving rise to the claims occurred here.

**FACTUAL ALLEGATIONS**

**The Tremont Defendants**

39. Madoff founded and ran BMIS, an SEC-registered broker-dealer. Madoff and BMIS also purported to provide investment advisory services. BMIS acted as prime broker and custodian for the assets Madoff claimed to manage for his investment advisory clients. Madoff limited the number of investors he would deal with directly, but accepted investments from funds sold by the Tremont Defendants. The Tremont Defendants marketed their single-manager funds to investors as a gateway to Madoff's investment advisory services.

40. The Tremont Defendants consistently represented – through, among other things, offering materials, financial disclosures, DDQs, and direct conversations – that they had conducted sufficient due diligence on Madoff and BMIS to

verify, among other things, the existence of the assets Madoff and BMIS claimed to hold and manage for the Tremont Defendants' investors, and the occurrence of the trades that Madoff and BMIS claimed to execute on those investors' behalf.

41. The Tremont Defendants' relationship with plaintiffs commenced in 1994, when plaintiff Meridian Horizon Fund, LP first invested in the Offshore Reference Entity (then operating under a different name).<sup>1</sup> This fund's assets (other than cash balances) were purportedly managed by Madoff and custodied with BMIS. After this initial investment, but before plaintiffs began investing in the XL Funds in October 2006, each plaintiff (except for the Meridian Absolute Return ERISA Fund, Ltd.) invested in other Tremont funds, making investments in the Prime Fund in July 1997, January 1999, and July 2001;<sup>2</sup> the Tremont Broad Market Fund, LDC in July 2001; and the Offshore Reference Entity in January 2002 and July 2004.<sup>3</sup> Plaintiffs made these investments relying on the years of history they had with the Tremont Defendants, including the numerous representations the Tremont Defendants made to plaintiffs' representatives about the due diligence the Tremont Defendants purportedly conducted on Madoff and BMIS.

42. The Tremont Defendants represented in, among other things, offering materials, DDQs, and direct conversations that they had conducted extensive due

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<sup>1</sup> This fund was called the Broad Market Fund, LP in 1994. The fund's name was changed on January 1, 1999, to the American Masters Broad Market Fund, LP, and again on July 7, 2006, to the Rye Select Broad Market Fund, LP.

<sup>2</sup> This fund was called the Broad Market Prime Fund, LP in 1997. The fund's name was changed on January 1, 1999, to the American Masters Broad Market Prime Fund, LP, and again on July 7, 2006, to the Rye Select Broad Market Prime Fund, LP.

<sup>3</sup> This fund was called the American Masters Broad Market Prime Fund II, Ltd., until it changed its name on July 31, 2006 to the Rye Select Broad Market Portfolio, Ltd.

diligence on Madoff and BMIS, and were monitoring Madoff and BMIS. The Tremont Defendants also claimed to have a comprehensive understanding of BMIS's operations. This understanding was particularly important to plaintiffs because the Tremont Defendants controlled and limited plaintiffs' access to Madoff and BMIS, and positioned and described themselves as the organization that would work with Madoff and BMIS to provide responses to all information requests made by plaintiffs.

43. For example, since late 2005, after the Tremont Defendants had previously granted plaintiffs' representatives access to Madoff on a few occasions for limited meetings, they declined to facilitate any additional contact with Madoff or BMIS, and emphasized that their role was, in part, to minimize the need for plaintiffs to have direct contact with Madoff or BMIS. Doing so, the Tremont Defendants explained, avoided disturbing Madoff.

44. The Tremont Defendants made these representations prior to and after each initial and subsequent investment in the XL Funds.

***The February – March 2006 Conference Calls***

45. On or about February 10, 2006, Darren Johnston ("Johnston") – a Director of the Offshore XL Fund, and Manager of RIM responsible for managing the Tremont Defendants' single-manager business globally, and for overseeing product development, portfolio management, marketing, and investor-service functions of RIM – participated in a conference call with plaintiffs' representatives. Johnston reported on the purported appreciation of the funds marketed and sold by the Tremont Defendants and managed by Madoff and BMIS, and conveyed representations made by Madoff and BMIS as to past and expected future returns. Johnston also described both Madoff's

commitment to continue managing the portfolio for another dozen years, and aspects of Madoff's and BMIS's operations.

46. On or about March 13, 2006, Johnston participated in another conference call with plaintiffs' representatives. Johnston again reported to plaintiffs' representatives on the purported appreciation of the funds marketed and sold by the Tremont Defendants and managed by Madoff and BMIS. Johnston stated that he and his colleagues planned to meet with Madoff in late March 2006. When plaintiffs' representatives asked if they could join the meeting, Johnston responded that he would get back to them on the feasibility of doing so. Subsequently it was communicated to plaintiffs' representatives that the Tremont Defendants were unable to coordinate a meeting with Madoff, despite the specific request of the plaintiffs' representatives to do so, and that the Tremont Defendants would handle any questions plaintiffs' representatives had for Madoff.

*The 2005 DDQ*

47. On or about March 14, 2006, plaintiffs received from Johnston the responses of Tremont Group Holdings (then called Tremont Capital Management, Inc.) to a standardized DDQ. In this DDQ, Tremont Group Holdings identified Tremont Partners as its main domestic subsidiary. In light of this representation, the representations made in the 2005 Tremont Group Holdings DDQ are attributable to both Tremont Group Holdings and Tremont Partners.

48. Tremont Group Holdings stated in this DDQ that although Madoff and BMIS had "full discretion over the assets within the brokerage account," the Tremont Defendants "control[led] the assets into and out of the brokerage account." Moreover,

Tremont Group Holdings claimed to “review the accuracy, completeness and timeliness of account statements” it received from Madoff and BMIS.

49. Tremont Group Holdings described how it came to have a detailed understanding of the managers with whom the Tremont Defendants invested (like BMIS): a “Manager Research Strategy Specialist” conducts a “rigorous interview” with each external portfolio manager that “focuses on the manager’s background, organization, strategy, plans for growth, leverage, decision-making process, portfolio construction, investment process and on their risk management procedures and policies.”

50. Tremont Group Holdings also claimed to investigate external fund managers’ back-office systems, explaining that “analysts perform an operational risk evaluation as part of the initial due diligence phase on all new managers that may be approved for possible investment.” This evaluation, Tremont Group Holdings explained, “involves at least one analyst visiting with the fund’s back office personnel, including the CFO, head trader, COO and other personnel,” and that it “follows up with the fund’s administrator, prime broker and auditor to make sure that the processes described at the manager level are actually carried out by the third party service providers.” If, as a result of this evaluation, Tremont Group Holdings’ “Manager Research Strategy Specialist is not comfortable with the business risks that they review ... they can eliminate a manager from further consideration.”

51. In addition, Tremont Group Holdings’ “finance area, under the supervision of its CFO and fund administration team, review the financials of all funds under consideration for investment.” This type of evaluation purportedly enabled Tremont Group Holdings, which claimed to be “sensitive to potential conflicts of

interest,” to “determine whether the organizational structure ensures the effective operation of the firm’s investment decision-making process.”

52. Tremont Group Holdings also noted that understanding the ownership of an external investment firm (like BMIS) “is important in determining how control of the firm is distributed among internal or external parties and what types of controls these parties may exercise.” Moreover, “[i]n reviewing the decision-making process” at external investment firms (like BMIS), Tremont Group Holdings claimed to “determine that lines of authority are well defined, that responsible parties are clearly identified, that implementation is carried out efficiently and that accountability is maintained.”

53. Once Tremont Group Holdings selected an investment manager, it claimed to have “ongoing contact with a manager through e-mails, letters, phone calls and face-to-face meetings” as part of what it called a “rigorous and consistent process” designed to “ensur[e] that [Tremont] [is] constantly aware of strategy or business issues confronting a manager.” This process purportedly included contacting the manager on a monthly basis to obtain updates, and coordinating quarterly conference calls with managers.

***The 2006 SEC Form ADV***

54. On or about March 14, 2006, Plaintiffs received from Johnston the Tremont Partners Form ADV, dated January 1, 2006. This form stated that “[t]he implementation and carrying out of Tremont’s investment management and advisory services through its team of portfolio managers and other investment professionals are conducted and overseen through Tremont’s Investment Committee, which is advised,

from time to time, by Tremont's Investment Advisory Board." In light of the substantial participation in Tremont Partners' business of Tremont Group Holdings (Tremont Partners' parent company), the representations made in this Form ADV are attributable to both Tremont Group Holdings and Tremont Partners.

55. Tremont Partners represented in this Form ADV that it "is engaged on a daily basis with custodians and/or trustees to monitor cash flow and fund compliance"; that "[f]und accounts are monitored in terms of securities holdings, asset mix and adherence to investment guidelines"; and that Tremont Partners "uses its own proprietary software programs to monitor the performance of investment managers."

*The XL Funds' Offering Materials*

56. In June 2006, the Tremont Defendants renamed some of their funds the "Rye Select Funds," and created the XL Funds, all organized under RIM, a new division at Tremont Group Holdings. On September 19, 2006, Johnston met with plaintiffs' representatives to discuss the XL Funds, and to review the XL Funds' offering materials and swap documents.

57. The Tremont Defendants promoted the XL Funds as designed to achieve a leveraged return on the Reference Entities by entry into swap transactions with independent counterparties. The XL Funds' offering materials explained that the return on investment would be derivative of the return on the Onshore Reference Entity and Offshore Reference Entity.

58. The Onshore XL Fund limited partnership agreement, dated September 1, 2006, stated that Tremont Partners "exercises ultimate authority over the Partnership." The Onshore XL Fund private placement memorandum ("PPM"), dated

September 1, 2006, identified Tremont Partners as the general partner, and stated that Tremont Partners was “responsible for managing the day-to-day operations and investment management of the Partnership.” Both the offering materials and partnership agreement acknowledged Tremont Partners’ fiduciary responsibilities and potential liability to that fund’s limited partners, who include the Onshore Plaintiffs. Similarly, the Offshore XL Fund Information Memorandum, dated September 1, 2006, identified Tremont Partners as the investment manager.

59. The prospectus for the Offshore Reference Entity, dated October 1, 2006, identified Tremont Bermuda as the investment manager and Tremont Partners as the sub-advisor. Tremont Partners also served as administrator for this fund.

60. The PPM and Information Memorandum for the XL Funds identified their investment objective as “to seek to (i) achieve long term capital appreciation and (ii) consistently generate positive returns irrespective of stock market volatility or direction, while focusing on preservation of capital.” These funds purportedly sought to accomplish this investment objective by leveraging the return on the Reference Entities, which “invest[ed] the majority of the assets with one Manager who employs a ‘split strike conversion’ strategy” – *i.e.*, Madoff and BMIS.

61. In light of the substantial participation of Tremont Group Holdings (of which RIM is a division) and Tremont Partners in the Onshore XL Fund’s management, the representations made in the Onshore XL Fund’s offering materials are attributable to each of these defendants. In light of the substantial participation of Tremont Group Holdings, Tremont Bermuda, and Tremont Partners in the Offshore XL

Fund's management, the representations made in the Offshore XL Fund's offering materials are attributable to each of these defendants.

*The December 2006 – May 2007 Conference Calls and Meetings*

62. On December 18, 2006, Johnston and Monica Pascu ("Pascu"), RIM's Director of Investment Services, met with plaintiffs' representatives. Johnston and Pascu reported to plaintiffs' representatives, among other things, that Tremont Partners used an industry-standard system in the administration and monitoring of investment advisors' trading and portfolios.

63. On January 31, 2007, Johnston participated in a conference call with plaintiffs' representatives. Johnston reported to plaintiffs' representatives the purported appreciation of the portfolio managed by Madoff and BMIS.

64. In March 2007, Johnston and Brian Marsh ("Marsh"), a RIM associate, participated in a conference call with plaintiffs' representatives. Johnston and Marsh reported to plaintiffs' representatives the purported appreciation of the portfolio managed by Madoff and BMIS. Johnston and Marsh also described how the Tremont Defendants purportedly monitored and reconciled Madoff's and BMIS's reported trading activity.

65. On May 4, 2007, Johnston and Marsh participated in a conference call with plaintiffs' representatives. Johnston and Marsh reported to plaintiffs' representatives the purported appreciation of the portfolio managed by Madoff and BMIS. Johnston and Marsh explained that Robert I. Schulman (Tremont Group Holdings' Chief Executive Officer and Chairman, and the President and CEO of RIM)

was focused on single-manager platforms and maintaining relationships with, among others, Madoff and BMIS.

***The Offshore Reference Entity 2007 DDQ***

66. On November 1, 2007, plaintiffs received the Offshore Reference Entity's responses to a standardized DDQ dated June 30, 2007. In light of the substantial participation of Tremont Group Holdings (of which RIM is a division), Tremont Bermuda (the investment manager) and Tremont Partners (the sub-advisor) in the management of the Offshore Reference Entity, the representations made in this DDQ are attributable to each of these defendants.

67. With respect to the funds' accounts with BMIS, the Tremont Defendants claimed in this DDQ to "control[] the assets into and out of the brokerage account." Moreover, the Tremont Defendants explained that they had put in place a structure whereby they "manage[] liquidity and ha[ve] full control over the brokerage account." With respect to trading activity by BMIS, the Tremont Defendants claimed that Tremont Bermuda, as investment manager, "reviews each of the trades to ensure that the investment adviser does not deviate from the stated investment strategy," and that trades were reconciled to broker confirmations monthly.

***The August 2007 – June 2008 Conference Calls and Meetings***

68. On August 7, 2007, Marsh participated in a conference call with plaintiffs' representatives. Marsh reported to plaintiffs' representatives the purported appreciation of the portfolio managed by Madoff and BMIS.

69. On October 26, 2007, Johnston and Pascu met with plaintiffs' representatives. During this meeting, Johnston and Pascu told plaintiffs that, given the

personal history between the Tremont Defendants and Madoff and BMIS, and the very sizeable commitment of funds that they directed to BMIS, the Tremont Defendants maintained a close relationship with Madoff and BMIS. Johnston and Pascu told plaintiffs that Schulman and Johnston met with Madoff each year, including most recently in August 2007, and that Schulman spoke with Madoff at least once a month. Johnston and Pascu highlighted the importance of this regular contact with Madoff on behalf of the investors in funds managed by the Tremont Defendants.

70. On January 4, 2008, Marsh participated in a conference call with plaintiffs' representatives. Marsh reported to plaintiffs' representatives the purported appreciation of the portfolio managed by Madoff and BMIS.

71. On March 13, 2008, Marsh participated in a conference call with plaintiffs' representatives. Marsh reported to plaintiffs' representatives the purported appreciation of the portfolio managed by Madoff and BMIS.

72. On June 9, 2008, Johnston and Marsh participated in a conference call with plaintiffs' representatives. Johnston and Marsh reported to plaintiffs' representatives the purported appreciation of the portfolio managed by Madoff and BMIS.

***The RIM 2008 DDQ***

73. On September 23, 2008, plaintiffs received RIM's responses to a standardized DDQ dated June 30, 2008. In light of RIM being a division of Tremont Group Holdings, and the substantial participation in RIM's management of Tremont Partners (chief operating subsidiary of Tremont Group Holdings), the representations

made in this DDQ are attributable to both Tremont Group Holdings and Tremont Partners.

74. In a response to a question about whether it conducted ongoing due diligence visits to BMIS, RIM stated that there were “regular visits by [RIM] staff and senior management of Tremont including the Chief Compliance Officer and representatives from Tremont’s Fund Administration department.”

75. RIM stated that the Tremont Defendants have a “dedicated Operational Due Diligence team that conducts a comprehensive operational review of a manager and its hedge funds prior to a manager being considered for investment.” That team, RIM explained, “is responsible for ensuring that all managers in which Tremont invests, whether directly or through the Rye Select Funds, are operationally sound in all respects.” RIM defined “operational risk” as “the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events,” including “legal risk, which is the risk of loss resulting from failure to comply with laws as well as prudent ethical standards and contractual obligations”; and it identified operational risk losses as being characterized by “several factors including fraud, business practices, business disruption and system failures.”

76. RIM also claimed to have an operational risk management framework in place, and assured that the employees tasked with this process remained independent through “a series of checks and balances,” and the systematization of many aspects of the evaluation process so to “ensure that it is not dependent solely on human judgment.” RIM described the “initial operational review” as covering “all of the non-investment related aspects of the manager and its funds,” including “compliance, trade

execution, reconciliations, valuation and NAV calculation, cash movements and business continuity plans.” The operational review team “focuses in-depth on the valuation review to include discussions with senior operations professionals to gain an understanding of the products that are traded, the source of the pricing data used for valuation, and who is responsible for the official NAV calculation for the hedge fund.”

***The September 2008 – November 2008 Conference Calls and Meetings***

77. On September 19, 2008, Mitchell and Marsh participated in a conference call with plaintiffs’ representatives. Mitchell and Marsh reported to plaintiffs’ representatives the purported appreciation of the portfolio managed by Madoff and BMIS.

78. On November 12, 2008, James V. Mitchell (“Mitchell”), who was a Director of the Offshore XL Fund, Senior Vice President and Managing Director of RIM, and a member of defendant Tremont Group Holdings’ Investment Committee; Johnston; Marsh; Pascu; and Patrick Kelly (“Kelly”), a Senior Vice President at Tremont Group Holdings and Tremont Partners, met with plaintiffs’ representatives for a business operations due diligence meeting. At this meeting, these individual defendants conveyed to plaintiffs’ representatives that returns on the XL Funds are reported weekly on the funds’ web site; monthly returns estimates are available on the fifth business day of the following month; and the NAV/Capital Balance Statement is available on the last business day of the month.

***Financial Disclosures***

79. In addition to the communications described above, the Tremont Defendants sent to plaintiffs’ representatives detailed documentary presentations

throughout the duration of plaintiffs' investment in the XL Funds that purported to reflect the financial results of the XL Funds' investments.

80. The financial disclosures the Tremont Defendants sent to plaintiffs' representatives included the 2005 financial statements for the Prime Fund, received April 10, 2006; the 2005 financial statements for the Offshore Reference Entity, dated March 30, 2006; the 2006 financial statements for the Onshore XL Fund, dated March 26, 2007; the 2006 financial statements for the Onshore Reference Entity, dated March 26, 2007; the 2006 financial statements for the Offshore XL Fund, dated April 27, 2007; the 2006 financial statements for the Offshore Reference Entity, dated May 22, 2007; the 2007 financial statements for the Onshore XL Fund, dated March 24, 2008; the 2007 financial statements for the Onshore Reference Entity, dated March 24, 2008; the 2007 financial statements for the Offshore XL Fund, dated May 9, 2008; and the 2007 financial statements for the Offshore Reference Entity, dated May 9, 2008. The Tremont Defendants also sent to plaintiffs' representatives quarterly account statements and monthly performance updates for the XL Funds.

81. All of these financial disclosures indicated that these funds' assets existed and were consistently appreciating.

***The Tremont Defendants' Representations Were Knowingly or Recklessly False and Misleading***

82. The representations by the Tremont Defendants described above, and others, were knowingly or recklessly false and misleading. During the first week of December 2008, it was revealed that Madoff's and BMIS's investment advisory operation was a massive fraud. Madoff reportedly told a senior employee that he was "finished," that he had "absolutely nothing," that "it's all just one big lie," and that it was

“basically, a giant Ponzi scheme.” He reportedly explained that he had for years been paying returns to certain investors out of the principal received from other, different, investors; and that the business was insolvent and had been for years.

83. On March 12, 2009, Madoff pled guilty to all eleven counts in the criminal information filed by the United States Attorney’s Office, admitting that he perpetrated a fraud since the early 1990s (prosecutors charged that the fraud began in the early 1980s). In his plea allocution, Madoff admitted that he never invested his investment advisory clients’ funds in securities, that he never employed the split-strike conversion strategy he (and the Tremont Defendants) touted, and that he never had custody of the securities he purportedly held for his investment advisory clients. Instead, Madoff and BMIS merely deposited client funds into an account at Chase Manhattan Bank, and distributed money from this account to clients who requested redemptions.

84. Madoff also admitted that he caused to be created and sent to his clients false trading confirmation and client account statements that reflected bogus transactions and positions. Prosecutors charged that Madoff hired numerous employees with little or no prior pertinent training or experience in the securities industry to perform these and other “back office” functions. Madoff admitted that he knew that the audited financial statements he filed with the SEC were false and misleading; BMIS’s accountant (F&H) was soon thereafter charged with fraud on March 18, 2009.

85. Madoff also described in his plea allocution how he wired money between BMIS’s bank accounts and the London bank account of BMIS United Kingdom affiliate Madoff Securities International Ltd. Prosecutors charged that these transfers

were designed to give the appearance that he was conducting securities transactions in Europe.

86. If the Tremont Defendants actually had conducted the due diligence and monitoring they claimed, they would have been aware of these facts. They would have realized that the assets BMIS purportedly held and the trades BMIS purportedly executed for the benefit of the Reference Entities and the XL Funds could not be corroborated with sources independent of Madoff and BMIS.

87. Without such corroborating evidence, the Tremont Defendants never could have gained a sufficient basis to provide plaintiffs with reports that purported to reflect positive returns and the Tremont Defendants' active and effective oversight of plaintiffs' invested capital.

88. The Tremont Defendants either failed to perform the due diligence or monitoring they claimed to have performed, or they uncovered evidence of Madoff's Ponzi scheme, and knowingly or recklessly misrepresented to plaintiffs' representatives that the Reference Entities' and the XL Funds' assets existed and were appreciating – all in order to continue collecting substantial management fees from plaintiffs.

### **KPMG**

89. KPMG LLP was engaged to perform audits of the financial statements of the Onshore XL Fund for the years 2006 and 2007, and the Onshore Reference Entity and the Prime Fund for the years 2005 through 2007; KPMG Cayman was engaged to perform audits of the financial statements of the Offshore XL Fund and Offshore Reference Entity for the years 2006 and 2007 (the audited onshore and offshore

funds are collectively referred to herein as the “Audited Entities”). These audits were to be performed in accordance with United States GAAS.

***GAAS Requirements***<sup>4</sup>

90. GAAS required KPMG to exercise due professional care in the performance of its audits and the preparation of its reports. (AU §§ 150.02, 230.02.) Due professional care required KPMG to exercise professional skepticism, an attitude that includes a questioning mind and a critical assessment of audit evidence. (AU § 230.07.)

91. GAAS required KPMG to obtain a sufficient understanding of the Audited Entities and their environment, including their internal controls, in order to assess the risk of material misstatement of the Audited Entities’ financial statements, whether due to error or fraud, and to design the nature, timing, and extent of further audit procedures. (AU § 150.02.)

92. As part of the process of obtaining an understanding of the Audited Entities and their environment, KPMG was required to obtain an understanding of, among other things, the Audited Entities’ industry; their nature; and the objectives, strategies, and related business risks that may result in a material misstatement of the their financial statements. This included obtaining an understanding of the Audited

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<sup>4</sup> In early 2006, the Auditing Standards Board of the AICPA, which promulgates GAAS, issued several new Statements on Auditing Standards, primarily to emphasize the auditor’s assessment of the risk of material misstatement of financial statements and the responses to such assessed risk. These standards became effective for audits of periods beginning after December 15, 2006, but auditors (like KPMG) could elect to apply these new standards earlier. Sections of the prior codification, where different from the current section numbers, are cited here as “Old AU § xxx.xx.”

Entities' operations, ownership, governance, structure, how they were financed, and the types of investments they made. (AU §§ 314.21, 314.26; Old AU §§ 311.06, 311.07.)

93. As part of the process of obtaining an understanding of the Audited Entities' internal controls, GAAS required KPMG to evaluate the design of those controls, and determine whether they had been implemented. (AU § 314.40; Old AU § 319.25.) Additionally, if KPMG planned to rely on the internal controls of the Audited Entities, GAAS required KPMG to determine that these controls were operating effectively. (AU §§ 318.13, 318.23, 318.24, 318.45; Old AU § 319.66.) "Internal control is a process – effected by those charged with governance, management, and other personnel – designed to provide reasonable assurance about the achievement of the entity's objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations." (AU § 314.41; Old AU § 319.06.)

94. GAAS recognizes that an understanding of an entity and its environment, including its internal controls, does not provide by itself a sufficient basis for forming an opinion on an entity's financial statements. Rather, GAAS requires the auditor to perform further audit procedures. (AU § 150.02.) Further audit procedures include "tests of controls" and/or "substantive procedures."

95. *Tests of controls* are used to "obtain audit evidence that controls operate effectively. This includes obtaining audit evidence about how controls were applied at relevant times during the period under audit, the consistency with which they were applied, and by whom or by what means they were applied." (AU § 318.26; Old AU § 319.76.) *Substantive procedures* are performed to detect material misstatements,

and primarily include tests of details of balance sheet and income statement accounts, and of analytical procedures. (AU § 318.50; Old AU § 319.108.)

96. Because effective internal controls generally reduce, but do not eliminate, the risk of material misstatement, and because an auditor's assessment of risk is judgmental and may not be sufficiently precise to identify all risks of material misstatement, tests of controls reduce, but do not eliminate, the need for substantive procedures. (AU §§ 318.09, 318.51.) Therefore, GAAS required KPMG to design and perform substantive procedures for each of the Audited Entities' material balance sheet and income statement accounts – such as the Audited Entities' investments and their investment income. More specifically, KPMG was required to test (i) the existence and valuation of the Audited Entities' securities at every balance sheet date; (ii) the Audited Entities' ownership of those securities; (iii) the occurrence and accuracy of the Audited Entities' transactions in U.S. Treasury obligations, stocks, and options; and (iv) the reasonableness of the Audited Entities' reported investment income. (AU §§ 318.09, 318.51, 326.15, 332.21-22, 332.25; Old AU §§ 319.107, 326.03 -326.07.)

97. Upon information and belief, KPMG knew that Tremont Partners (as general partner of the onshore Audited Entities, and investment manager/sub-advisor to the offshore Audited Entities) engaged Madoff and BMIS to perform the functions of investment advisor, prime broker, and custodian of the Audited Entities' investments.

98. This concentration of functions at BMIS created risks requiring special audit consideration – what GAAS calls “significant risks.” (AU § 314.110.) Because *all* of the Audited Entities' investment and income information available to KPMG was based on information from BMIS, KPMG needed to do more than rely *solely*

on the procedures it performed with respect to the Audited Entities. (AU §§ 314.115, 318.53, 332.20.)<sup>5</sup> In these circumstances, KPMG should have determined whether a reputable auditor conducted adequate procedures to satisfy itself as to the effectiveness of BMIS's internal controls (AU §§ 332.18, 332.20), or as to the existence of assets and the occurrence of trades reported by BMIS.

99. Here, BMIS's auditor failed to perform such procedures. GAAS required KPMG, to the extent it relied on any audit work performed by F&H,<sup>6</sup> to consider F&H's reputation and standing in the audit community. (AU §§ 324.18, 543.10.) F&H operated out of a small storefront office in Rockland County, New York, and consisted of one retiree in Florida (since deceased), an administrative assistant, and one active accountant who represented to the AICPA that he does not perform audit services. Moreover, F&H had not been "peer reviewed," which posed increased risk and greater concern.

100. These facts alone, easily discoverable by KPMG (AU §§ 324.18, 543.10(a) n.4), should have caused KPMG, if it intended to rely on F&H's audit work, to perform additional procedures to assess the adequacy of that work.

101. Had KPMG reviewed F&H's work papers (*see* AU §§ 324.19, 543.12), it would have discovered that F&H's audits were a sham, and that it failed to

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<sup>5</sup> Pursuant to the prior codification of auditing standards, GAAS required KPMG, upon identifying a risk of a material misstatement due to fraud, to develop an understanding of internal controls related thereto, evaluate the design of such controls, determine whether they have been placed in operation, and develop an appropriate audit response. (Old AU §§ 316.44, 316.48.)

<sup>6</sup> It is unclear whether KPMG received audit reports by F&H. The SEC, in its complaint against Friehling and F&H, alleges that F&H prepared an "Independent Auditors' Report on Internal Control," and that BMIS provided this report directly only to certain investors.

document its purported findings and conclusions, as required by GAAS (AU § 339.10). As the SEC has alleged in its complaint against Friebling and F&H, F&H never conducted legitimate audits. Specifically, the SEC has alleged that F&H failed, among other things, to conduct any audit procedures with respect to BMIS's internal controls, or to confirm that the securities BMIS claimed to hold for its customers did, in fact, exist. Instead, the SEC alleges, F&H, among other things, conducted only physical inventory checks of securities that happened to be on hand, without verifying the existence of certificates purportedly held by outside clearing organizations or depositories.

102. In view of this concentration of functions, the reputation and standing of F&H, and the inadequacy of F&H's work, KPMG should have obtained additional audit evidence relating to the effectiveness of the functions performed by BMIS relevant to the Audited Entities' reported investments and investment income. (AU § 332.18, 332.20.)

103. For example, KPMG should have obtained additional audit evidence about the operating effectiveness of those controls relating to initiation, recording, processing, and reporting of BMIS's investment advisory clients' transactions (including those of the Audited Entities), and those relating to the custody of BMIS's investment advisory clients' investments (including those of the Audited Entities). (AU §§ 318.25, 332.18, 332.20; Old AU §§ 319.65 - 319.74.) Furthermore, KPMG should have required that substantive procedures be performed at BMIS relating to the Audited Entities' reported investments and investment income. (AU §§ 318.09, 318.51; Old AU § 319.107.) KPMG could have performed these procedures itself, or it could have relied

on a report from a reputable auditor whose work was adequate to meet these audit objectives. (AU §§ 324.10, 324.12, 324.18-19, 543.10, 543.12.)

***KPMG Acted Improperly***

104. For the reasons described below, KPMG could not have obtained sufficient audit evidence about the operating effectiveness of controls at BMIS, or reasonably have satisfied itself about the existence of the investments and the reasonableness of the reported investment income by performing substantive audit procedures. Nevertheless, it recklessly issued unqualified audit opinions on the Audited Entities' financial statements.

105. In view of the unreliability of F&H's audit work, as described above, KPMG could not have issued unqualified audit opinions on the Audited Entities' financial statements unless additional audit procedures were performed, the results of which reasonably satisfied KPMG that the reported securities existed and the reported investment income was reasonably stated. KPMG could have tried to obtain this satisfaction either by (i) having a reputable auditor engaged to perform adequate audit procedures, or (ii) performing these procedures itself. No evidence has been reported to date that suggests such procedures were performed by any auditor, including KPMG. Moreover, it is highly unlikely that Madoff would have allowed a reputable auditor to perform the procedures required by GAAS. If these required procedures could not be performed, then GAAS required that KPMG disclaim an opinion on the Audited Entities' financial statements. (AU § 508.62.)

106. Even if KPMG or another reputable firm *had* performed these required procedures, for the reasons described below doing so would have uncovered that the securities did not exist and trades did not occur.

107. Because of the concentration of functions at BMIS, the reputation and standing of F&H, and the inadequacy of F&H's work, the resulting need for heightened professional skepticism would have required that the procedures performed by KPMG or another reputable firm include seeking corroboration of the existence of the assets and the occurrence of trades from sources *independent of BMIS*. (AU §§ 326.08, 326.11.) Any such attempts would have revealed the Madoff/BMIS fraud.

108. For example, Madoff and BMIS claimed to hold all of its investment advisory clients' assets – purportedly billions of dollars – in U.S. Treasuries at the end of each reporting period. An auditor having access to BMIS's books and records easily could have sought to corroborate the existence of these U.S. Treasuries – especially given the large amount reported – by requesting confirmations from the depository institutions or clearing institutions at which book entries for these assets should have existed. If Madoff and BMIS actually held the U.S. Treasuries reported, these confirmations would have indicated U.S. Treasuries BMIS held in the aggregate for all of its clients totaling in the multi-billions of dollars.

109. However, no such confirmations were possible. As Madoff admitted in his plea allocution, Madoff and BMIS held *no* investment advisory clients' assets in Treasuries, let alone *billions* of dollars worth. Rather, according to Madoff, BMIS held only cash in an account at Chase Manhattan Bank, from which he operated his Ponzi scheme. Accordingly, a confirmation from these depository institutions or

clearing institutions would have shown only the U.S. Treasuries BMIS held for the clients of its legitimate brokerage business – an amount, if anything, that in all likelihood would have been dwarfed by the billions of dollars BMIS claimed to hold for its investment advisory clients. In other words, seeking such confirmations, which depository institutions routinely send, very likely would have immediately revealed Madoff's and BMIS's fraud.

110. KPMG also could have sought to corroborate Madoff's and BMIS's purported purchases and sales of equities for the Audited Entities by (a) instructing Madoff and BMIS to request confirmation of these trades from depository or clearing organizations or counterparties to the trades, and (b) reconciling the trades to settlement reports from these organizations or counterparties. Such procedures would have revealed either that no such trades had occurred, or that the amounts were inconsistent with the trades that the Audited Entities reported Madoff and BMIS had made.

111. With respect to the over-the-counter option trades Madoff and BMIS claimed to make for their investment advisory clients, Madoff testified to the SEC on or about May 19, 2006 that the counterparties to his purported option contracts were "basically European banks," and that there is "an affirmation that's generated electronically" and an electronic "master option agreement" that is attached to the affirmation that documented these option trades. Madoff admitted in his plea allocution that these option trades never occurred. Thus, had an auditor sought to confirm this non-existent documentation with these European bank (and any other) counterparties, the fraud would have been immediately revealed.

112. By whatever means, any meaningful attempt at seeking corroboration of the existence of assets and occurrence of trades independent of BMIS would have uncovered the fraud. Because KPMG issued unqualified audit opinions on the Audited Entities financial statements, it is clear that neither KPMG, nor any other reputable auditor at KPMG's request, ever attempted to obtain this independent corroboration.

113. In sum, in these circumstances KPMG (i) could not rely on F&H's purported audit work on BMIS, including any F&H reports on internal controls; and (ii) should have verified the existence of the assets and the occurrence of trades either by having a reputable auditor corroborate the reported assets and trades with sources independent of BMIS, or by doing so itself. Accordingly, under no circumstances should KPMG have issued unqualified opinions on the Audited Entities' financial statements, or claimed its audits were performed in accordance with GAAS. By doing so, KPMG acted improperly, and was reckless.

***KPMG Disseminated False Audit Reports to Plaintiffs***

114. Although KPMG failed to perform its audits of the Audited Entities in accordance with GAAS, it nevertheless sent to plaintiffs unqualified audit opinions with respect to the financial statements of each of the Audited Entities.

115. KPMG LLP sent to plaintiffs audit reports on the Prime Fund's 2005 financial statements dated March 6, 2006, which the Onshore Plaintiffs received on or about April 10, 2006; on the Onshore XL Fund's 2006 financial statements dated March 26, 2007; and on the 2007 financial statements dated March 24, 2008.

116. KPMG Cayman sent to plaintiffs audit reports on the Offshore XL Fund's 2006 financial statements dated April 27, 2007; on the Offshore Reference Entity's 2006 financial statements dated May 22, 2007; on the Offshore XL Fund's 2007 financial statements dated May 9, 2008; and for the Offshore Reference Entity's 2007 financial statements dated May 9, 2008.

117. In each of its audit reports sent to plaintiffs, KPMG stated that it conducted its audits in accordance with GAAS, and expressed its unqualified opinion that the funds' financial statements "present fairly, in all material respects, the financial position of the [fund] ... and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States."

118. Because KPMG violated GAAS in the face of known dangers arising from the concentration of functions at BMIS and the unreliability of F&H's purported audit work, it was reckless for KPMG to send to plaintiffs unqualified audit opinions on the Audited Entities' financial statements.

***Plaintiffs Justifiably Relied on KPMG's Audit Opinions to Their Detriment***

119. KPMG knew that plaintiffs would rely on the audit opinions it sent to plaintiffs concerning the Audited Entities' financial statements. In particular, KPMG LLP knew that the Onshore Plaintiffs would rely on its audits of all of the onshore Audited Entities when the Onshore Plaintiffs made and retained investments in the Onshore XL Fund, because Madoff and BMIS purportedly managed each Audited Entity's portfolio using the same strategy. Similarly, KPMG Cayman knew that the

Offshore Plaintiffs would rely on its audits of all of the offshore Audited Entities when the Offshore Plaintiffs made and retained investments in the Offshore XL Fund.

120. The Onshore Plaintiffs reasonably and justifiably relied on KPMG LLP's audit opinions in deciding to buy and retain partnership interests/shares in the Onshore XL Funds, and the Offshore Plaintiffs reasonably and justifiably relied on KPMG Cayman's audit opinions in deciding to buy and retain partnership interests/shares in the Offshore XL Funds.

121. The Onshore Plaintiffs were damaged by KPMG LLP's wrongful conduct in that it caused them to purchase and retain partnership interests in the Onshore XL Funds that were worthless, and also caused them to lose all of their investments in the Onshore XL Funds when those funds collapsed. The Offshore Plaintiffs were damaged by KPMG Cayman's wrongful conduct in that it caused them to purchase and retain partnership interests in the Offshore XL Funds that were worthless, and also caused them to lose all of their investments in the Offshore XL Funds when those funds collapsed.

**FIRST CLAIM FOR RELIEF**  
**(By the Onshore Plaintiffs**  
**against Tremont Group Holdings and Tremont Partners**  
**for Violation of Section 10(b) of the Securities Exchange Act of 1934**  
**and Rule 10b-5 Thereunder)**

122. Plaintiffs repeat the allegations of paragraphs 1 through 121 as if set forth in their entirety herein.

123. Tremont Group Holdings and Tremont Partners knowingly or recklessly made or approved deceptive and materially false and misleading statements to the Onshore Plaintiffs, including in offering materials, DDQs, financial disclosures, and

direct conversations, that are attributable to Tremont Group Holdings and Tremont Partners as particularized above.

124. These false and misleading statements misrepresented that Tremont Group Holdings and Tremont Partners had conducted due diligence on Madoff and BMIS, were familiar with Madoff's and BMIS's operations, and were monitoring Madoff's and BMIS's transactions, internal controls, and operational risk; that the assets purportedly managed by Madoff and BMIS on behalf of the Onshore XL Fund and the Onshore Reference Entity existed and were appreciating; and that the trades Madoff and BMIS purported to be making on behalf of the Onshore XL Fund and the Onshore Reference Entity occurred.

125. In fact, Tremont Group Holdings and Tremont Partners knew or recklessly ignored that Madoff and BMIS were engaging in a massive Ponzi scheme; that they had not conducted due diligence on Madoff and BMIS, were not familiar with Madoff's and BMIS's operations, and were not monitoring Madoff's and BMIS's transactions, internal controls, and operational risk; that the assets purportedly managed by Madoff and BMIS on behalf of the Onshore XL Fund and the Onshore Reference Entity did not exist; and that the trades Madoff and BMIS purported to be making on behalf of the Onshore XL Fund and the Onshore Reference Entity had not occurred.

126. If Tremont Group Holdings and Tremont Partners had conducted due diligence on Madoff and BMIS, were familiar with Madoff's and BMIS's operations, and were monitoring Madoff's and BMIS's transactions, internal controls, and operational risk as they represented, it would have been so obvious to Tremont Group

Holdings and Tremont Partners that the assets did not exist and the trades had not occurred that they would have been aware of these facts.

127. Tremont Group Holdings and Tremont Partners knew and intended that the Onshore Plaintiffs would rely on their misrepresentations in purchasing partnership interests in the Onshore XL Fund.

128. The Onshore Plaintiffs reasonably and justifiably relied on Tremont Group Holdings' and Tremont Partners' misrepresentations in purchasing partnership interests in the Onshore XL Fund. The Onshore Plaintiffs would not have bought partnership interests in the Onshore XL Fund if they had been aware that Tremont Group Holdings and Tremont Partners had not conducted due diligence on Madoff and BMIS, and were not monitoring Madoff's and BMIS's transactions, internal controls, and operational risk; or that the assets purportedly managed by Madoff and BMIS on behalf of the Onshore XL Fund and the Onshore Reference Entity did not exist; or that the trades Madoff and BMIS purported to be making on behalf of the Onshore XL Fund and the Onshore Reference Entity had not occurred.

129. Tremont Group Holdings and Tremont Partners, by their use of the means or instrumentalities of interstate commerce and/or the mails, to knowingly or recklessly employ devices, schemes, and artifices to defraud, make untrue statements of material facts, and engage in acts of fraud and deceit upon the Onshore Plaintiffs, all in connection with the purchase or sale of a security, violated Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder.

130. Each of the Onshore Plaintiffs has been damaged by the wrongful conduct of Tremont Group Holdings and Tremont Partners in that it caused each of the

Onshore Plaintiffs to purchase partnership interests in the Onshore XL Fund that were worthless.

131. By reason of the foregoing, the Onshore Plaintiffs are entitled to judgment awarding rescissory damages to them against Tremont Group Holdings and Tremont Partners, jointly and severally, in an amount to be determined at the trial of this action, but no less than the entire consideration paid by the Onshore Plaintiffs for their interests in the Onshore XL Fund, net of any redemption proceeds received from the Onshore XL Fund, together with interest at the maximum rate allowable.

132. In the alternative, the Onshore Plaintiffs are entitled to judgment awarding compensatory damages to them against Tremont Group Holdings and Tremont Partners, jointly and severally, in an amount to be determined at the trial of this action, together with interest at the maximum rate allowable.

**SECOND CLAIM FOR RELIEF**  
**(By the Offshore Plaintiffs**  
**against the Tremont Defendants**  
**for Violation of Section 10(b) of the Securities Exchange Act of 1934**  
**and Rule 10b-5 Thereunder)**

133. Plaintiffs repeat the allegations of paragraphs 1 through 132 as if set forth in their entirety herein.

134. The Tremont Defendants knowingly or recklessly made or approved deceptive and materially false and misleading statements to the Offshore Plaintiffs, including in offering materials, DDQs, financial disclosures, and direct conversations, that are attributable to the Tremont Defendants as particularized above.

135. These false and misleading statements misrepresented that the Tremont Defendants had conducted due diligence on Madoff and BMIS, were familiar

with Madoff's and BMIS's operations, and were monitoring Madoff's and BMIS's transactions, internal controls, and operational risk; that the assets purportedly managed by Madoff and BMIS on behalf of the Offshore XL Fund and the Offshore Reference Entities existed and were appreciating; and that the trades Madoff and BMIS purported to be making on behalf of the Offshore XL Funds and the Offshore Reference Entities occurred.

136. In fact, the Tremont Defendants knew or recklessly ignored that Madoff and BMIS were engaging in a massive Ponzi scheme; that they had not conducted due diligence on Madoff and BMIS, were not familiar with Madoff's and BMIS's operations, and were not monitoring Madoff's and BMIS's transactions, internal controls, and operational risk; that the assets purportedly managed by Madoff and BMIS on behalf of the Offshore XL Fund and the Offshore Reference Entity did not exist; and that the trades Madoff and BMIS purported to be making on behalf of the Offshore XL Fund and the Offshore Reference Entity had not occurred.

137. If the Tremont Defendants had conducted due diligence on Madoff and BMIS, were familiar with Madoff's and BMIS's operations, and were monitoring Madoff's and BMIS's transactions, internal controls, and operational risk as they represented, it would have been so obvious to the Tremont Defendants that the assets did not exist and the trades had not occurred that they would have been aware of these facts.

138. The Tremont Defendants knew and intended that the Offshore Plaintiffs would rely on their misrepresentations in purchasing shares of the Offshore XL Fund.

139. Plaintiffs reasonably and justifiably relied on the Tremont Defendants' misrepresentations in purchasing shares of the Offshore XL Fund. The Offshore Plaintiffs would not have bought shares of the Offshore XL Fund if they had been aware that the Tremont Defendants had not conducted due diligence on Madoff and BMIS, and were not monitoring Madoff's and BMIS's transactions, internal controls, and operational risk; or that the assets purportedly managed by Madoff and BMIS on behalf of the Offshore XL Fund and the Offshore Reference Entity did not exist; or that the trades Madoff and BMIS purported to be making on behalf of the Offshore XL Fund and the Offshore Reference Entity had not occurred.

140. The Tremont Defendants, by their use of the means or instrumentalities of interstate commerce and/or the mails, to knowingly or recklessly employ devices, schemes, and artifices to defraud, make untrue statements of material facts, and engage in acts of fraud and deceit upon Offshore Plaintiffs, all in connection with the purchase or sale of a security, violated Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder.

141. Each of the Offshore Plaintiffs has been damaged by the wrongful conduct of the Tremont Defendants in that it caused each of the Offshore Plaintiffs to purchase shares of the Offshore XL Fund that were worthless.

142. By reason of the foregoing, the Offshore Plaintiffs are entitled to judgment awarding rescissory damages to them against each of the Tremont Defendants, jointly and severally, in an amount to be determined at the trial of this action, but no less than the entire consideration paid by the Offshore Plaintiffs for their interests in the

Offshore XL Fund, net of any redemption proceeds received from the Offshore XL Fund, together with interest at the maximum rate allowable.

143. In the alternative, the Offshore Plaintiffs are entitled to judgment awarding compensatory damages to them against each of the Tremont Defendants, jointly and severally, in an amount to be determined at the trial of this action, together with interest at the maximum rate allowable.

**THIRD CLAIM FOR RELIEF**  
**(By the Onshore Plaintiffs and the Offshore Plaintiffs**  
**against Oppenheimer Acquisition**  
**for Violation of Section 20(a) of the Securities Exchange Act of 1934)**

144. Plaintiffs repeat the allegations of paragraphs 1 through 143 as if set forth in their entirety herein.

145. As alleged more fully above, the Tremont Defendants violated Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder.

146. At all relevant times, Oppenheimer Acquisition had the power, both direct and indirect, to control Tremont Group Holdings (and its subsidiaries), and it did in fact exercise such control:

- (i) Tremont Group Holdings was 100% owned by Oppenheimer Acquisition;
- (ii) Oppenheimer Acquisition provided extensive support services to the Tremont Defendants, including compliance, audit, finance, and human resources;
- (iii) Oppenheimer Acquisition directed the Tremont Defendants to change its auditors from Ernst & Young to KPMG, which Oppenheimer Acquisition engaged for its subsidiaries' audit work; and
- (vi) Oppenheimer Acquisition placed John V. Murphy –President and Director of Oppenheimer Acquisition since July 2001, Chairman, Chief Executive Officer, and Director of OppenheimerFunds since June 2001, and President of OppenheimerFunds from September

2000 through February 2007 – on the Board of Directors of Tremont Group Holdings (f/k/a Tremont Capital Management) in November 2001.

147. As a result of Oppenheimer Acquisition's control over the Tremont Defendants, Oppenheimer Acquisition was a controlling person within the meaning of Section 20(a) of the Securities Exchange Act of 1934.

148. By reason of the foregoing, plaintiffs are entitled to judgment awarding rescissory damages to all plaintiffs against Oppenheimer Acquisition in an amount to be determined at the trial of this action, but no less than the entire consideration paid by these plaintiffs for their interests in the XL Funds, net of any redemption proceeds received from the XL Funds, together with interest at the maximum rate allowable.

149. In the alternative, plaintiffs are entitled to judgment awarding compensatory damages to all plaintiffs against Oppenheimer Acquisition in an amount to be determined at the trial of this action, together with interest at the maximum rate allowable.

**FOURTH CLAIM FOR RELIEF**  
**(By the Onshore Plaintiffs**  
**against Tremont Group Holdings and Tremont Partners**  
**for Fraud)**

150. Plaintiffs repeat the allegations of paragraphs 1 through 149 as if set forth in their entirety herein.

151. Tremont Group Holdings and Tremont Partners knowingly or recklessly made or approved deceptive and materially false and misleading statements to the Onshore Plaintiffs, including in offering materials, DDQs, financial disclosures, and

direct conversations, that are attributable to Tremont Group Holdings and Tremont Partners as particularized above.

152. These false and misleading statements misrepresented that Tremont Group Holdings and Tremont Partners had conducted due diligence on Madoff and BMIS, were familiar with Madoff's and BMIS's operations, and were monitoring Madoff's and BMIS's transactions, internal controls, and operational risk; that the assets purportedly managed by Madoff and BMIS on behalf of the Onshore XL Fund and the Onshore Reference Entity existed and were appreciating; and that the trades Madoff and BMIS purported to be making on behalf of the Onshore XL Fund and the Onshore Reference Entity occurred.

153. In fact, Tremont Group Holdings and Tremont Partners knew or recklessly ignored that Madoff and BMIS were engaging in a massive Ponzi scheme; that they had not conducted due diligence on Madoff and BMIS, were not familiar with Madoff's and BMIS's operations, and were not monitoring Madoff's and BMIS's transactions, internal controls, and operational risk; that the assets purportedly managed by Madoff and BMIS on behalf of the Onshore XL Fund and the Onshore Reference Entity did not exist; and that the trades Madoff and BMIS purported to be making on behalf of the Onshore XL Fund and the Onshore Reference Entity had not occurred.

154. If Tremont Group Holdings and Tremont Partners had conducted due diligence on Madoff and BMIS, were familiar with Madoff's and BMIS's operations, and were monitoring Madoff's and BMIS's transactions, internal controls, and operational risk as they represented, it would have been so obvious to Tremont Group

Holdings and Tremont Partners that the assets did not exist and the trades had not occurred that they would have been aware of these facts.

155. Tremont Group Holdings and Tremont Partners knew and intended that the Onshore Plaintiffs would rely on their misrepresentations in purchasing and retaining partnership interests in the Onshore XL Fund.

156. The Onshore Plaintiffs reasonably and justifiably relied on Tremont Group Holdings' and Tremont Partners' misrepresentations in purchasing, and retaining, partnership interests in the Onshore XL Fund. The Onshore Plaintiffs would not have bought partnership interests in the Onshore XL Fund if they had been aware that Tremont Group Holdings and Tremont Partners had not conducted due diligence on Madoff and BMIS, and were not monitoring Madoff's and BMIS's transactions, internal controls, and operational risk; or that the assets purportedly managed by Madoff and BMIS on behalf of the Onshore XL Fund and the Onshore Reference Entity did not exist; or that the trades Madoff and BMIS purported to be making on behalf of the Onshore XL Fund and the Onshore Reference Entity had not occurred.

157. Each of the Onshore Plaintiffs has been damaged by the wrongful conduct of Tremont Group Holdings and Tremont Partners in that such wrongful conduct caused each of the Onshore Plaintiffs to purchase and/or hold partnership interests in the Onshore XL Fund that were worthless, causing each Onshore Plaintiff to lose all of its investment.

158. By reason of the foregoing, the Onshore Plaintiffs are entitled to judgment awarding rescissory damages to them against Tremont Group Holdings and Tremont Partners, jointly and severally, in an amount to be determined at the trial of this

action, but no less than the entire consideration paid by the Onshore Plaintiffs for their interests in the Onshore XL Fund, net of any redemption proceeds received from the Onshore XL Fund, together with interest at the maximum rate allowable.

159. In the alternative, the Onshore Plaintiffs are entitled to judgment awarding compensatory damages to them against Tremont Group Holdings and Tremont Partners, jointly and severally, in an amount to be determined at the trial of this action, together with interest at the maximum rate allowable.

**FIFTH CLAIM FOR RELIEF**  
**(By the Offshore Plaintiffs**  
**against the Tremont Defendants**  
**for Fraud)**

160. Plaintiffs repeat the allegations of paragraphs 1 through 159 as if set forth in their entirety herein.

161. The Tremont Defendants knowingly or recklessly made or approved deceptive and materially false and misleading statements to the Offshore Plaintiffs, including in offering materials, DDQs, financial disclosures, and direct conversations, that are attributable to the Tremont Defendants as particularized above.

162. These false and misleading statements misrepresented that the Tremont Defendants had conducted due diligence on Madoff and BMIS, were familiar with Madoff's and BMIS's operations, and were monitoring Madoff's and BMIS's transactions, internal controls, and operational risk; that the assets purportedly managed by Madoff and BMIS on behalf of the Offshore XL Fund and the Offshore Reference Entity existed and were appreciating; and that the trades Madoff and BMIS purported to be making on behalf of the Offshore XL Fund and the Offshore Reference Entity occurred.

163. In fact, the Tremont Defendants knew or recklessly ignored that Madoff and BMIS were engaging in a massive Ponzi scheme; that they had not conducted due diligence on Madoff and BMIS, were not familiar with Madoff's and BMIS's operations, and were not monitoring Madoff's and BMIS's transactions, internal controls, and operational risk; that the assets purportedly managed by Madoff and BMIS on behalf of the Offshore XL Fund and the Offshore Reference Entity did not exist; and that the trades Madoff and BMIS purported to be making on behalf of the Offshore XL Fund and the Offshore Reference Entity had not occurred.

164. If the Tremont Defendants had conducted due diligence on Madoff and BMIS, were familiar with Madoff's and BMIS's operations, and were monitoring Madoff's and BMIS's transactions, internal controls, and operational risk as they represented, it would have been so obvious to the Tremont Defendants that the assets did not exist and the trades had not occurred that they would have been aware of these facts.

165. The Tremont Defendants knew and intended that the Offshore Plaintiffs would rely on their misrepresentations in purchasing and retaining shares of the Offshore XL Fund.

166. The Offshore Plaintiffs reasonably and justifiably relied on the Tremont Defendants' misrepresentations in purchasing, and retaining, shares of the Offshore XL Fund. The Offshore Plaintiffs would not have bought shares of the Offshore XL Fund if they had been aware that the Tremont Defendants had not conducted due diligence on Madoff and BMIS, and were not monitoring Madoff's and BMIS's transactions, internal controls, and operational risk; or that the assets purportedly managed by Madoff and BMIS on behalf of the Offshore XL Fund and the Offshore

Reference Entity did not exist; or that the trades Madoff and BMIS purported to be making on behalf of the Offshore XL Fund and the Offshore Reference Entity had not occurred.

167. Each of the Offshore Plaintiffs has been damaged by the wrongful conduct of the Tremont Defendants in that such wrongful conduct caused each of the Offshore Plaintiffs to purchase and/or hold shares of the Offshore XL Fund that were worthless, causing each Offshore Plaintiff to lose all of its investment.

168. By reason of the foregoing, the Offshore Plaintiffs are entitled to judgment awarding rescissory damages to them against each of the Tremont Defendants, jointly and severally, in an amount to be determined at the trial of this action, but no less than the entire consideration paid by the Offshore Plaintiffs for their interests in the Offshore XL Fund, net of any redemption proceeds received from the Offshore XL Fund, together with interest at the maximum rate allowable.

169. In the alternative, the Offshore Plaintiffs are entitled to judgment awarding compensatory damages to them against each of the Tremont Defendants, jointly and severally, in an amount to be determined at the trial of this action, together with interest at the maximum rate allowable.

**SIXTH CLAIM FOR RELIEF**  
**(By the Onshore Plaintiffs**  
**against Tremont Group Holdings and Tremont Partners**  
**for Breach of Fiduciary Duty)**

170. Plaintiffs repeat the allegations of paragraphs 1 through 169 as if set forth in their entirety herein.

171. As the general partner to the Onshore XL Fund (Tremont Partners), and the entity of which RIM was a division (Tremont Group Holdings),

respectively, Tremont Partners and Tremont Group Holdings owed the Onshore Plaintiffs the fiduciary duty to use reasonable care, or the competence or skill of a professional investment advisor, in managing and overseeing the Onshore Plaintiffs' assets that were invested with the Onshore XL Fund.

172. Tremont Partners and Tremont Group Holdings entrusted management and custody of the Onshore Plaintiffs' assets to Madoff and BMIS, but retained a fiduciary responsibility to ensure that the Onshore Plaintiffs' assets were being managed as represented by Madoff and BMIS, and with reasonable care, or the competence or skill of a professional investment advisor.

173. Tremont Partners and Tremont Group Holdings breached the fiduciary duties they owed to the Onshore Plaintiffs, and acted in bad faith, with gross negligence and in utter disregard for due care and reasonable and prudent investment standards, by failing to use reasonable care, or the competence or skill of a professional investment advisor, in performing due diligence, managing plaintiffs' investments, providing accurate financial disclosures, and overseeing Madoff's and BMIS's management of the Onshore Plaintiffs' assets.

174. Tremont Partners' and Tremont Group Holdings' failure to use reasonable care, or the competence or skill of a professional investment advisor, to verify that the Onshore Plaintiffs' assets were being managed as represented by Madoff and BMIS, enabled Madoff and BMIS to perpetrate and continue their fraudulent scheme by convincing the Onshore Plaintiffs to invest in, and remain invested in, the Onshore XL Fund.

175. As a result of Tremont Partners' and Tremont Group Holdings' breach of their fiduciary duties, Madoff and BMIS misappropriated the assets he purportedly managed for the Onshore XL Fund as part of his massive Ponzi scheme.

176. Each of the Onshore Plaintiffs has been damaged by the wrongful conduct of Tremont Partners and Tremont Group Holdings in that such wrongful conduct caused each of the Onshore Plaintiffs to purchase and/or hold partnership interests in the Onshore XL Fund that were worthless, causing each Onshore Plaintiff to lose all of its investment.

177. By reason of the foregoing, the Onshore Plaintiffs are entitled to judgment awarding rescissory damages to them against Tremont Partners and Tremont Group Holdings, jointly and severally, in an amount to be determined at the trial of this action, but no less than the entire consideration paid by the Onshore Plaintiffs for their interests in the Onshore XL Fund, net of any redemption proceeds received from the Onshore XL Fund, together with interest at the maximum rate allowable.

178. In the alternative, the Onshore Plaintiffs are entitled to judgment awarding compensatory damages to them against Tremont Partners and Tremont Group Holdings, jointly and severally, in an amount to be determined at the trial of this action, together with interest at the maximum rate allowable.

**SEVENTH CLAIM FOR RELIEF**  
**(By the Offshore Plaintiffs**  
**against the Tremont Defendants**  
**for Breach of Fiduciary Duty)**

179. Plaintiffs repeat the allegations of paragraphs 1 through 178 as if set forth in their entirety herein.

180. As the investment manager for the Offshore XL Fund and the sub-advisor to the Offshore Reference Entity (Tremont Partners), the investment manager for the Offshore Reference Entity (Tremont Bermuda), and the entity of which RIM was a division (Tremont Group Holdings), respectively, the Tremont Defendants owed the Offshore Plaintiffs the fiduciary duty to use reasonable care, or the competence or skill of a professional investment advisor, in managing and overseeing the Offshore Plaintiffs' assets that were invested with the Offshore XL Fund.

181. The Tremont Defendants entrusted management and custody of the Offshore Plaintiffs' assets to Madoff and BMIS, but retained a fiduciary responsibility to ensure that the Offshore Plaintiffs' assets were being managed as represented by Madoff and BMIS, and with reasonable care, or the competence or skill of a professional investment advisor.

182. The Tremont Defendants breached the fiduciary duties they owed to the Offshore Plaintiffs, and acted in bad faith, with gross negligence and in utter disregard for due care and reasonable and prudent investment standards, by failing to use reasonable care, or the competence or skill of a professional investment advisor, in performing due diligence, managing plaintiffs' investments, providing accurate financial disclosures, and overseeing Madoff's and BMIS's management of the Offshore Plaintiffs' assets.

183. The Tremont Defendants' failure to use reasonable care, or the competence or skill of a professional investment advisor, to verify that the Offshore Plaintiffs' assets were being managed as represented by Madoff and BMIS, enabled

Madoff and BMIS to perpetrate and continue their fraudulent scheme by convincing the Offshore Plaintiffs to invest in, and remain invested in, the Offshore XL Fund.

184. As a result of the Tremont Defendants' breach of their fiduciary duties, Madoff and BMIS misappropriated the assets he purportedly managed for the Offshore XL Fund as part of his massive Ponzi scheme.

185. Each of the Offshore Plaintiffs has been damaged by the wrongful conduct of the Tremont Defendants in that such wrongful conduct caused each of the Offshore Plaintiffs to purchase and/or shares of the Offshore XL Fund that were worthless, causing each Offshore Plaintiff to lose all of its investment.

186. By reason of the foregoing, the Offshore Plaintiffs are entitled to judgment awarding rescissory damages to them against each of the Tremont Defendants, jointly and severally, in an amount to be determined at the trial of this action, but no less than the entire consideration paid by the Offshore Plaintiffs for their interests in the Offshore XL Fund, net of any redemption proceeds received from the Offshore XL Fund, together with interest at the maximum rate allowable.

187. In the alternative, the Offshore Plaintiffs are entitled to judgment awarding compensatory damages to them against each of the Tremont Defendants, jointly and severally, in an amount to be determined at the trial of this action, together with interest at the maximum rate allowable.

**EIGHTH CLAIM FOR RELIEF**  
**(By the Onshore Plaintiffs**  
**against Tremont Partners and Tremont Group Holdings**  
**for Negligence)**

188. Plaintiffs repeat the allegations of paragraphs 1 through 187 as if set forth in their entirety herein.

189. As the general partner to the Onshore XL Fund (Tremont Partners), and the entity of which RIM was a division (Tremont Group Holdings), respectively, Tremont Partners and Tremont Group Holdings owed the Onshore Plaintiffs the duty to use reasonable care, or the competence or skill of a professional investment advisor in managing and overseeing the Onshore Plaintiffs' assets that were invested with the Onshore XL Fund.

190. Tremont Partners and Tremont Group Holdings failed to exercise reasonable care by negligently failing to manage and oversee the management by Madoff and BMIS of the Onshore Plaintiffs' investments in the Onshore XL Fund.

191. Tremont Partners' and Tremont Group Holdings' failure to exercise reasonable care enabled Madoff and BMIS to perpetrate and continue their fraudulent scheme by convincing the Onshore Plaintiffs, to invest in, and remain invested in, the Onshore XL Fund.

192. Each of the Onshore Plaintiffs has been damaged by Tremont Partners' and Tremont Group Holdings' failure to exercise reasonable care in that this failure caused each of them to purchase and/or hold partnership interests in the Onshore XL Fund that were worthless, causing each Onshore Plaintiff to lose all of its investment.

193. By reason of the foregoing, the Onshore Plaintiffs are entitled to judgment awarding rescissory damages to them against Tremont Partners and Tremont Group Holdings, jointly and severally, in an amount to be determined at the trial of this action, but no less than the entire consideration paid by the Onshore Plaintiffs for their interests in the Onshore XL Fund, net of any redemption proceeds received from the Onshore XL Fund, together with interest at the maximum rate allowable.

194. In the alternative, the Onshore Plaintiffs are entitled to judgment awarding compensatory damages to them against Tremont Partners and Tremont Group Holdings, jointly and severally, in an amount to be determined at the trial of this action, together with interest at the maximum rate allowable.

**NINTH CLAIM FOR RELIEF**  
**(By the Offshore Plaintiffs**  
**against the Tremont Defendants**  
**for Negligence)**

195. Plaintiffs repeat the allegations of paragraphs 1 through 194 as if set forth in their entirety herein.

196. As the investment manager for the Offshore XL Fund and the sub-advisor to the Offshore Reference Entity (Tremont Partners), the investment manager for the Offshore Reference Entity (Tremont Bermuda), and the entity of which RIM was a division (Tremont Group Holdings), respectively, the Tremont Defendants owed the Offshore Plaintiffs the duty to use reasonable care, or the competence or skill of a professional investment advisor in managing and overseeing the Offshore Plaintiffs' assets that were invested with the Offshore XL Fund.

197. The Tremont Defendants failed to exercise reasonable care by negligently failing to manage and oversee the management by Madoff and BMIS of the Offshore Plaintiffs' investments in the Offshore XL Fund.

198. The Tremont Defendants' failure to exercise reasonable care enabled Madoff and BMIS to perpetrate and continue their fraudulent scheme by convincing the Offshore Plaintiffs, to invest in, and remain invested in, the Offshore XL Fund.

199. Each of the Offshore Plaintiffs has been damaged by the Tremont Defendants' failure to exercise reasonable care in that this failure caused each of them to purchase and/or hold shares of the Offshore XL Fund that were worthless, causing each Offshore Plaintiff to lose all of its investment.

200. By reason of the foregoing, the Offshore Plaintiffs are entitled to judgment awarding rescissory damages to them against each of the Tremont Defendants, jointly and severally, in an amount to be determined at the trial of this action, but no less than the entire consideration paid by the Offshore Plaintiffs for their interests in the Offshore XL Fund, net of any redemption proceeds received from the Offshore XL Fund, together with interest at the maximum rate allowable.

201. In the alternative, the Offshore Plaintiffs are entitled to judgment awarding compensatory damages to them against each of the Tremont Defendants, jointly and severally, in an amount to be determined at the trial of this action, together with interest at the maximum rate allowable.

**TENTH CLAIM FOR RELIEF**  
**(By the Onshore Plaintiffs**  
**against KPMG LLP**  
**for Violations of Section 10(b) of the Securities Exchange Act of 1934**  
**and Rule 10b-5 thereunder)**

202. Plaintiffs repeat the allegations of paragraphs 1 through 201 as if set forth in their entirety herein.

203. KPMG LLP issued to the Onshore Plaintiffs audit reports in which it made materially false and misleading representations that it had conducted the audits of the Onshore XL Fund's, the Onshore Reference Entity's, and the Prime Fund's financial statements in accordance with GAAS, when in fact KPMG LLP did not conduct these

audits in the manner represented. Instead, KPMG LLP knowingly or recklessly failed to obtain sufficient appropriate evidence that the assets presented in the Onshore XL Fund's, the Onshore Reference Entity's, and the Prime Fund's financial statements actually existed, or that the trades from which the reported income was derived actually occurred.

204. The audit reports issued by KPMG LLP were materially false and misleading also in that they falsely represented that the Onshore XL Fund's, the Onshore Reference Entity's, and the Prime Fund's financial statements presented fairly, in all material respects, the financial positions of these funds, and the results of their operations, in conformity with generally accepted accounting principles ("GAAP"). In fact, if KPMG LLP had conducted its audits in accordance with GAAS, it would have been obvious to KPMG LLP that these funds' financial statements had not been prepared in accordance with GAAP, and misstated the existence of investment assets and earnings when those assets and earnings did not exist.

205. KPMG LLP knew that the Onshore Plaintiffs would rely on its audit reports and the false and misleading information contained therein, and would be induced by them to purchase partnership interests in the Onshore XL Fund.

206. The Onshore Plaintiffs relied upon these misstatements in making investment decisions with respect to the partnership interests in the Onshore XL Fund, which they would not have purchased if they had known that the statements made by KPMG LLP were materially false and misleading.

207. KPMG LLP, by its use of the means or instrumentalities of interstate commerce and/or the mails, to recklessly employ devices, schemes, and

artifices to defraud, make untrue statements of material facts, and engage in acts of fraud and deceit upon the Onshore Plaintiffs, all in connection with the purchase or sale of a security, violated Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder.

208. Each of the Onshore Plaintiffs has been damaged by KPMG LLP's wrongful conduct in that it caused each of them to purchase partnership interests in the Onshore XL Fund that were worthless.

209. By reason of the foregoing, the Onshore Plaintiffs are entitled to judgment awarding rescissory damages to them against KPMG LLP in an amount to be determined at the trial of this action, but no less than the entire consideration paid by the Onshore Plaintiffs for their interests in the Onshore XL Fund, net of any redemption proceeds received from the Onshore XL Fund, together with interest at the maximum rate allowable.

210. In the alternative, the Onshore Plaintiffs are entitled to judgment awarding compensatory damages to the Onshore Plaintiffs against KPMG LLP in an amount to be determined at the trial of this action, together with interest at the maximum rate allowable.

**ELEVENTH CLAIM FOR RELIEF**  
**(By the Offshore Plaintiffs**  
**against KPMG Cayman**  
**for Violations of Section 10(b) of the Securities Exchange Act of 1934**  
**and Rule 10b-5 thereunder)**

211. Plaintiffs repeat the allegations of paragraphs 1 through 210 as if set forth in their entirety herein.

212. KPMG Cayman issued to the Offshore Plaintiffs audit reports in which it made materially false and misleading representations that it had conducted the audits of the Offshore XL Fund's and the Offshore Reference Entity's financial statements in accordance with GAAS, when in fact KPMG Cayman did not conduct these audits in the manner represented. Instead, KPMG Cayman knowingly or recklessly failed to obtain sufficient appropriate evidence that the assets presented in the Offshore XL Fund's and the Offshore Reference Entity's financial statements actually existed, or that the trades from which the reported income derived actually occurred.

213. The audit reports issued by KPMG Cayman were materially false and misleading also in that they falsely represented that the Offshore XL Fund's and the Offshore Reference Entity's financial statements presented fairly, in all material respects, the financial positions of these funds, and the results of their operations, in conformity with GAAP. In fact, if KPMG Cayman had conducted its audits in accordance with GAAS, it would have been obvious to KPMG Cayman that these funds' financial statements had not been prepared in accordance with GAAP, and misstated the existence of investment assets and earnings when those assets and earnings did not exist.

214. KPMG Cayman knew that the Onshore Plaintiffs would rely on its audit reports and the false and misleading information contained therein, and would be induced by them to purchase shares of the Offshore XL Fund.

215. The Offshore Plaintiffs relied upon these misstatements in making investment decisions with respect to the shares of the Offshore XL Fund, which they would not have purchased if they had known that the statements made by KPMG Cayman were materially false and misleading.

216. KPMG Cayman, by its use of the means or instrumentalities of interstate commerce and/or the mails, to recklessly employ devices, schemes, and artifices to defraud, make untrue statements of material facts, and engage in acts of fraud and deceit upon the Onshore Plaintiffs, all in connection with the purchase or sale of a security, violated Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder.

217. Each of the Offshore Plaintiffs has been damaged by KPMG Cayman's wrongful conduct in that it caused each of them to purchase shares in the Offshore XL Fund that were worthless.

218. By reason of the foregoing, the Offshore Plaintiffs are entitled to judgment awarding rescissory damages to the Offshore Plaintiffs against KPMG Cayman in an amount to be determined at the trial of this action, but no less than the entire consideration paid by the Offshore Plaintiffs for their interests in the Offshore XL Fund, net of any redemption proceeds received from the Offshore XL Fund, together with interest at the maximum rate allowable.

219. In the alternative, the Offshore Plaintiffs are entitled to judgment awarding compensatory damages to the Offshore Plaintiffs against KPMG Cayman in an amount to be determined at the trial of this action, together with interest at the maximum rate allowable.

**TWELFTH CLAIM FOR RELIEF**  
**(By the Onshore Plaintiffs**  
**against KPMG LLP**  
**for Fraud)**

220. Plaintiffs repeat the allegations of paragraphs 1 through 219 as if set forth in their entirety herein.

221. KPMG LLP issued to the Onshore Plaintiffs audit reports in which it made materially false and misleading representations that it had conducted the audits of the Onshore XL Fund's, the Onshore Reference Entity's, and the Prime Fund's financial statements in accordance with GAAS, when in fact KPMG LLP did not conduct its audits of these funds in the manner represented. Instead, KPMG LLP knowingly or recklessly failed to obtain sufficient appropriate evidence that the assets presented in the Onshore XL Fund's, the Onshore Reference Entity's, and the Prime Fund's financial statements actually existed, or that the trades from which the reported income was derived actually occurred.

222. The audit reports issued by KPMG LLP were materially false and misleading also in that they falsely represented that the Onshore XL Fund's, the Onshore Reference Entity's, and the Prime Fund's financial statements presented fairly, in all material respects, the financial positions of these funds, and the results of their operations, in conformity with GAAP. In fact, if KPMG LLP had conducted its audits in accordance with GAAS, it would have been obvious to KPMG LLP that these funds' financial statements had not been prepared in accordance with GAAP, and misstated the existence of investment assets and earnings when those assets and earnings did not exist.

223. KPMG LLP knew that the Onshore Plaintiffs would rely on its audit reports and the false and misleading information contained therein, and would be induced by them to purchase and/or retain partnership interests in the Onshore XL Fund.

224. The Onshore Plaintiffs relied upon these misstatements in making investment decisions with respect to the partnership interests in the Onshore XL Fund,

which they would not have purchased and/or retained if they had known that the statements made by KPMG LLP were materially false and misleading.

225. Each of the Onshore Plaintiffs has been damaged by KPMG LLP's wrongful conduct in that it caused each of them to purchase partnership interests in the Onshore XL Fund that were worthless, and also caused each plaintiff to lose all of its investment in the Onshore XL Fund when that fund collapsed.

226. By reason of the foregoing, the Onshore Plaintiffs are entitled to judgment awarding rescissory damages to the Onshore Plaintiffs against KPMG LLP in an amount to be determined at the trial of this action, but no less than the entire consideration paid by the Onshore Plaintiffs for their interests in the Onshore XL Fund, net of any redemption proceeds received from the Onshore XL Fund, together with interest at the maximum rate allowable.

227. In the alternative, the Onshore Plaintiffs are entitled to judgment awarding compensatory damages to the Onshore Plaintiffs against KPMG LLP in an amount to be determined at the trial of this action, together with interest at the maximum rate allowable.

**THIRTEENTH CLAIM FOR RELIEF**  
**(By the Offshore Plaintiffs**  
**against KPMG Cayman**  
**for Fraud)**

228. Plaintiffs repeat the allegations of paragraphs 1 through 227 as if set forth in their entirety herein.

229. KPMG Cayman issued to the Offshore Plaintiffs audit reports in which it made materially false and misleading representations that it had conducted the audits of the Offshore XL Fund's and the Offshore Reference Entity's financial

statements in accordance with GAAS, when in fact KPMG Cayman did not conduct its audits of these funds in the manner represented. Instead, KPMG Cayman knowingly or recklessly failed to obtain sufficient appropriate evidence that the assets presented in the Offshore XL Fund's and the Offshore Reference Entity's financial statements actually existed, or that the trades from which the reported income was derived actually occurred.

230. The audit reports issued by KPMG Cayman were materially false and misleading also in that they falsely represented that the Offshore XL Fund's and the Offshore Reference Entity's financial statements presented fairly, in all material respects the financial positions of these funds, and the results of their operations, in conformity with GAAP. In fact, if KPMG Cayman had conducted its audits in accordance with GAAS, it would have been obvious to KPMG Cayman that these funds' financial statements had not been prepared in accordance with GAAP, and misstated the existence of investment assets and earnings when those assets and earnings did not exist.

231. KPMG Cayman knew that the Offshore Plaintiffs would rely on its audit reports and the false and misleading information contained therein, and would be induced by them to purchase and retain shares of the Offshore XL Fund.

232. The Offshore Plaintiffs relied upon these misstatements in making investment decisions with respect to the shares of the Offshore XL Fund, which they would not have purchased and/or retained if they had known that the statements made by KPMG Cayman were materially false and misleading.

233. Each of the Offshore Plaintiffs has been damaged by KPMG Cayman's wrongful conduct in that it caused each of them to purchase and hold shares of

the Offshore XL Fund that were worthless, and also caused each plaintiff to lose all of its investment in the Offshore XL Fund when that fund collapsed.

234. By reason of the foregoing, the Offshore Plaintiffs are entitled to judgment awarding rescissory damages to the Offshore Plaintiffs against KPMG Cayman in an amount to be determined at the trial of this action, but no less than the entire consideration paid by the Offshore Plaintiffs for their interests in the Offshore XL Fund, net of any redemption proceeds received from the Offshore XL Fund, together with interest at the maximum rate allowable.

235. In the alternative, the Offshore Plaintiffs are entitled to judgment awarding compensatory damages to the Offshore Plaintiffs against KPMG Cayman in an amount to be determined at the trial of this action, together with interest at the maximum rate allowable.

**FOURTEENTH CLAIM FOR RELIEF**  
**(By the Onshore Plaintiffs  
against KPMG LLP  
for Negligence)**

236. Plaintiffs repeat the allegations of paragraphs 1 through 235 as if set forth in their entirety herein.

237. As auditors of the Onshore XL Fund, the Onshore Reference Entity, and the Prime Fund, KPMG LLP owed the Onshore Plaintiffs the duty to use reasonable care, or the competence or skill of a professional independent auditor, in conducting audits on these funds, and rendering corresponding audit opinions that were addressed and distributed to the Onshore Plaintiffs, in accordance with GAAS. KPMG LLP knew that the Onshore Plaintiffs would rely upon its audit reports in purchasing and retaining their partnership interests in the Onshore XL Fund.

238. KPMG LLP failed to exercise reasonable care by negligently and/or grossly negligently failing to conduct audits on the Onshore XL Fund, the Onshore Reference Entity, and the Prime Fund in accordance with GAAS, and by addressing and disseminating to the Onshore Plaintiffs unqualified audit opinions that should have been qualified or disclaimed. In the course of this conduct, KPMG LLP failed to inquire into many crucial facts, which, in the exercise of ordinary care, they should not have ignored and should have investigated. KPMG LLP demonstrated a complete disregard for the rights of the Onshore Plaintiffs, as well as for the security of their investments.

239. KPMG LLP's negligence and/or gross negligence enabled Madoff, BMIS, and the Tremont Defendants to perpetrate and continue their fraudulent scheme by convincing the Onshore Plaintiffs to invest in, and remain invested in, the Onshore XL Fund.

240. Each of the Onshore Plaintiffs has been damaged by KPMG LLP's failure to exercise reasonable care in that such failure caused each of them to purchase and/or hold partnership interests in the Onshore XL Fund that were worthless, causing each plaintiff to lose all of its investment.

241. By reason of the foregoing, the Onshore Plaintiffs are entitled to judgment awarding rescissory damages to the Onshore Plaintiffs against KPMG LLP in an amount to be determined at the trial of this action, but no less than the entire consideration paid by the Onshore Plaintiffs for their interests in the Onshore XL Fund, net of any redemption proceeds received from the Onshore XL Fund, together with interest at the maximum rate allowable.

242. In the alternative, the Onshore Plaintiffs are entitled to judgment awarding compensatory damages to the Onshore Plaintiffs against KPMG LLP in an amount to be determined at the trial of this action, together with interest at the maximum rate allowable.

**FIFTEENTH CLAIM FOR RELIEF**  
**(By the Offshore Plaintiffs  
against KPMG Cayman  
for Negligence)**

243. Plaintiffs repeat the allegations of paragraphs 1 through 242 as if set forth in their entirety herein.

244. As auditors of the Offshore XL Fund and the Offshore Reference Entity, KPMG Cayman owed the Offshore Plaintiffs the duty to use reasonable care, or the competence or skill of a professional independent auditor, in conducting audits on these funds, and rendering corresponding audit opinions that were addressed and distributed to the Offshore Plaintiffs, in accordance with GAAS. KPMG Cayman knew that the Offshore Plaintiffs would rely upon its audit reports in purchasing and retaining their shares of the Offshore XL Fund.

245. KPMG Cayman failed to exercise reasonable care by negligently and/or grossly negligently failing to conduct audits on the Offshore XL Fund and the Offshore Reference Entity in accordance with GAAS, and by addressing and disseminating to the Offshore Plaintiffs unqualified audit opinions that should have been qualified or disclaimed. In the course of this conduct, KPMG Cayman failed to inquire into many crucial facts, which, in the exercise of ordinary care, they should not have ignored and should have investigated. KPMG Cayman demonstrated a complete

disregard for the rights of the Offshore Plaintiffs, as well as for the security of their investments.

246. KPMG Cayman's negligence and/or gross negligence enabled Madoff, BMIS, and the Tremont Defendants to perpetrate and continue their fraudulent scheme by convincing the Offshore Plaintiffs to invest in, and remain invested in, the Offshore XL Fund.

247. Each of the Offshore Plaintiffs has been damaged by KPMG Cayman's failure to exercise reasonable care in that such failure caused each of them to purchase and/or hold shares of the Offshore XL Fund that were worthless, causing each plaintiff to lose all of its investment.

248. By reason of the foregoing, the Offshore Plaintiffs are entitled to judgment awarding rescissory damages to the Offshore Plaintiffs against KPMG Cayman in an amount to be determined at the trial of this action, but no less than the entire consideration paid by the Offshore Plaintiffs for their interests in the Offshore XL Fund, net of any redemption proceeds received from the Offshore XL Fund, together with interest at the maximum rate allowable.

249. In the alternative, the Offshore Plaintiffs are entitled to judgment awarding compensatory damages to the Offshore Plaintiffs against KPMG Cayman in an amount to be determined at the trial of this action, together with interest at the maximum rate allowable.

**WHEREFORE, plaintiffs pray for judgment awarding them:**

(a) Rescissory damages against each of the defendants, jointly and severally, in an amount to be determined at the trial of this action, but no less than the

entire consideration paid by these plaintiffs for their interests in the XL Funds, net of any redemption proceeds received from the XL Funds;

- (b) In the alternative, compensatory damages against each of the defendants, jointly and severally, in amounts to be determined at trial;
- (c) Interest on any award at the maximum allowable rate;
- (d) Their costs and disbursements in this action including, to the extent applicable, attorneys' fees; and
- (e) Such other and further relief as the Court deems just and proper.

**JURY DEMAND**

Plaintiffs hereby demand a trial by jury of all issues so triable.

Dated: New York, New York  
April 10, 2009

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