SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK
- X

STATE OF NEW YORK,

Plaintiff,

-against-

COMPLAINT

Index No.

MILLENNIUM PARTNERS, L.P.,
MILLENNIUM USA, L.P., MILLENNIUM GLOBAL
ESTATE, L.P., MILLENNIUM
INTERNATIONAL, LTD., MILLENNIUM
MANAGEMENT, L.L.C., MILLENNIUM
INTERNATIONAL MANAGEMENT, L.L.C.,
MILLENNIUM HOLDING GROUP, L.P., *et al.*,

Defendants.

ELIOT SPITZER
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Attorney for Plaintiff
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New York, New York 10271
(212) 416-6542

Of Counsel:

CHARLES T. CALIENDO

Assistant Attorney General

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KP FAMILY, LLC, KP FAMILY ANNUITY TRUST,
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LINKAGE ASSOCIATES LLC, MANTECA LLC,
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TAIGA GROUP, LLC, TIPTON ASSOCIATES, LLC,
TRITIUM, LLC, TRUMAN LLC, TUNICA LLC,
UMBER PARTNERS LLC, UMIAK WAY LLC,
VALONIA LLC, VARIAD LLC, VENTURA WAY LLC,
VERSINE LLC, WARREN WAY LLC, WHESTON LLC, :
WIGGINS LLC, WYATT ATWOOD & CO. LLC,
YAXIS GROUP LLC, YAKIMA LLC, ZENITH COURT
LLC, ZIRCON VENTURES LLC, ZORGON LLC,
ISRAEL A. ENGLANDER, TERENCE W. FEENEY,
FRED M. STONE and KOVAN K. PILLAI,

Defendants.

Plaintiff, by Eliot Spitzer, Attorney General of the State of New York (the "Attorney General"), on behalf of the State of New York, complaining of the above-named defendants, alleges the following upon information and belief:

SUMMARY OF THE CASE

1. The Attorney General brings this civil action against (a) Millennium Partners, L.P. and more than one hundred subsidiaries or affiliated entities (individually or collectively sometimes referred to as "Millennium"), (b) Israel A. ("Izzy") Englander, Millennium's controlling principal, (c) Terence W. Feeney, a Millennium Vice Chairman and its Chief Operating Officer, (d) Fred M. Stone, Millennium's General Counsel, and (e) Kovan K. Pillai, a Millennium securities trader, for fraud, deception, false pretenses and concealment and suppression of material facts involving securities in violation of New York State's Martin Act and other statutes. The Attorney General additionally brings this action for common law fraud.

2. Millennium is a private investment fund (commonly referred to as a "hedge fund") for wealthy individuals and institutions. The minimum investment is $5 million.

3. To deploy the more than $5 billion it has under management, Millennium employs numerous professional securities and commodities traders who execute various investment strategies. Their mission, according to Millennium's offering documents, "is to exploit market inefficiencies and to profit by financial arbitrage." In pursuit of this objective – a legitimate one shared by many hedge funds and other investors, Millennium's senior management coordinates the activities of these traders and decides how much capital to allocate to which strategy and then to which of the several traders executing that strategy.

4. From at least 1999 to 2003, one strategy employed by Millennium was trading shares of mutual funds on a short-term basis. This strategy, commonly referred to as "market timing," was designed primarily, but not exclusively, to exploit inefficiencies in the way that

mutual funds price their shares. Millennium's senior management devoted between up to approximately 15% and 25% of Millennium's capital to market timing strategies and Millennium's traders enjoyed considerable success. Market timing accounted for between approximately 10% and 20% of Millennium's profits from 2001 to 2003.

5. Market timing can cause damage to long term mutual fund shareholders. To discharge their fiduciary obligations, mutual funds (or their agents) generally seek to identify, monitor and reject harmful "timing" transactions in accordance with the mutual fund's legal rights to prevent professional traders and others from engaging in such activity and restrictions on short-term trading stated in prospectuses and/or fund company policies.

6. Millennium's market timing activities caused damage to long term mutual fund shareholders. It was not necessarily illegal or fraudulent, however, for Millennium to have simply engaged in a market timing strategy. The mutual funds owed fiduciary duties to long term shareholders; Millennium did not. It was, therefore, the responsibility of mutual funds – not Millennium – to protect the interests of long term shareholders. But, Millennium did not achieve all or even a substantial part of its market timing investment returns by simply "exploiting market inefficiencies." Many mutual fund complexes would not and did not knowingly allow Millennium to exploit financial arbitrage opportunities in their funds at the expense of ordinary investors to whom they owe fiduciary duties.

7. Instead, Millennium and others acting in concert with it implemented and periodically refined an elaborate fraud designed to exploit not market inefficiencies or financial arbitrage opportunities, but loopholes in the methods employed by mutual funds and others to detect and prevent market timing activities. The fraud – known euphemistically as "flying under

the radar" – enabled Millennium to disguise itself and, therefore, transact billions in market timing volume that mutual funds or others would not have allowed had they known Millennium's true identity.

8. To carry out its deceptions, Millennium had the complicity of brokers and other intermediaries who processed mutual fund transactions and even enlisted the assistance of its own rank and file employees. In summary, Millennium's fraudulent market timing activities included:

(a) establishing more than one hundred subsidiaries or affiliates with names ostensibly unconnected to "Millennium" (the entities named as defendants in the caption) and using distinct tax identification numbers for such subsidiaries or affiliates to disguise Millennium's association with market timing transactions and evade detection by mutual funds and others who sought to monitor, restrict and/or prevent them;

(b) establishing – at thirty nine different brokerage firms or other clearing platforms – more than 1000 accounts between and among which market timing transactions were rotated and/or broken up to disguise Millennium's association with such transactions and evade detection by mutual funds and others who sought to monitor, restrict and/or prevent them;

(c) paying numerous registered investment advisory firms that are unaffiliated with Millennium to act as "fronts" by using accounts in their own names (sometimes referred to by Millennium as "blind" accounts) even though investment decisions with respect to transactions associated with the accounts were made entirely by Millennium traders in a scheme to disguise Millennium's association with market timing transactions and evade detection by mutual funds and others who sought to monitor, restrict and/or prevent them;

(d) concocting and executing a plan whereby twenty-five Millennium employees (including its top executives) acted as sham "annuitants" or "key persons" with respect to numerous variable annuity contracts and variable life insurance policies through which Millennium accessed hundreds of "sub-accounts" that were used to place market timing trades "below the radar screen" of mutual fund complexes and others who sought to monitor, restrict and/or prevent them; and

(e) creating at least twelve purported "family" trusts (also named as defendants in the caption) for use in connection with variable annuities to not only suppress Millennium's association with market timing activities, but create the false impression that no hedge fund at all was connected with the activities, in an effort to evade detection by mutual funds and others who sought to monitor, restrict and/or prevent them.

9. These schemes and others detailed herein were known to, approved or recklessly disregarded by Millennium's most senior management, including Izzy Englander – the firm's founder.

10. Englander knew mutual funds had the right to put a stop to Millennium's harmful timing activities and that many were actively seeking to do so. As phrased in an e-mail from a Millennium trader to Englander:

> **[T]here is language in every prospectus that gives carte blanche...to a fund house to accept/reject any trade if its deemed as a `market timing' trade.** Hence, on any given buy or sell day i get as much as 10-18% of my trades rejected....they got us by the [#*%&$].

(Emphasis added; expletive deleted) Feeney, Stone, Pillai and others also knew. But Millennium was not deterred.

11. One of many examples of senior management's active participation in Millennium's schemes appears in the following e-mail from Pillai, who at the time was new to the company, to Feeney:

> **At my old company, whenever we were kicked out of funds, we rotated into a different entity with a different Tax ID.** Is this feasible for me to do here? I spoke to Fred [Stone] and he suggested that I talk to you about this.

(Emphasis added) Millennium was already engaged in such practices; Feeney replied in an e-mail which was copied to Stone: "yes, we can do this...."

12. Englander was also aware of these schemes as reflected in the following e-mail from Pillai:

> Izzy,
>
> Since our discussion last month, I have stopped entering "same find multiple trades" in different accounts under the same tax ID and same broker. I am still, however, entering multiple trades under different tax ID's with the same broker (e.g. trading [a particular mutual fund] under different tax D's at [a particular broker]). I am also entering multiple trades under the same tax ID with different brokers (e.g. trading [a particular mutual fund] with two brokers under the [Millennium shell] entity [and defendant] Gilmore and Gillespie [LLC]). In all cases, I am trying not to have more than a total exposure of 0.50% of fund assets in any one fund. **Using different tax ID's and different broker rep numbers should shield us to some extent from fund crackdowns. If we cannot trade a given fund in more than one...tax ID [at a particular broker], for example, it would severely curtail the amount of capital we could deploy....**

(Emphasis added)

13. Millennium's current Chief Financial Officer was more explicit in an e-mail to other Millennium employees relating to the creation of a new Millennium shell company:

> This entity is being set up to **hide Millenniums [sic] name** when applying for fund accts.

(Emphasis added)

14. Another deception approved by Millennium's senior management was the use of multiple registered representative numbers by Millennium's timing brokers to get back into funds Millennium had been banned from trading. Typically, mutual fund representatives responsible for detecting timing activities did not know the identity of a broker by name, but only by an anonymous registered representative number assigned by the brokerage firm. Consequently,

mutual funds (or their agents) often restricted particular brokers from trading their funds by placing a "block" on their "rep" number. The circumvention of mutual fund "blocks" using multiple registered "rep" numbers was explained to Feeney by a Millennium employee in an e-mail:

> **In order to be able to re-enter funds that Kovan has been restricted from,** [Millennium's timing brokers] have obtained a new rep number by joining forces with another...broker....Initially, I will be opening one Gilmore & Gillespie account and, if the system works well, we will probably open more accounts.

(Emphasis added)

15. The lengths to which Millennium went to disguise its association with market timing even included the use of mailing addresses under false pretenses. Millennium rented at least two "post office" boxes from Mail Boxes, Etc. for use when opening new brokerage accounts. The mail drops were used in lieu of Millennium's Midtown Manhattan office address at 666 Fifth Avenue because Millennium knew mutual funds and others were tracking its market timing activities by street address. The deception was outlined by a Millennium employee in an e-mail to Feeney:

> [O]ne of [our trader's] accounts at [a particular clearing platform] was...flagged because of [market timing]. I **would like to open a new account using [defendant] Ikebana [LLC] with a non-666 address....**

(Emphasis added) Feeney's response: "ok-good idea[.]" Mail drops were used instead of Millennium's real business address to open accounts in connection with at least fifteen different Millennium shell entities. Englander, Stone and other Millennium employees also approved the use of their home addresses on account opening documents to throw mutual funds and others seeking to prevent timing activities off Millennium's trail.

16. On occasion, Millennium's traders ran across brokers who told them their deceptions could not be tolerated. For example, in an e-mail from a broker who had been asked by Pillai whether the broker could use multiple registered rep numbers to deceive mutual funds, the broker replied:

> I needed to drop you a line this morning concerning your potential account here....After checking with my home office regarding trading the international funds, and using various rep id's, I uncovered some items for you to know about. **The most important is that I will not be able to change rep id's as needed to "throw off' the fund families.** My compliance department has stated that they need to adhere to the mutual fund companies [sic] wishes.

(Emphasis added)

17. Such "red flags" were ignored. Millennium's traders and its senior management knew Millennium's deceptive activities carried risks to the firm, but they chose to suffer the potential consequences. E-mail exchanges between a Millennium trader and senior management typify Millennium's casual disregard for the prospectus and other limitations their schemes were designed to evade:

> [I] go into [this particular fund family's mutual funds] and leave them routinely. the amt changes all the time. the fact that [Feeney] gets a letter [from this fund family] is irrelevant to me[.] i **get scores of letters a week,** I **get kicked out of fistfuls of annuity companies by the week....I'm not being an ass, its [sic] just pointless to seize upon this letter to somehow judge the risk to the firm....you** can fwd this to [Feeney] if you like.

(Emphasis added) The e-mail was forwarded to Feeney who in turn copied Englander. Nevertheless, deceptive mutual fund timing at Millennium continued unabated.

18. Pillai and one other Millennium trader also engaged in illegal "late trading" – a market timing strategy that involves placing mutual fund orders for same-day pricing after the close of the financial markets, which usually occurs at 4:00 p.m. EST. It enables a market timer

to make trading decisions based on information released after the close that is not available to law abiding investors who must make their investment decisions prior to 4 p.m.

19. The nature of the advantage was succinctly set forth in a business plan prepared by D.C. Capital, L.L.C., the brokerage firm through which Millennium transacted the majority of its deceptive market timing and late trades:

> [We] allow[] the financial community to place their mutual fund transactions after 4:00 pm EST. The financial community has mostly been restricted from placing their trades after 4:00 pm EST. The majority of the industry requires trades to be placed before 4:00 pm EST. [We] allow[] clients to place their trades up to 5:00 pm EST and in some cases up to 5:15 pm EST. **This service is in high demand allowing the client to gather any information after all of the US markets have closed and still being able to receive the NAV [i.e., the mutual fund price] for that day. Earring's [sic] announcements and other news are released between 4:00 and 5:00 which play an important decision making process for the client.**

(Emphasis added)

20. The business plan itself was not provided to Millennium. But a Millennium trader who used D.C. Capital to clear substantial amounts of market timing transactions nevertheless got the message. The trader, Steven B. Markovitz, who has since been dismissed by Millennium, wrote in an e-mail to his trading assistants:

> dc capital also is a new acct....normal brokerage acct, with the advantage of, errr, shall we say, very late mkt trading.

21. In or about early 2002, Englander and Feeney became aware that Markovitz was actually engaged in late trading through D.C. Capital and another brokerage firm. Feeney was uncomfortable. He reviewed mutual fund prospectus provisions concerning the times orders could be placed, forwarded them to Stone and asked Stone for his input. Subsequently, Englander, Feeney and Stone concluded that mutual fund orders needed to be placed prior to the

close of the market to receive same-day pricing. As a result, sometime in early May 2002, Englander told Markovitz that he was not to engage in late trading.

22. Thereafter, on or about May 13, 2002, a timing broker and principal of D.C. Capital (the "D.C. Capital Timing Broker"), attended a meeting at Millennium's offices with Englander, Feeney, Markovitz and Stone. During the meeting, the D.C. Capital Timing Broker claimed that the SEC's "forward pricing rule," which governs how mutual funds are to compute share prices for mutual fund orders, applied only to mutual funds and brokers. Therefore, the D.C. Capital Timing Broker asserted, only D.C. Capital (not Millennium) was at risk if late trading was impermissible. The D.C. Capital Timing Broker further claimed that everyone, including large broker-dealers, was engaging in late trading.

23. In response, Stone stated that even if the forward pricing rule did not apply to Millennium, the representations concerning the times orders were being placed that appeared in clearing agreements between D.C. Capital or its clearing broker and the mutual funds would be false if Millennium were to late trade through D.C. Capital. Therefore, Stone explained to the D.C. Capital Timing Broker, Millennium could be guilty of aiding and abetting violations of the securities laws if D.C. Capital late traded on Millennium's behalf. After the meeting ended and following further discussion among Englander, Feeney and Stone, Englander again told Markovitz that he was not to engage in late trading.

24. Approximately one week after the meeting with the D.C. Capital Timing Broker, Markovitz wrote in an e-mail to Englander:

> in my opinion, forces are conspiring quickly and violently to end the timing game. Despite my intentions to keep it alive for as long as possible, the forces are more powerful than me.

> Nonetheless, everything i experience on a daily basis from brokers, clearing firms, annuity companies and fund companies is about timing....THAT **IS the game that will make headlines, nothing else.**
> **If we can stomach that headline risk, the late trade risk – as you pointed out –** is **a secondary, much more subtle risk.**
>
> **the later trading truly helps me in ways more than you know. To lose it is not good. I would rather not expedite the death of a game that is likely going to die anyway.**

(Emphasis added; ellipsis in original)

25. Despite Markovitz's expressed desire to keep the benefits of late trading, Millennium failed to put any procedures in place to monitor the times at which Markovitz was placing mutual fund trades or to otherwise enhance supervision. Given the lack of oversight, but without the knowledge of senior management, Markovitz continued to avail himself of late trading's advantages through July 2003 when the Attorney General's Office served a subpoena that asked whether Millennium engaged in late trading. At that time, Millennium discovered that while Markovitz had stopped late trading for a short period of time, he later resumed the practice in violation of Englander's instructions. Millennium cooperated with the Attorney General's investigation and in October 2003 Markovitz pleaded guilty to a Class E felony violation of the Martin Act.

26. Following the May 13, 2002 meeting with the D.C. Capital Timing Broker, Millennium also failed to inquire whether its other market timers were engaging in the allegedly widespread practice of late trading, let alone instruct them not to do it. Not surprisingly, Markovitz was not the only trader who exploited late trading's advantages. Pillai executed a late trading strategy in two mutual funds through a broker other than D.C. Capital from in or about November 2002 to January 2003. When Englander learned about Pillai's late trading in January

2003, Pillai was instructed to stop and he did so. In a telephone conversation with a Millennium investor after Markovitz's guilty plea became public, as reflected in the investor's notes, Englander admitted he was "likely guilty of failing to supervise" Millennium's traders.

27. In all, via its network of more than one hundred shell companies, on top of which was layered more than 1000 accounts, numerous registered investment adviser "front" companies and other layers of deception, Millennium was able to trade (or sometimes "late trade") in and out of more than one hundred mutual funds by executing more than 76,000 short-term "round trips" in a total transaction volume exceeding $52 billion.

28. The mutual funds that were traded using the most accounts were international funds and included the following:

International Fund	No. of Accounts Used To Trade This Fund	No. of "Round Trips"	Approximate Transaction Volume	Millennium's Approximate Profit
Fund A	459	1691	$ 1.9 billion	$13.7 million
Fund B	216	1470	$ 718 million	$ 6.9 million
Fund C	177	1045	$ 826 million	$ 6.3 million
Fund D	165	1032	$ 589 million	$ 4.9 million

There was no legitimate reason to trade these funds using more than a few accounts, let alone hundreds spread across multiple clearing platforms.

29. Similar schemes were executed through Millennium's use of variable annuities and variable life insurance policies. These insurance products are designed for ordinary long term investors to help them meet retirement and estate planning goals. The products provide death benefits like a traditional insurance policy, but allow an individual to contribute funds to an

account and then chose among various investment options that are essentially "clones" of retail mutual funds. Much like an individual retirement account or 401(k), the account grows in value on a tax-deferred basis and the participant withdraws the accumulated funds during retirement or, in the event of death, the funds are paid to heirs.

30. Millennium was not interested in tax-deferred investing, retirement planning or life insurance. It used these products as a way to market time mutual funds (or, more precisely, the mutual fund "clones" offered through these insurance products) using hundreds of "sub-accounts" that helped to conceal its identity. Pillai explained Millennium's use for these products in an e-mail to Feeney:

> The insurance company does not reveal [to the mutual fund] the account from which [an annuity] trade originates, so my trades would be disguised....

31. The reason why the trades were "disguised" is due to the way insurance companies (or their agents) routinely process transfers of annuity participants between and among investment choices in "cloned" mutual funds. Generally, annuity participants' trades, are netted together and then submitted in one large "batch" to the mutual fund. But, just in case "batch" processing did not provide sufficient camouflage, Millennium used its network of shell companies to add another concealing layer. For example, the Millennium employee who was responsible for dispensing new shell companies to Millennium's traders explained in an e-mail to Pillai which was copied to Feeney:

> I just spoke with [our broker].... We cannot use [defendant] Cottantail [Associates LLC], as you have another...annuity under that name [at the same insurance company]. I will be giving you [defendant] Saga Partners, LLC, to use as an additional entity. I will form new entities later in the month....

32. Millennium enjoyed considerable success using these techniques. Feeney, Stone,

Markovitz and Pillai, for example, were annuitants or insureds under more than one hundred separate annuity contracts or variable life insurance policies which gave Millennium access to numerous "sub-accounts" and thousands of "round trips" as follows:

Annuitant	No. Of Annuity Contracts or Policies	Round Trips	Approximate Transaction Volume	Millennium's Approximate Profit
Feeney	27	1357	$ 4.6 billion	$ 21.6 million
Stone	28	758	$ 960 million	$ 4.5 million
Markovitz	33	2561	$ 3.8 billion	$ 12.3 million
Pillai	26	939	$ 1.7 billion	$ 6.8 million

At least five of the annuity contracts for which Feeney and Stone acted as annuitants were owned by purported "family" trusts designed to create the false impression that the entities were not associated with a hedge fund and, therefore, would appear far less likely to be engaged in market timing activities. Englander himself was an annuitant with respect to one variable annuity contract. The contract was owned by defendant Kovan Family Annuity Trust, although neither Pillai, his family nor any family whatsoever had an interest in the trust or the annuity contract.

33. Less notable employees were also enlisted to assist in Millennium's schemes. For example, Millennium claimed that a 23-year old analyst earning $75,000 per year was a "key man" necessitating coverage under a $33 million variable life insurance policy. The policy carried an annual premium of $900,000, which was more than ten times this "key man's" salary. To satisfy the policy's "live body" requirement, the employee participated in a group physical, along with numerous other supposedly "key" Millennium employees. In fact, at least ten

Millennium employees (including a computer programmer, an assistant trader and various back-office personnel) with salaries averaging approximately $111,000 were covered under purported "key man" variable life policies bearing an aggregate face value in excess of $300 million. Englander, the only "key man" identified in Millennium's partnership agreements, was not among them.

34. In all, through the hundreds of sub-accounts Millennium accessed via sham transactions involving at least 248 annuity contracts and variable life insurance policies, Millennium was able to execute more than 10,000 short-term "round trips" in a total transaction volume exceeding $19 billion.

35. Millennium profited handsomely from its schemes. Its total profit from all mutual fund trading and variable annuity and variable life "sub-account" trading was in excess of $100 million, a substantial portion of which was attributable to schemes used by Millennium to hide or disguise its association with such transactions. Long term mutual fund shareholders and annuity and variable life participants suffered significantly; their investment interests were substantially diluted as a result of schemes used by Millennium to hide or disguise its association with market timing transactions. Other harm, including increased transaction and brokerage costs, was caused as well.

36. The Attorney General seeks recovery of the damage suffered by long term mutual fund shareholders and purchasers of annuity contracts and variable life policies as a result of these fraudulent activities, disgorgement of defendants' profits earned as a result of engaging in them, restitution, punitive damages and other relief.

PARTIES

37. Plaintiff is represented by Eliot Spitzer, Attorney General of the State of New York. Pursuant to Article 23-A of the General Business Law, the Attorney General oversees the offer, sale, issuance, promotion, advertisement, exchange, marketing, distribution and transfer of, or investment advice for, securities within and from the State of New York, and has authority to commence legal action when fraudulent activities have occurred or are about to occur. The Attorney General's principal office for oversight of the securities industry in New York State is located in New York County. Pursuant to sections 349 and 350-d of Article 22-A of the General Business Law, the Attorney General has the authority to obtain civil penalties for deceptive acts and practices in New York State. Pursuant to section 63(12) of the Executive Law, the Attorney General has the authority to obtain injunctive relief, restitution, and damages for repeated or persistent fraud in the conduct of business in or from New York State.

38. Defendant Millennium Partners, L.P. ("MLP") is an exempted limited partnership organized and existing under the laws of the Cayman Islands, with its principal United States offices at 666 Fifth Avenue in New York County.

39. Defendant Millennium USA, L.P. ("Millennium USA") is a limited partnership organized and existing under the laws of the State of Delaware with its principal offices at 666 Fifth Avenue in New York County. Millennium USA is a limited partner of MLP.

40. Defendant Millennium Global Estate, L.P. ("Millennium Global") is a limited partnership organized and existing under the laws of the State of Delaware with its principal offices at 666 Fifth Avenue in New York County. Millennium Global is a limited partner of MLP.

41. Defendant Millennium International, Ltd. ("Millennium International") is a Cayman Islands Exempted Company organized and existing under the laws of the Cayman Islands. Millennium International is a limited partner of MLP.

42. Defendant Millennium Management, L.L.C. is a limited liability company organized and existing under the laws of the State of Delaware, serves as a General Partner of Millennium USA and Millennium Global and is controlled and majority owned by Englander and other entities affiliated with him. The principal office of Millennium Management, L.L.C. is and/or was at all relevant times located in New York County.

43. Defendant Millennium International Management, L.L.C. is a limited liability company organized and existing under the laws of Delaware, serves as investment manager to Millennium International and is controlled and majority owned by Englander and other entities affiliated with him. The principal office of Millennium International Management, L.L.C. is and/or was at all relevant times located in New York County.

44. Defendant Millennium Holding Group, L.P. is a limited partnership organized and existing under the laws of the State of Delaware.

45. Defendant Millennium USA 1, L.P. is a limited partnership organized and existing under the laws of the State of Delaware.

46. Defendants Acorn Way LLC, A'DELIA Inc., Andres Pillai Family Trust, Angle View LLC, Anya Family, LLC, Anya Family Trust, Apulia LLC, Auric Ventures, LLC, Axiom Group LLC, Azinnia LLC, Baker Street LLC, Banta Way LLC, Bamabus and Co. LLC, Beantree LLC, Bishop Institutional Advisers LLC, Buka Group LLC, Caitlin Ventures LLC, Carroll Hinrichs & Co. LLC, Castlemark Ltd., Chiba LLC, Chiswick Family Annuity Trust,

Chiswick Park LLC, Cottontail Associates, LLC, Dagwood, LLC, Davis Family, LLC, Davis Family Annuity Trust, Derby Lane LLC, Duckpin LLC, Dyad Group LLC, East View LLC, Elbert LLC, Equatrion LLC, EXMOOR Ltd., FARALON LLC, Forest Green LLC, Fortnight LLC, Foxtail Ltd., Galin & McElroy LLC, Galloping Hill LLC, Geyser Group LLC, Gilmore and Gillespie LLC, Gu Family, LLC, Gu Family Annuity Trust, Haidar Family, LLC, Haidar Family Annuity Trust, Hawkbill LLC, Hook Drive LLC, Hobart Way LLC, Hudson View LLC, Hunterstone LLC, Ichyrus LLC, Ikebana LLC, Impala Road LLC, Jackson Drive LLC, Joliette LLC, Juneberry LLC, Jura LLC, KP Family, LLC, KP Family Annuity Trust, Klondike LLC, Knight Advisers LLC, KOMODO LLC, Kovan Family, LLC, Kovan Family Annuity Trust, Lamma Partners LLC, Lanckton LLC, Lemata LLC, Linkage Associates LLC, Manteca LLC, Mazzard Group LLC, Michael Present Inc., Millenco, LP, Modillion LLC, Napa Drive LLC, Natick LLC, Navasota LLC, Nekton LLC, NOEMI Ltd., Oak Lawn LLC, Optik Group LLC, Otter Ridge LLC, Osaykanyu LLC, Ozark Ventures LLC, Palomino Ventures LLC, Pelkey Family, LLC, Pelkey Family Annuity Trust, Periwinkle LLC, Petersen Family Trust, Plum Court LLC, Portwine LLC, Quadrillion LLC, Quail Ventures LLC, Quince & Co. LLC, Ravenscourt LLC, Redwing Group LLC, Richard Lewis Inc., Riverview LLC, Rizzoli Management LLC, Saga Partners, LLC, Scrimshaw Associates LLC, SM Family, LLC, SM Family Annuity Trust-I, S. Murray, LLC, S. Murray Annuity Trust, Smike & Co. LLC, Straight Drive LLC, Stone Castle Ltd., Taiga Group LLC, Tipton Associates, LLC, Tritium, LLC, Truman LLC, Tunica LLC, Umber Partners LLC, Umiak Way LLC, Valonia LLC, Variad LLC, Ventura Way LLC, Versine LLC, Warren Way LLC, Wheston LLC, Wiggins LLC, Wyatt Atwood & Co. LLC, Yaxis Group LLC, Yakima LLC, Zenith Court LLC, Zircon Ventures LLC and Zorgon LLC are and/or were at all relevant times, as applicable, limited liability companies formed under the laws of the State of Delaware, corporations formed under the laws of the State of Delaware (or, with respect to those entities with the designation "Ltd.," the laws of the Cayman Islands), or trusts formed under the laws of the State of New York, and either direct or indirect subsidiaries or affiliates of MLP, Millennium USA and/or Millennium International.

47. Defendant Israel A. Englander is the managing principal of Millennium and a resident of the State of New York.

48. Defendant Terence W. Feeney is a senior officer of Millennium and a resident of the State of New York.

49. Defendant Fred M. Stone is General Counsel of Millennium and a resident of the State of New Jersey. Stone is admitted to practice law in the State of New York.

50. Defendant Kovan K. Pillai is a Millennium employee and resident of the State of New York.

STATUTORY AND LEGAL FRAMEWORK

51. The Attorney General brings this action pursuant to his statutory and common law authority and under the following provisions of law.

52. Article 23-A of the General Business Law of the State of New York, commonly referred to as the "Martin Act," and the regulations issued pursuant thereto, regulate the offer and sale of securities within and from the State of New York and authorize the Attorney General to investigate the conduct of persons and entities engaged in, *inter alia,* the issuance, exchange, purchase, sale, promotion, negotiation, advertisement or distribution within or from the State of New York of any securities or the rendering of investment advice with respect

thereto.

53. The Martin Act proscribes fraudulent practices in connection with the sale of securities. Among the provisions relevant to this action are the following:

(a) General Business Law § 352(1), which prohibits fraud and fraudulent practices and provides, *inter alia,* that a violation of any section of Article 23-A of the General Business Law is a fraudulent practice and authorizes the Attorney General to investigate such practices;

(b) General Business Law § 352-c, which prohibits any person, partnership, or corporation from making any false representations, engaging in deception, fraud or false pretense, or concealing any material facts that the person knew, should have known, or made no reasonable effort to ascertain the truth; and

(c) General Business Law § 353, which authorizes the Attorney General to seek a permanent injunction enjoining any individual or entity who has taken part in, or has been concerned with, fraudulent practices from directly or indirectly engaging in the issue, sale, or offer of securities within or from the State of New York, and to seek restitution.

54. General Business Law § 349 declares unlawful any deceptive acts or practices in the conduct of any business, trade or commerce or in the furnishing of any service in the State of New York. Pursuant to General Business Law § 350-d, Plaintiff is entitled to a civil penalty of up to $500 for each of the defendants' violations of General Business Law § 349.

55. Section 63(12) of the Executive Law authorizes the Attorney General to seek an injunction barring repeated fraudulent and/or illegal conduct in the carrying on, conducting or transaction of business, and to seek restitution and damages.

56. Finally, as the State of New York's chief legal officer, the Attorney General brings this action pursuant to his *parens patriae* authority. Where, as here, the interests

and well-being of the people of the State of New York are implicated, the Attorney General possesses *parens patriae* authority to commence legal actions for violations of state law. The State of New York has a quasi-sovereign interest in upholding the rule of law, in protecting the economic well-being of its residents and, with specific reference to the present action, in ensuring that the marketplace for the trading of securities functions fairly with respect to all persons who participate or consider participating therein.

MARKET TIMING AND LATE TRADING

I. Market Timing And Deceptive Market Timing Techniques

57. "Market timing" is the short-term trading of mutual fund shares. Sophisticated financial entities known as hedge funds often engaged in "market timing" strategies. Typically, computerized trading "models" utilized by hedge funds signaled when to engage in frequent buys and sells of mutual funds.

58. These "models" were often complex and varied depending upon the strategy being utilized. For purposes of illustration, a simple strategy might work as follows. When a model indicated financial markets would rise in the short-term, the hedge fund would fully invest in equity mutual funds to capitalize on the expectation that the stocks comprising the mutual funds' portfolios would rise and, consequently, the share prices of the mutual funds would also rise. When the model subsequently indicated that financial markets would suffer a short-term decline, the expectation changed – a drop in the share price of the mutual funds was anticipated. On a downward signal, therefore, the hedge fund would sell its fully-invested position in equity mutual funds, capture a short-term profit and typically invest the proceeds in a virtually riskless position in a money market fund. While resting in the security of the money market fund, the

hedge fund would lie in wait for its next opportunity. When the model again predicted a short-term rise in financial markets, the hedge fund would sell its money market position and again buy equity mutual funds. When the model indicated the short-term upward rally was over, the hedge fund would sell its position in equity funds, again lock-in a profit and again return the proceeds to the safety of a money market fund.

59. These short-term exchanges of mutual fund shares – sometimes referred to as "round trips" – often occurred within a day, a few days or a few weeks of each other. Depending on the strategy, a hedge fund might engage in fifty or more "round trips" in less than a year allowing its money to rest safely in a money market fund most of the time. If a hedge fund "timed the market" right, therefore, it could dramatically reduce its stock market risk with little or no loss in upside potential.

60. A common strategy involved international time-zone differences. Rapid traders used international mutual funds to capture an "arbitrage" profit. A typical international strategy works as follows.

61. "Domestic" mutual funds invest primarily in stocks of U.S. companies trading primarily on markets within the United States. These markets usually close at 4 p.m. New York time. Domestic mutual funds calculate their NAVs as of the 4 p.m. New York time close of these U.S. markets. In other words, the stocks comprising the mutual fund's portfolio are usually actively traded up until 4 p.m. and, therefore, the stock prices are current as of the time at which mutual funds price fund shares.

62. By contrast, "international" mutual funds invest primarily in foreign stocks trading in financial markets outside the United States. Given time zone differences, these foreign

markets close much earlier than 4 p.m. New York time and do not reopen until the next day. Consequently, the last trade in the foreign stocks comprising the international mutual fund's portfolio may have been much earlier that morning at, for example, 4 a.m New York time. By 4 p.m. that afternoon (N.Y. time), the prices of the foreign stocks are twelve hours old; they are stale, not current like the prices of the domestic stocks. The arbitrage opportunity existed because even though prices were (in this example) twelve hours old, international mutual funds used those stale prices to calculate their NAVs.

63. As a result, while the foreign markets were closed during the U.S. trading day, market timers would watch what financial markets in the United States were doing. If U.S. markets were up significantly during the day and continued to stay up toward the 4 p.m New York time close of the markets, it was probable that when foreign markets opened later that day (e.g., at 9 p.m. that night (N.Y. time)), the foreign markets would follow suit. In a way, therefore, the international mutual fund was "mis-priced" because the rise in U.S. markets (and probable corollary rise in foreign markets) was not factored into the mutual fund's share price. To exploit this pricing inefficiency, the timer bet on the expectation that the prices of foreign stocks would rise the next day by buying international mutual funds. When U.S. markets subsequently dropped a day or a few days later, the timer would sell the mutual fund thereby capturing a short-term profit. Many timers would engage in a cycle of short-term mutual fund investing throughout the year.

64. While international equity mutual funds were most often targeted, many timers executed successful market timing strategies in domestic large and small capitalization equity funds, high yield bond funds and other types of mutual funds as well. Regardless of the strategy

being used, the key to success was the availability of "round trips."

65. Mutual funds are not designed or marketed as short-term trading vehicles. Rapid trading by market timers can injure long term shareholders in at least three ways.

66. First, rapid traders increase transaction costs for the mutual fund as a whole. Shareholders who constantly buy and sell cost the fund more money in processing trades than those who buy and hold for the long term.

67. Second, market timing allows frequent traders to profit at the expense of long term investors. This effect, known as "dilution," is illustrated by the following. When a timer buys into an equity fund, a mutual fund portfolio manager will, generally speaking, either invest the timer's money in stocks or hold the funds in cash. If the share price of the mutual fund rises a few days later, the timer will typically redeem his shares in the equity fund, lock in a profit and retreat to the safety of a money market fund. If the portfolio manager held the timer's money in cash during the timer's round trip, the mutual fund, in effect, simply gives the uninvested cash back to the timer, plus the timer receives a pro rata portion of the gain on the stocks in the mutual fund's portfolio. Allowing the timer to share in any portion of the increase in portfolio value is unfair because he contributed nothing to the gain. Since the timer's money remained in cash, the timer's "investment" was never put to work to earn a profit for all shareholders. To the contrary, the market timer darted into the equity fund at the last moment and clipped part of the upside that would otherwise have gone to buy and hold shareholders. When timers make many of these uninvested "round trips" in and out of the fund, they continually "pick off' pieces of long term shareholders' profit. This substantially waters down – or "dilutes" – investment returns.

68. The third form of damage can result regardless of whether a timer's money is

held in cash or invested by the mutual fund. In either instance, the mutual fund may incur unnecessary costs associated with having to buy and sell securities or otherwise raise cash to meet timer redemptions. In the situation where a timer's cash was not invested, in order to give the timer his piece of the increase in value of the portfolio's shares, the mutual fund may have to either draw down on a line of credit or sell stocks to raise the money. Both options result in costs to long term shareholders. Drawing on a line of credit causes the mutual fund to incur borrowing costs. When timers conduct numerous round trips, such costs can be substantial. Selling stocks can also cause substantial harm. A portfolio manager may have to sell stocks that were just purchased into a falling market. This not only jettisons the *long term* investment potential of the securities — the reason they were purchased in the first place — but causes the fund to incur otherwise unnecessary brokerage costs to sell the securities. These brokerage costs can also be substantial and are an utter waste because the securities were never given a meaningful opportunity to contribute to mutual fund returns. In addition, where the portfolio manager sells stocks that would have been held but for the timer's redemption, the fund may incur additional capital gains tax liabilities that are ultimately borne by long term shareholders. These same adverse consequences may result when a portfolio manager has invested a timer's cash in stocks only to have to convert securities back to cash a short time later to meet the timer's redemption.

69. Significantly, mutual funds have the legal tools necessary to prevent shareholders from engaging in frequent short-term "round trips." And given the harmful effects, as fiduciaries, mutual fund managers have obligations to affirmatively use these tools to put a stop to market timing activities.

70. Many fund prospectuses expressly state: (a) the mutual fund has the absolute

right to refuse to allow purchases of its shares (or exchanges between different funds in the same fund family) by any shareholder; (b) the mutual fund has a numerical limit on the trades a given shareholder can execute in a fund; and/or (c) the mutual fund does not allow harmful "market timing" activities. Similarly, many fund companies' internal policies contain restrictions on short-term trading.

71. Many mutual funds honored their fiduciary obligations. They vigilantly attempted to enforce restrictions on market timing in their funds.

72. Other mutual funds were "two-faced." On one hand, they breached their fiduciary duties by entering into agreements that expressly permitted shareholders to "time" the funds. Such arrangements — sometimes referred to as "capacity" agreements — often permitted the timer to exceed restrictions on short-term trading in the relevant prospectus and/or internal fund company policies. The mutual fund manager's reward for breaching its obligations was the fees generated by the timing assets in its funds. In addition, in exchange for the right to rapidly trade in certain funds, some timers made "static" investments in the same or a different fund within the same fund family (i.e., an investment that would not be rapidly traded) to induce mutual fund managers to breach their fiduciary obligations to long term shareholders. These so-called "sticky money" investments generated additional fees for fund managers. On the other hand, even "two-faced" mutual fund managers attempted to enforce anti-market timing rules with respect to timers with which they did not have an express "capacity" agreement.

A. <u>The "Timing Police"</u>

73. Both vigilant and "two-faced" mutual funds (or their agents) typically employed personnel to ferret out "timers" and put a stop to their harmful short-term trading activities in

mutual funds. Such employees were generally known as the "timing police." For a variety of reasons, however, identifying market timing transactions among thousands of legitimate transactions could prove challenging.

74. The multi-trillion dollar mutual fund industry processes thousands of buy, sell and exchange transactions everyday on behalf of a multitude of institutions and individuals. Some customers purchase and sell shares in direct transactions with the fund company. Other customers, such as retirement plans and their beneficiaries, typically clear transactions indirectly through a trust company or other intermediary. Still other customers, such as hedge funds, typically clear their mutual fund transactions indirectly through brokerage firms. In the indirect clearing scenarios, mutual funds often do not know the identity of their shareholders. In the system for processing mutual fund transactions, many times it is the broker or intermediary who has superior information.

75. The specific transaction information given to a mutual fund by a broker varies. By way of example, sometimes the mutual fund is provided an anonymous account at the brokerage firm represented by a series of account numbers, but not the shareholder's identity. The mutual fund may not be provided with the registered representative's name associated with an account, but rather only the identification number assigned to the "rep" by the brokerage firm. In such situations, some timing police attempt to track suspected market timing transactions by "rep" number and/or account number. Other mutual funds may be aware of the shareholder's identity by name, by tax identification number or sometimes both. In such "fully disclosed" situations, timing police can track suspected market timing trades by name and "tax id," as well as account number and "rep" number.

76. Timing cops are generally aware that many timers typically wanted to trade mutual funds in large dollar amounts to make the timing as profitable as possible. To reduce the burden of having to sift through an enormous amount of data, mutual funds often set minimum transaction thresholds to identify a suspected market timing transaction. If the dollar volume of a given trade falls below a certain level, the timing cops may not examine it to identify whether it was placed by a suspected timer. For example, the timing police might establish $300,000 as the transaction threshold. As a result, all trades that are above $300,000 and placed within a short period of time by the same registered representative or in the same account number might be investigated. If after further investigation a "timing" transaction was identified, it might be rejected and a so-called "stop" or "cease and desist" letter might be sent by the mutual fund to the broker. A typical stop letter said the following:

> We have noticed a pattern of excessive trading in these...accounts. As you know, mutual funds are intended to be long-term investments. Short-term trading hinders the portfolio manager's ability to adhere to the fund's investment strategy and may adversely affect performance....As stated in the prospectus, we reserve the right to restrict exchanges and share purchases that we do not feel are in the best interests of the funds or the majority of the shareholders....[W]e take this responsibility to our shareholders very seriously. Therefore, since your excessive trading could be detrimental to the fund, we have placed a stop purchase on your account and we have removed all of your exchange privileges....

B. "Flying Under The Radar"

77. Certain hedge funds and other market timers fraudulently evaded mutual fund-imposed and other restrictions designed to prevent market timing.

78. In situations where "capacity" agreements were not desirable or available, evading detection efforts by mutual funds was paramount to reaping the considerable profits to be made market timing funds. Consequently, an arrangement with a brokerage firm that was

willing to fraudulently manipulate its informational advantage over mutual funds to conceal, disguise and/or misrepresent the source of market timing activities was a coveted relationship. Over time, various pretenses were developed to hide or disguise market timing activities and thereby make them more difficult to detect and prevent. These schemes were known among market timers as "flying under the radar" of the mutual fund and brokers were paid handsome "wrap" fees for engaging in them – often as much as 1% to 2% of the dollar amount being timed.

79. One scheme is reminiscent of a "shell game" designed to deceive the timing police. After initially getting "caught" conducting market timing transactions in an account, the mutual fund would send the broker a "stop" letter. In an attempt to deliberately evade the trading restriction, the hedge fund and broker simply opened a new account, perhaps under a different "rep" number, and placed the market timing trades in the new account. If they got "caught" again, the broker would simply open a third account and so on. Alternatively, some timers would not wait for the timing cops to catch them and send a "stop" letter before opening a new account. Instead, in anticipation of the actions of the timing police, the timer would open perhaps five or ten accounts at the outset. Trades would be rotated between and among different accounts to "hide the ball." These practices were sometimes referred to among market timers as creating "also" accounts or "cloning." In both cases, the idea was to disguise the activities and trick the timing cops by creating the false impression that the harmful trading had stopped or was not occurring in the first place. Alternatively, the scheme was designed to create the false impression that the short-term trades were not being placed by the same shareholder. In this way, if the mutual fund prospectus and/or the fund company's anti-timing policy allowed a shareholder to conduct four exchanges per year, by using ten accounts instead of just one, the timer might be

able to get away with forty exchanges rather than the four the mutual fund intended to allot.

80. A related method of flying under the radar involved breaking the trades up into smaller dollar amounts to avoid detection by the timing police. The hedge fund (or the broker on the hedge fund's behalf) sometimes solicited corrupt "wholesalers" or other employees of the mutual fund's investment adviser to ascertain the dollar threshold at which timing police scrutinized suspected timing transactions. Alternatively, an experienced timer or timing broker could simply make an "educated guess" concerning the dollar threshold at which a given mutual fund would scrutinize suspected timing transactions. If, for example, the threshold was $1 million, rather than submit a single trade in the amount of $1 million on behalf of a hedge fund, the broker might submit five separate trades in the amount of $200,000 in the same account or different accounts to avoid detection by the timing police.

81. In instances where the shareholders' identity was "fully disclosed" to mutual funds by name and/or tax identification number, certain hedge funds would simply create multiple shell companies and give them different names that could not be readily connected by the timing cops or others who might question or disapprove of the timing transactions. To further the illusion that the trading was not emanating from a single shareholder, hedge funds obtained separate tax identification numbers for the shell companies even though there was no legitimate purpose or need for the separate corporate existence. The shell companies were often limited liability companies whose sole member was the "parent" hedge fund. The companies typically had no employees or operations independent from the "parent" hedge fluid and did not file a separate tax return. Instead, the "parent" hedge fund filed a single consolidated tax return on behalf of all the shell entities. The true purpose for having the separate corporate existence

was to perpetuate the charade with the mutual fund and evade detection by fund companies that treated (or would have treated if they knew the truth) all companies under the "parent" hedge fund's umbrella as a single shareholder for purposes of its market timing restrictions. The prospectus language in one fund company's prospectus is illustrative:

> Because excessive trading (including short-term, "market timing" trading) can hurt the Fund's performance, the Fund may refuse any exchange (1) from any shareholders account from which there have been two exchanges in the preceding three month period, or (2) where the exchanged shares equal in value the lesser of $1,000,000 or 1% of the Fund's net assets....Accounts **under common ownership or control, including those with the same taxpayer ID number..., will be considered one account for this purpose....**

(Emphasis added)

82. Another method of flying under the radar was to clear transactions through intermediaries other than broker-dealers. For example, some market timers cleared trades through trust companies that typically processed mutual fund transactions for employees participating in corporate retirement plans. The idea was to hide the hedge funds' trades among the mass of retiree trades being processed legitimately. Still others used the clearing platforms at large mutual fund "supermarkets" such as Charles Schwab & Co., Inc. and Fidelity Investments (or their affiliates). These "supermarkets" often process mutual fund transactions in "omnibus" format in the ordinary course of business. "Omnibus" processing often means that purchase and sale orders of thousands of "supermarket" customers are aggregated and submitted to the mutual fund on a net basis. Timers cleared through these "supermarkets" in an effort to have their market timing trades go undetected in the multitude of combined transactions.

C. Market Timing Through Variable
<u>Annuities And Variable Life Insurance Policies</u>

83. Another method of flying under the radar involved variable annuities and variable life insurance policies.

84. Variable annuities are hybrid securities intended for retirement. They combine elements of four different financial products: mutual funds, tax-deferred investments like Individual Retirement Accounts ("IRAs"), life insurance policies, and traditional annuities. After purchasing a variable annuity, a consumer (referred to as the "annuitant") can direct that his or her money be invested in one or more mutual fund "subaccounts" offered by the insurance company. These subaccounts minor the mutual funds available to retail investors and are usually run by the retail mutual fund manager. In other words, the fund manager invests the variable annuity subaccount assets in the same stocks or bonds as he or she does for the retail mutual fund. The subaccounts, therefore, are essentially "clones" of the retail mutual funds.

85. Variable annuities offer investors the chance to convert their investment, after a certain number of years, into a guaranteed stream of annuity payments for a period of years or for life. Prior to withdrawal, gains in the variable annuity subaccounts compound on a tax-deferred basis; no taxes need be paid until the monies are withdrawn by the annuitant. The typical variable annuity also has a death benefit guaranteeing the return of the investor's principal to heirs if death precedes the start of annuity payouts.

86. Variable life insurance policies are similar to variable annuities. An insured purchases a life insurance policy and pays premiums to the insurance company. In the event of death, the insured's beneficiaries will receive a death benefit. But, the death benefit is not

necessarily the face amount of the insurance policy. It could alternatively be, for example, twice the value of a "subaccount" that is invested by the insured. Like an annuitant, the insured can direct that his or her premium payments be invested in one or more mutual fund "clones" offered by the insurance company. The value of the "subaccount" grows on a tax-deferred basis and the variable life policy accrues a cash value. An insured can elect to terminate the policy prior to its maturity date in which case cash value in the subaccount is surrendered to the insured.

87. Hedge funds that purchased variable annuities and variable life insurance policies were not interested in tax-deferred investing, life insurance or a stream of annuity payments. They were interested in preying upon the cloned mutual fund sub-accounts that they likely would not have been permitted to trade if their transactions were conducted directly in the retail mutual fund. In some cases, hedge funds timed the "clones" of retail mutual funds in which they had already been restricted from trading.

88. Hedge funds also sought anonymity. Annuity investors make transfers or trades among the subaccounts by sending directions to the insurance company or its agent. Similiar to "omnibus" processing through a mutual fund "supermarket," transfers into and out of each subaccount are then aggregated by the company or its agent and forwarded to the mutual fund manager as "batch trades." As a result, the mutual fund manager generally is not aware of the identity of the shareholders whose trades are grouped together in a single batch.

II. Late Trading

89. The price at which an investor can buy or sell a stock listed on an exchange or traded in the over-the-counter market fluctuates during the trading day. By contrast, prices of mutual fund shares are set once a day, after the market is closed.

90. The price at which shares of a mutual fund are bought and sold is referred to as the net asset value or "NAV." Many mutual funds' NAVs are calculated as of the closing time of the New York Stock Exchange, which is usually 4:00 p.m. New York time. Orders to buy, sell or exchange mutual fund shares placed with those mutual funds, or a broker-dealer or other intermediary at or before the closing time are priced at that day's NAV.

91. "Late trading" refers to a market timer placing – and a mutual fund, broker-dealer or other intermediary accepting – orders after the mutual fund's deadline and yet still receiving same-day pricing. Corporate earnings announcements, significant press releases and other events affecting the financial markets often occur after 4:00 p.m. Such material information can be predictive of the probable direction of - or determinative of actual – mutual fund share prices and, therefore, can play an important role in the market timer's decision-making process on whether to purchase or sell a mutual fund and/or engage in related "hedging" transactions. And such post-4:00 p.m. information is not available to law abiding investors who must place their mutual fund orders prior to the mutual fund's deadline to receive that day's price.

92. Late trading occurred primarily because broker-dealers and other intermediaries fraudulently manipulated the industry-wide system for processing mutual fund transactions. Unlike the near instantaneous transmission of stock orders for execution, broker-dealers and other intermediaries could (and often did) transmit mutual fund orders to fund companies for execution after 4:00 p.m. Fund companies (or their agents) then tally the orders and calculate the NAV *as of* the 4:00 p.m. close of the market. This calculation often did not occur until 5:30 p.m. or later. To prevent "late trading," fund companies would generally require that the broker-

dealer or other intermediary make an express or implied representation to the mutual fund that the order being transmitted was placed by the mutual fund shareholder at or before the close of the market and, therefore, was entitled to that day's pricing.

93. To earn substantial fees, certain broker-dealers and other intermediaries abused this system. They gave hedge funds the ability to place orders after 4:00 p.m. (including, in some cases, to place orders after the time at which NAVs were actually *calculated)* by transmitting those orders with legitimate orders to be processed using that day's price. In so doing, these broker-dealers and other intermediaries breached their representations to mutual funds and engaged in false pretenses in connection with the sale of securities under the Martin Act.

THE FRAUDULENT PRACTICES OF THE DEFENDANTS

I. The **Millennium Hedge Fund Complex**

94. MLP was formed in 1989 by Izzy Englander. MLP bills itself as an "alternative investment fund" that engages in multi-strategy proprietary trading through a "master feeder" structure – an arrangement whereby investors' money is initially placed into smaller sub-funds and then pooled into one large fund. MLP, therefore, has two so-called "feeder" funds. They are Millennium USA, which is used to receive investments made by Millennium's domestic investors, and Millennium International, which is used for investments made by international investors. Millennium USA and Millennium International then in turn invest substantially all their assets in MLP. A third fund, Millennium Global, is used for special investments of "separate accounts" and "general accounts" by insurance companies. Millennium Global also invests a portion of its assets in MLP.

95. Investments in MLP are offered privately; they are not open to the public at

large and, in any event, are well beyond the means of ordinary investors such as those who purchase mutual funds and variable annuities for savings and retirement. The minimum investment in MLP is $5 million.

96. In Wall Street parlance, MLP and its various affiliates are known as a "hedge fund." Institutions and wealthy individuals invest in Millennium and, in exchange for a fee, various entities controlled by Englander make investment decisions for investors and otherwise manage their assets. The fee is roughly calculated as 20% of investors' gains. Thus, the greater the return earned by investors, the more earned by the entities controlled by Englander.

97. The investment advisers to MLP, Millennium USA, Millennium International and Millennium Global are defendants Millennium Management, L.L.C. and Millennium International Management, L.L.C. These advisers are ultimately controlled and majority owned by Englander and other entities affiliated with him.

A. <u>Millennium's Management Structure</u>

98. Izzy Englander sits atop Millennium's corporate organizational chart. To deploy the more than $5 billion Millennium has under management (which, after the effects of leverage, gives Millennium access to approximately $20 billion in trading capital), Englander orchestrates the activities of more than one hundred traders executing various investment strategies. All Millennium traders and all other personnel ultimately report to Englander; he is also Millennium's largest investor. As of December 31, 2004, Englander and his family members beneficially owned more than 14% of Millennium; more than one hundred Millennium employees owned an additional 4% of Millennium.

99. Terence W. Feeney is a Millennium Vice Chairman and its Chief Operating

Officer. Feeney also has a significant investment in Millennium. The head of Millennium's Operations department (the "Head of Operations"), among others, reported to Feeney. The Operations area had a separate unit consisting of several employees that supported the market timing activities of Millennium's traders. This unit was referred to by certain Millennium employees as market timing operations and its supervisor was a junior employee who reported indirectly to Feeney (the "head of market timing operations").

100. Fred M. Stone is Millennium's General Counsel. During the relevant time, he was responsible for legal and compliance matters. His responsibilities initially included the creation of new legal entities and then later supervision of others who created new legal entities. Stone reported to Feeney during the relevant time period. Millennium also employed during the relevant time a compliance officer – referred to by Millennium as the "Compliance Coordinator" – who reported to Stone. The Compliance Coordinator, who worked as an assistant to Stone with a previous employer, had no college degree, securities licenses or professional certifications. The Compliance Coordinator did, however, have a paralegal's certificate and attended one-day legal and securities industry conferences from time to time.

101. Among the ranks of Millennium traders during the relevant time was Steven B. Markovitz who executed a mutual fund market timing strategy. At certain points in time, Markovitz managed more of Millennium's assets than any other Millennium trader – market timer or otherwise.

102. Millennium employed four other traders who were engaged in mutual fund market timing strategies. One of them was Kovan Pillai. Relative to Markovitz, Pillai had a smaller, but still substantial, percentage of Millennium's assets under management.

103. Millennium also engaged outside investment advisers who were not Millennium employees to manage assets for Millennium. During the relevant time, Millennium engaged at least three such outside advisers who had investment discretion over Millennium's money and engaged primarily or exclusively in mutual fund market timing strategies. Separately, Millennium made investments in other hedge fund complexes that engaged in market timing strategies.

104. Although they executed the same or similar strategies, Markovitz, Pillai and Millennium's outside advisers did not coordinate their activities. To the contrary, they were quite secretive and proprietary about their strategies as were all traders at Millennium. Only upper management at Millennium was privy to the specifics of the various strategies Millennium's inside and outside traders were executing.

B. Millennium's Investment Objective

105. Identifying and exploiting financial arbitrage opportunities is a legitimate objective pursued and achieved by many hedge funds. Millennium shared this goal. Its offering documents state:

> Millennium's objective is **to exploit market inefficiencies and to profit by financial arbitrage,** in order to achieve consistent overall returns uncorrelated with stocks, bonds and other traditional investments.

(Emphasis added)

106. In pursuit of its objective, Millennium deployed the billions it had under management in several different strategies including fixed income arbitrage, statistical arbitrage, merger arbitrage, futures arbitrage and, most relevantly, market timing of mutual funds.

107. Englander and his top executives manage risk and make the decisions

concerning how much capital to devote to which strategy and then to which of the several traders executing that strategy. In connection with these decisions, traders update Englander and top management on their strategies and exposure to various so-called "asset classes" (e.g., technology stocks, whether owned directly, indirectly through mutual funds, or derivatively through more exotic financial instruments). Englander and top management adjust Millennium's exposure according to, among other factors, Millennium's appetite for risk relative to the potential reward to be gained.

108. At times, Englander allotted more capital to Millennium's market timing strategies through Markovitz, Pillai and other internal and external managers than to any other strategy. This allocation was lucrative for Millennium's investors. Mutual fund market timing accounted for as much as 20% of Millennium's yearly investment returns. These returns were substantial especially given the limited risk inherent in a market timing strategy. Unlike ordinary mutual fund investors who buy and hold for the long term and are, therefore, continuously subject to downside risk, Millennium's capital was at risk of loss only a fraction of that time because its assets often rested safely in virtually riskless money market or short-term bond funds. In addition, even when Millennium was "long" mutual funds, the position was often partially or fully "hedged" through the use of derivatives or other financial products to further protect against potential losses. Such risk-adjusted returns helped Millennium earn a reputation as one of the more savvy hedge fund managers on Wall Street.

109. But, Millennium did not achieve all or even a substantial part of its mutual fund market timing investment returns by simply "exploiting market inefficiencies." Many mutual fund complexes would not and did not knowingly allow Millennium to exploit financial arbitrage

opportunities in their funds at the expense of ordinary investors to whom the fund managers owed fiduciary duties.

110. Instead, Millennium and others acting in concert with it implemented and periodically refined an elaborate fraud designed to exploit not market inefficiencies, but loopholes in the methods employed by mutual funds and others to detect and prevent market timing activities. The fraud enabled Millennium to disguise itself and, therefore, transact billions in market timing volume that mutual funds or others would not have allowed had they known Millennium's true identity.

111. The first layer of Millennium's deception was an illegitimate web of more than one hundred limited liability companies, purported "family" trusts and other entities that was designed and existed solely for the purpose of deceiving mutual funds and others who sought to prevent market timing.

112. Millennium created a second layer of camouflage to further disguise its identity. The elaborate web of shell companies was used to open hundreds and hundreds of accounts at numerous broker-dealers and other clearing platforms. Sometimes Millennium hired and paid substantial fees to other investment advisers to act as "fronts" with respect to certain accounts. The investment advisers had no investment discretion over Millennium's money, did not render any investment advice to Millennium or otherwise provide any real services. Investment decisions with respect to transactions associated with these accounts were made entirely by Millennium traders. The investment advisers simply used accounts in their own names to disguise Millennium's association with the transactions and throw the timing police or others seeking to prevent market timing off Millennium's trail.

113. A third layer was added when Millennium employees pretended they were "annuitants" and "key persons" with long term retirement or estate planning objectives in order to secure access to variable annuities and variable life insurance policies. Through such false pretenses (and sometimes with the complicity of insurance companies), Millennium successfully shielded itself from fund managers and others seeking to prevent the siphoning of profits that rightfully belonged to bona fide long term annuity participants and owners of variable life policies.

114. Each layer of deception was understood, approved or recklessly disregarded by Millennium's most senior management.

115. An integral part of Millennium's deceptions were carried out by a small Long Island brokerage firm known as D.C. Capital, L.L.C. Englander introduced Markovitz to D.C. Capital which ultimately conducted billions worth of deceptive market timing transactions through approximately one hundred D.C. Capital accounts. Markovitz also engaged in "late trading" of mutual fund shares on behalf of Millennium through D.C. Capital (and two other broker-dealers) during the period between in or about early 2002 through in or about July 2003. In October 2003, Markovitz pleaded guilty to a felony violation of the Martin Act.

II. **Deceptive Market Timing** At **Millennium**

116. Mutual fund market timing at Millennium began at least as early as 1999, when Markovitz was first hired. Englander had been introduced to Markovitz through a mutual acquaintance. During a job interview, Markovitz showed Englander the results of a market timing strategy Markovitz had developed and traded using his own money. The strategy was based on international time zone arbitrage using international mutual funds.

117. While Markovitz had not invented this strategy, his results using it were impressive; investment returns of approximately 30% to 40%. Englander hired him and thereafter Markovitz began market timing with Millennium's money. Other Millennium internal and external traders began (or were already) market timing as well.

118. Over time, it became increasingly difficult for Millennium's traders (or others acting on Millennium's behalf) to find fund companies that would knowingly permit market timing in their funds, particularly international funds. Many fund companies understood how timers were exploiting pricing inefficiencies to the detriment of their long term shareholders. Consequently, whereas once they may have tolerated it, many fund companies began to crack down and disallow market timing transactions, as it was their right and obligation as fiduciaries to do.

119. On the other hand, as the supply of "timeable" funds began to shrink, mutual fund timers were willing to pay more for the ability to time a mutual fund. For their own gain, some hind companies disregarded their fiduciary obligations and knowingly permitted market timing transactions with certain timers even though the transactions harmed long term shareholders. One way such fund companies were compensated was "sticky money."

120. "Sticky money" generally refers to a deal negotiated directly with a mutual fund whereby a static investment is made in exchange for the right to trade rapidly. The mutual fund's investment adviser typically earns substantial fees on such "sticky" investments.

121. Pillai discussed "sticky" money in a February 2003 e-mail to Englander:

> Izzy,
>
> In funds, we have 280 M deployed in international and 40 M deployed as

> domestic sticky money....[I]n addition to the above, we have 30 M in sticky money market money that [Feeney] set up via [one of our timing brokers]. This bought us 15 M in negotiated international capacity....We are still looking for cheaper negotiated deals directly with the fund companies.

122. For a timer like Millennium, tying up capital in "sticky asset" investments was not an efficient use of capital. Indeed, Markovitz characterized such investments as "bribes." In a January 2, 2003 e-mail to Englander relating to a proposed timing strategy in municipal bond funds, Markovitz wrote:

> [I] need capital. lots of it. good news about this strategy: a) very few timers already [into it; and] b) fairly efficient use of capital in that **you don't have to post bribe money to play these funds, mainly becuase (sic] no one is watching the gate.**

(Emphasis added)

A. <u>"Watching The Gate"</u>

123. At most mutual fund complexes, there were people "watching the gate" – the timing police. Millennium's market timers and its senior management knew this full well. They knew market timing potentially could be harmful to, and/or actually was harming, long term mutual fund shareholders. They knew mutual funds had the legal right to stop market timing in their mutual funds and that market timers (including Millennium) were frequently "kicked out" of mutual funds. For example, a "stop" letter sent to Millennium by a broker in or about February 2001 stated:

> **Short-term trading can negatively impact long-term fund shareholders by increasing fund trading costs, increasing volatility, and decreasing fund returns.** If you prefer short-term trading, you may wish to consider alternative investment vehicles, such as exchange-traded funds (closed-end funds), or those made available through other entities.

(Emphasis added)

124. Instead of looking for another arbitrage opportunity where it could legally exploit pricing inefficiencies, Millennium chose to accomplish its otherwise legal market timing strategy by disguising itself from the timing police.

B. Millennium Studied Market Timing Detection Methods

125. Millennium worked hard to deceive mutual funds. Its employees studied the methods of timing police and others responsible for detecting mutual fund timing activities. Millennium's traders sought out unscrupulous timing brokers and dishonest employees of mutual fund investment advisers and insurance company employees to help them. For example, as phrased by a timing broker in an e-mail to Markovitz:

> We've been doing our research and **I'm going to swoop under the radar screen like a stealth bomber.** By the time they figure out what has happened we will be 30 million long. Been talking with the wholesalers[;] some are full of [*&%#] but others have given me their **blueprint** of how to get these accounts opened and traded **without crossing the higher ups desk.**

(Emphasis added; expletive deleted)

126. Another example appears in an e-mail dated April 26, 2002 from a timing broker to one of Markovitz's trading assistants:

> The purchases were busted - I think they have a very good radar system and the [international fund] we purchased is a very small fund (only $18 Million). The **Wholesaler is coming in next week to meet with us. He may have a way to be able to purchase under the radar....**

(Emphasis added)

127. Other Millennium internal market timers examined whether timing police had the ability to track Millennium's trading activity in its funds even when it was done through different brokers. A junior trader wrote in a series of e-mails in mid-April 2003:

> One open question is whether the fund families have the ability to track the same investor (e.g., by tax ID) at different brokers. That seems unlikely, but it is an important thing to look into, since it could change our trading behavior.
>
> * * *
>
> Regarding the question of whether fund families have the available data to aggregate between different brokers, I have heard different things from different brokers. I have definitely heard that fund families find out more than simply the account number of a given fund holder. I **have been told from various people that changing the name, changing the address, changing the name slightly, or changing the entity itself is the best strategy for reopening an account without restrictions.** It is unclear, although unlikely, that fund families can aggregate between brokers, but worth looking into.

(Emphasis added) Millennium found it worth "looking into" these methods of detection and others.

128. When the timing police caught on, as sometimes happened, Millennium's Compliance Coordinator and employees in the Operations and market timing operations departments assisted Millennium traders in a team effort to deceive the mutual funds.

129. For example, defendant Carroll Hinrichs & Co. LLC was a new entity Millennium created so a mutual fund trader could time under the radar. A brand new account was established in the name of this new entity at a particular clearing platform. Therefore, no Millennium trader had previously used the new entity or the new account.

130. Nevertheless, the Millennium trader was not able to fly quite low enough below the radar screen. A particularly alert mutual fund (or clearing platform on the mutual fund's behalf) apparently caught on to Millennium's deception by noticing that the new "LLC" shared the same tax identification number as other shell entities Millennium created for use by other Millennium timers.

131. The Millennium trader was puzzled by the mutual fund's quick determination

that he was a mutual fund timer notwithstanding the use of a new entity and account. In an August 2001 e-mail to the Head of Operations and the head of market timing operations, the Millennium trader wrote:

> I was trying to figure out why [a particular mutual fund] inquired about my holding period intentions on the...purchase that they rejected....As this is a brand new trading account and new entity, I was surprised they would call before taking the trade - almost seemed like they suspected I was guilty of being a market timer before even talking to us....[T]his brand new account has no history...As this is **a brand new account the only way this could happen is if [the mutual fund] checks both account id's and taxpayer-identification numbers for trades submitted to them....I think [the Compliance Coordinator] mentioned that there are several** other **accounts** with the same **taxpayer id** as the **[account in** the **name of defendant] Carroll, Hinrichs** & Co....

(Emphasis added)

132. The Head of Operations was confused as to why the brand new shell entity and account did not provide sufficient cover and replied: "[The] Carroll Hinrichs & Co. account was a **copy** set up for you, no one else has traded it." (Emphasis added)

133. The Compliance Coordinator subsequently educated the Head of Operations and coordinated a solution:

> [A particular Millennium trader] is using [defendant] Carroll Hinrichs [& Co. LLC] and Kovan [Pillai] is using [defendants] Gilmore & Gillepsie [LLC] and Gahn & McElroy [LLC]. [The clearing platform] seems to track by tax id number and has been mixing the two of them up (this has not been such a good thing for either, especially [the particular Millennium trader]). I have applied for a new tax id number for Gahn & McElroy, and will be receiving new tax id numbers for the two new entities we will be using for [the particular Millennium trader], [defendants] Zircon [Ventures LLC] and Scrimshaw [Associates LLC]. I think this may lighten up, or even solve, the problem.

134. Englander was well aware that Millennium was deceiving mutual funds. For example, Pillai wrote in an e-mail to Englander dated December 5, 2001:

> I have delayed getting back to you on this project because the broker I was working with was not happy with doing $5M in a single fund straight away - he would have been happy to start with about $1M and build up to $5M. The **wholesaler he works with insists that that is the way to stay under the radar....**

(Emphasis added)

135. Other examples of Englander's knowledge of deceptive practices include the following e-mails from Pillai:

- 6/15/01 e-mail to Englander: "[A timing broker] also has contacts that would enable me to trade through Schwab via an intermediary, so there would be little chance of getting kicked out."

- 10/31/01 e-mail to Englander: "I have a list of 35 `good' small-cap funds. One example of these is [a particular ticker symbol]. The asset size is 712M, so we could probably trade 2M or so and still stay below the radar."

- 7/30/02 e-mail to Feeney and forwarded to Englander: "[A timing broker] claims that none of the mutual fiend timers has ever been kicked out of this new platform [Millennium is considering]....He claims also that this would be a truly omnibus account."

C. Millennium's Program Of Deception

136. Companies often have confusing corporate structures filled with numerous entities. Such structures are adopted for legitimate reasons such as to comply with federal securities laws, segregate assets in the event of bankruptcy, limit liability to a particular class of shareholders or to protect confidential trading strategies from would-be copycats.

137. Millennium's confusing web of more than one hundred shell companies was not created to implement its "feeder" structure, to segregate the assets of international investors from domestic investors, to execute different investment strategies in different entities or even to legitimately protect its confidential trading strategies. It existed for no purpose other than to

disguise Millennium's identity and fool mutual funds and others that sought to (or would have sought to if they knew the truth) put a stop to Millennium's harmful market timing activities.

138. The vast majority of Millennium's shell entities were limited liability companies the sole members of which were a Millennium "parent" hedge fund. The shell entities had no employees or operations independent from the "parent" hedge fund and did not file a separate tax return. Instead, the "parent" hedge fund filed a single consolidated tax return on behalf of all the shell entities. Millennium also obtained separate tax identification numbers for most or all of the shell entities to thwart timing cops that may have tracked market timing transactions by tax identification number. There was no legitimate need for these separate corporate existences since there were no employees or operations independent from the Millennium "parents."

139. Millennium had a set procedure for creating new entities. When a Millennium market timer needed a new entity, Millennium's Compliance Coordinator coordinated their requests. The Compliance Coordinator would typically receive the request by e-mail and seek the approval of either Feeney or Stone (or both) for the creation of the new entity. The Compliance Coordinator also created new entities that were placed "on the shelf for future use."

140. One e-mail request to the Compliance Coordinator dated October 28, 2002 from an outside Millennium timer makes clear one purpose for new entity creation:

> We would like to open 8 accounts (each) at [two different clearing brokers] through [a particular firm] as the introducing broker. These accounts will replace the lost...capacity [at another broker] (approx. 12 mm). I am waiting to find out if the tax id information will be fully disclosed to the fund families, or if they will only see the rep numbers. **If the tax id's are fully disclosed...then we will need to set up a few new entities to hide the activity at [one of the clearing brokers].**

(Emphasis added) The Compliance Coordinator forwarded the e-mail to Feeney seeking approval. Feeney's response: "ok."

141. Millennium's Chief Financial Officer, who reported to Feeney, also understood the purpose behind creating new entities. In a January 2002 e-mail relating to the creation of a new Millennium entity, Millennium's CFO wrote:

> This entity is being set up **to hide Millenniums [sic] name** when applying for fund accts.

(Emphasis added)

142. The Compliance Coordinator also had responsibility for coordinating the paperwork involved in forming a new limited liability company or other entity and for applying to the Internal Revenue Service for a new tax identification number; many of the tax id applications were signed by Englander. The job of selecting a name for the new company fell upon different Millennium employees at different times. Sometimes it was a collaborative effort.

143. At first, Stone chose the names for new entities that were created for the purpose of "flying under the radar." Entities without the word "Millennium" in their names were selected to reduce the chances that mutual funds or others responsible for identifying and preventing market timing would link the newly-created entity with Millennium. Stone conceived the idea of stringing together the names of various Millennium employees to avoid name association with Millennium. Thus, shell entities were given such names as Carroll Hinrichs & Co. LLC, Galin & McElroy LLC, Gilmore and Gillespie, LLC and Wyatt Atwood & Co. LLC.

144. Later, the Compliance Coordinator had primary responsibility for selecting entity names. The Compliance Coordinator typically chose entity names in more mundane ways than Stone, such as randomly from a dictionary. Other more suggestive names were sometimes

chosen by the Compliance Coordinator, however, such as "Superfluous Ventures LLC" (which was never used because it was frivolous).

145. Millennium then obtained tax identification numbers separate from each shell company's "parent" entity to throw off the trail those mutual funds or others that may have been tracking market timing transactions by tax number.

146. The necessity for new shell entities with separate tax identification numbers was explained succinctly to Feeney in an e-mail from an internal Millennium market timer. The e-mail dated October 10, 2001 was entitled "Carroll, Hinrichs & Co. trading account tax id problem" and explained:

> I've just opened my 4th trading account and I believe you said that I could have one more account initially, ie 5 in all. I wanted to ask if in addition I could have a replacement for the above account. The Carroll, Hinrichs account at [a particular broker], as you might know, was the first account I opened but unfortunately it shares the same tax identifier number with one or two other entities used for mutual fund timing by other people I believe. Anyway, I have had three rejections of buy trades for international funds and they have all been attempted first time purchases associated with this account, presumably because the fund companies have tracked trades by the other entities with the same tax id. I haven't had any rejections in my other accounts (with unique tax ids) so far and so I'm pretty sure the problem is with the shared tax id. As a result, I am not really able to effectively use this account for international trades. Hope this makes sense. Thanks for any help.

Feeney's reply: "bk."

147. The deceptions were also concisely outlined for Englander. For example, in a June 3, 2002 e-mail from Pillai to Englander, Pillai wrote:

> Izzy,
>
> Since our discussion last month, I have stopped entering "same fund multiple trades" in different accounts under the same tax ID and same broker. I am still, however, entering multiple trades under different tax ID's with the same broker

> (e.g. trading [a particular mutual fund] under different tax ID's at [a particular broker]). I am also entering multiple trades under the same tax ID with different brokers (e.g. trading [a particular mutual fund] with two brokers under the [Millennium] entity Gilmore and Gillespie [LLC]). In all cases, I am trying not to have more than a total exposure of 0.50% of fund assets in any one fund. **Using different tax ID's and different broker rep numbers should shield us to some extent from fund crackdowns. If we cannot trade a given fund in more than one ...tax ID, for example, it would severely curtail the amount of capital we could deploy....**

(Emphasis added)

148. Senior management's oversight of activities designed to deceive mutual funds was not limited to occasional e-mails. The Compliance Coordinator and an assistant maintained a "Mutual Fund Status Chart" that was circulated periodically to Feeney, the Head of Operations and the head of market timing operations. The charts detailed the number of accounts that had been created or were in the process of being created for each Millennium trader (both internal and external) for the purpose of "flying under the radar." With respect to one such chart dated in May, 2003, Feeney remarked to Englander:

> i need to talk to kovan-he has 77 acts in the pipeline-i think he is just churning and burning these accts and it does effect other people [i.e., Millennium's other market timers.]

Englander's suggestion in reply was:

> can't he set up in his own company (companies that other guys don't use) so that it doesn't effect anyone else?

149. Feeney pointed out that Englander's suggestion may not work because even a new shell entity would have the same signatories (e.g., Englander's and Feeney's signatures) that could be linked together if timing police or others were tracking timers by authorized signatories. Feeney replied: "he is, but there are common items—eg–who can move $$ signatures[.]"

150. Englander had apparently forgotten; earlier he had received an e-mail stating that Schwab or the fund companies pierced the complex veil of Millennium shell companies and made the association between Millennium and some of the shell companies by identifying Englander and Feeney as signatories. In an e-mail dated February 28, 2002 that was forwarded to Englander, Feeney and Stone, Markovitz informed the Compliance Coordinator:

> [I] am on the brink of losing 60m Intl across all my schwab accts. [T]hey **made the link via the signing authorities across the accts, that is [Millennium's CFO], Feeney and Englander.**

(Emphasis added)

151. Millennium's senior management approved a counter to this method of market timing detection as well.

152. By January 2003, Millennium already had accounts at Schwab in the names of at least fifteen different entities, some or all of which had separate tax id numbers. Numerous fund companies had requested that timing activity stop. Since timing cops or others had caught on to some of Millennium's tricks by identifying common signatures, Millennium's Compliance Coordinator coordinated a solution.

153. In an e-mail dated January 23, 2003 to Feeney and copied to the Head of Operations, the head of market timing operations, and Markovitz, the Compliance Coordinator sought approval to stay one step ahead of the timing cops:

> Three of Steve's Schwab accounts [opened] through [a broker] got flagged yesterday because they linked Izzy's name to all three accounts. **Upon your approval, we will be testing the Schwab waters by opening a new account through [the broker] using a clean entity ([defendant] Caitlin Ventures [LLC]).** I **would** like to use [the names of Millennium's Vice **Chairman and CFO] as authorized persons in an attempt to keep your and Izzy's name off the radar screen.** We can always add additional signatories later, if need be. I

will **also be using a different mail address.** Pls let me know if ok to proceed.

(Emphasis added) Feeney's response: "ok."

154. In addition to the use of multiple entities, separate tax id numbers and additional signatories, Millennium changed the address of some entities to throw the timing police or others off its trail.

155. Millennium's headquarters are located at 666 Fifth Avenue, a large office building in Midtown Manhattan. During the relevant time, the building had the ability to receive postal deliveries and Millennium, in fact, received mail at this address and continues to receive mail at this address. Nevertheless, to further disguise itself as the source of market timing activities, Millennium obtained at least two mail drops at Mail Boxes Etc. locations in the Midtown area in an attempt to thwart the efforts of mutual funds or others seeking to detect and prevent timing activities. These addresses were used on account opening documents in the names of different entities to reduce the chances that timing cops or others would make the association between Millennium and the various entities.

156. The Compliance Coordinator proposed the use of this deception in a January 23, 2003 e-mail to Feeney:

> [O]ne of Steve[] [Markovitz's] accounts at [a particular clearing platform] was also flagged because of the [common] signatories [on the accounts]. I **would like to open a new account using [defendant] Ikebana** [LLC] with **a non-666 address.** Additionally, I would like to begin the account using [different Millennium employees] as signatories....

(Emphasis added) Feeney's response: "ok-good idea[.]"

D. Multiple Accounts, Multiple Clearing Platforms, Multiple Registered "Rep" Numbers and "Fronts"

157. Millennium's network of companies was also used to open multiple accounts at multiple broker-dealers. In total, using at least thirty nine different clearing brokers, Millennium opened approximately 1000 brokerage accounts in the names of more than ninety different entities. Many or all of these brokerage accounts were used for the purpose of rotating or breaking up transactions between and among accounts in an effort to "fly under the radar" of mutual funds.

158. In an e-mail to Markovitz dated February 7, 2003, a timing broker explained one of the uses for multiple accounts:

> Now that we have [defendant] Stone Castle [Ltd.] open, we are going to open Stone Castle 2-5. Once the position comes in we are going to break it up among the accounts.

Markovitz replied:

> more accts is fine, however in the...case [of a particular mutual fund family] it is counterproductive to make many small trades out of 1 big trade. why? because they count turns and are not terribly sensitive to size. that is you get 8 r/t a yr or something similar..its best to do this on 2-3-4-5m trades not 322k trades. in [one particular fund family] or others we may touch[,] smaller under the radar is always better. recommendation, have 1 or 2 sub accts opened for StonCastle [sic], we don't necessarily need 5 for now. in addition we can split...trades up [in one fund family], for [the other, however,] keep larger and fewer....

159. Separately, the Compliance Coordinator explained in a July 25, 2001 e-mail to Feeney:

> I just spoke w/Kovan and he further clarified that the reason we are opening so many accounts is that if smaller sums of money are invested in each account they will be less visible.

160. To further the schemes, timing brokers acting in complicity with Millennium used

yet another layer of deception – multiple registered representative numbers along with the multiple accounts. The Compliance Coordinator explained one use for multiple registered representative numbers in an e-mail dated December 5, 2001 to Feeney, the Head of Operations and the head of market timing operations:

> **In order to be able to re-enter funds that Kovan has been restricted from,** [Millennium's timing brokers] have obtained a new rep number by joining forces with another...broker....Initially, I will be opening one Gilmore & Gillespie account and, if the system works well, we will probably open more accounts.

(Emphasis added)

161. Englander himself even suggested ways to hinder the detection efforts of mutual funds seeking to put a stop to Millennium's market timing activities. For example, Englander wrote in an e-mail to Feeney and the head of market timing operations:

> i was told today that having a foreign entity be the account name for the mutual funds as opposed to a domestic/u.s. company has it's advantages. **supposedly, the funds don't perceive int'l/offshore accounts to be market timers, yet. how do we start opening accounts that have an offshore element to them?**

(Emphasis added)

162. Englander also suggested the use of multiple brokers and multiple accounts to avoid the loss of "capacity." For example, in an e-mail dated May 14, 2002 from Pillai to Englander, Pillai wrote:

> I apologize for the large...positions we were trading [in a particular mutual fund] - our fund universe at [a particular broker-dealer] had shrunk so much, we ended up trading the same fund in several accounts. We are tackling this problem by getting more brokers and therefore new universes so we have less concentration in individual funds.

In reply, Englander's suggestion was: "try regional firms located outside of the new york area."

163. Markovitz used regional firms with limited success. In an August 2002 e-mail to

Englander and Feeney concerning "lost capacity," Markovitz wrote:

> just lost
> 6m [Broker#1]
> 9m [Broker #2]
> <u>3m Misc</u>
> 18m
>
> in first 2 cases shut down by broker dealer;
>
> Izzy, [Broker #2] was my recent attempt to deal with smaller regional firms. Acct was based out of *Cleveland*, believe it or not.

(Emphasis in original)

164. Considerably more success was had through the use of at least eighteen registered investment advisers that acted as "fronts" for Millennium to take advantage of omnibus processing through the "registered investment adviser channel" at Charles Schwab & Co., Inc. Millennium Management, L.L.C., the general partner to MLP, was itself an investment adviser and did not need to hire even one, let alone eighteen, to open accounts at Charles Schwab. Indeed, Millennium already had numerous accounts at Charles Schwab in the "retail" channel where the name Millennium (or a derivative containing the root letters "Mill") appeared in the account titles. Millennium's timing activities using Schwab's "retail" channel had been greatly restricted by mutual funds. Using the "RIA channel" would provide, in the words of a Millennium timer, a "buffer" between Millennium and the mutual funds. To access the "RIA channel," Millennium hired and paid registered investment advisory firms to act as "fronts" with respect to certain accounts. The investment advisers did not have investment discretion over Millennium's money, did not render any investment advice to Millennium or otherwise provide any real services. Investment decisions with respect to transactions associated with these

accounts were made entirely by Millennium traders. The "buffer" RIAs simply used accounts in their names to disguise Millennium's association with the transactions and throw the timing police or others seeking to detect and prevent market timing off Millennium's frail.

165. Millennium sometimes referred to the accounts used by the "fronts" as "blind accounts." For example, in an June 2002 e-mail the Compliance Coordinator informed Feeney that Markovitz requested that a new account be opened at a particular broker-dealer through one of the "front" investment advisers. Feeney replied: "ok-just to let you know we are seeing a lot of cancelled trades thru Schwab-seem to be cracking down..." The Compliance Coordinator replied: "Yes, they are...this is **a blind wrap account** through [the registered investment adviser]...hopefully, he'll have better luck with it." (Emphasis added)

166. Through these "front" RIAs, Millennium enjoyed a good degree of success. Millennium was able to obscure more than 6200 round trip market timing transactions in numerous mutual finds in an aggregate transaction volume exceeding $5.4 billion resulting in an approximate profit of $10.9 million.

167. Another idea that was floated given the difficult timing environment that persisted in mid-2003 was the use of clearing platforms associated with retirement plans. For example in a June 11, 2003 e-mail to Feeney (who later forwarded the e-mail to Englander), Pillai wrote:

> Some special features of this [clearing] platform is that they clear a lot of 401 K business (for [a particular company])...and clear trades for [a large insurance company] and **so our trades would be relatively inconspicuous since the accounts are omnibus....**

(Emphasis added) The goal was to have Millennium's market timing trades processed along with those of legitimate retirement plan participants in the hopes that mutual funds would not detect them as timing transactions. This suggestion was never implemented, however.

III. **Variable Annuities** And **Variable** Life **Insurance Policies**

168. Millennium ultimately turned to variable annuities and other insurance-related products as an additional way to market time "under the radar."

169. During the relevant time, Millennium did not need life insurance and was not interested in tax-deferred investing or a stream of annuity payments. Millennium's true interest was using variable annuity "batch" processing to market time "under the radar." Millennium was able to do so through the use of more than two hundred sub-accounts to which it gained access through bogus variable annuity and variable life insurance transactions.

170. An example of Millennium's desire for anonymity appears in a December 2001 e-mail to Feeney in which Pillai wrote:

> The insurance company does not reveal the account from which a trade originates, so my **trades would be disguised** if there were more `sticky assets' in the annuity.

(Emphasis added) Many of the subaccounts Millennium market-timed are the "mirror images" of mutual funds that Millennium was told to stop timing or would not have been able to market time if Millennium's intentions were known.

171. With respect to variable annuities, to satisfy the requirement of having a natural person, Millennium had various employees serve as sham "annuitants." To induce lower-salaried employees to participate, many or all of them received a free dinner with a spouse or significant other compliments of Millennium.

172. The annuity contract was owned by Millennium, and Millennium (not the annuitant's heirs) was the designated beneficiary in the event of the employee's death.

Therefore, one of most basic features of the annuity – its tax advantages – was not available to Millennium. Markovitz, Pillai or one of the other market timers (not the annuitant) made all investment decisions with respect to switching investments between and among mutual fund "clone" investment options.

173. Millennium also chose annuity commencement dates that were so far into the future there was no realistic chance that the contracts would ever "annuitize." In other words, no employee would survive long enough for Millennium (the annuity owner) to actually receive an annuity payment. For example, with respect to one contract where Markovitz served as the annuitant, Millennium elected to have annuity payments begin June 30, 2053 when Markovitz would be ninety years old. In many instances, Millennium employees also falsely claimed that the annuity contracts were suitable for *their* retirement and insurance needs.

174. To lay a smokescreen for mutual funds and others who might become suspicious about timing activities and seek to put a stop to them, Millennium used its network of shell companies. Later, Millennium added a new wrinkle to its deceptions.

175. Beginning in 2002, Millennium created at least eleven purported "family" trusts for use with variable annuities to throw timing cops and others off Millennium's scent. These trusts are defendants Andres Pillai Family Trust, Anya Family Trust, Chiswick Family Annuity Trust, Davis Family Annuity Trust, Gu Family Annuity Trust, Haidar Family Annuity Trust, KP Family Annuity Trust, Kovan Family Annuity Trust, Pelkey Family Annuity Trust, Petersen Family Trust, SM Family Annuity Trust-I and S. Murray Annuity Trust. They were established to create the false impression that the entity was not only unconnected to Millennium, but not connected to any hedge fund at all and, therefore, was less likely to be engaged in market timing

activities.

176. To carry out the "family" trust deception, Millennium first created a new "family" limited liability company with a name ostensibly unconnected to Millennium. The new "LLC" was not necessarily sufficient, however, to effectively disassociate Millennium with the timing activity; as an "LLC," it would still appear too much like a hedge fund. So, Millennium added yet another layer to the onion timing cops needed to peel by creating a "family" trust. The mechanics worked as follows.

177. A senior Millennium officer (in one case, Englander himself) was appointed as the "nominee" of the newly-created family "LLC." A "family" trust was then created. Pursuant to a trust agreement, the nominee, on behalf of the "family" LLC (referred to as the "Donor") transferred $1 to a trustee. A senior Millennium employee (including, in at least one case, Fred Stone) served as trustee. Variable annuity contracts were purchased by Millennium to trade sub-account "clones" and the trust became the owner. Thus, for example, defendant SM Family LLC was created and acted as the "Donor" to defendant The SM Family Annuity Trust-I pursuant to a trust agreement dated July 15, 2002. Englander acted as Nominee and Feeney acted as its Trustee. "SM" stood for Steven Markovitz, but neither Markovitz nor any member of his family (or any family) was a beneficiary of or connected with the trust.

178. To further the pretended disassociation with Millennium, a separate tax identification number was obtained for the trusts and use of Millennium's true business address was avoided. In fact, Millennium used Stone's and Englander's home addresses in several instances. One of Millennium's market timers was then given investment discretion to conduct mutual fund timing transactions in annuity sub-accounts on behalf of the trust.

179. Through the misleading impression created by use of the expression "family" trust, Millennium was able to execute more than $550 million in market timing transactions.

180. With respect to variable life insurance policies, Millennium had its employees act as "insureds" under the guise of obtaining "key man" insurance or providing deferred compensation arrangements for Millennium employees. The employees, who again were treated to dinners or other events courtesy of Millennium, actually underwent group physicals with a medical doctor to satisfy the live body requirement. These were sham transactions.

181. None of the variable life policies provided deferred compensation to any Millennium employee. A Millennium entity was both owner and beneficiary under the policies. And, Millennium employees and/or Millennium itself falsely answered "yes" to the question in the life insurance application: "is...the policy...in accord with your insurance and long term investment objectives and anticipated financial needs?" Millennium had no long term investment objective. Separately, in at least one case, Millennium signed a statement in the application falsely indicating that "as and when authorized by its employees," Millennium USA 1, L.P. would "make the necessary payments/deductions for premiums on such policies from employees [sic] compensation and arrange for such deductions to be remitted to [the insurance company]..." No such authorizations or deductions were necessary because there were no deferred compensation arrangements; the transaction was accomplished under false pretenses designed to enable Millennium to trade under the radar. In other instances, Millennium employees falsely stated on the insurance applications that there were "written plans" relating to non-existent deferred compensation arrangements.

182. In addition, most of the Millennium employees who served as insureds could

hardly be considered "key persons."

183. For example, Millennium obtained variable life policies in or about July through November 2001 as follows:

- a $27,500,000 policy with an annual premium of approximately $1 million covering a key 35 year old human resources employee who had been with Millennium for two years and earned $65,000 per year;

- a $33 million policy with an annual premium of approximately $900,000 covering a key 23 year old analyst (the "Analyst") who had been with Millennium for one year and earned $75,000 per year;

- a $34 million policy with an annual premium of approximately $1.4 million covering a key 37 year old operations manager who had been with Millennium for one year and earned $105,000 per year;

- a $34,500,000 policy with an annual premium of approximately $1.2 million covering a key 33 year old programmer (the "Programmer") who had been with Millennium for two years and earned $85,000 per year;

- a $34,500,000 policy with an annual premium of approximately $1.4 million covering a key 39 year old operations analyst who had been with Millennium for one year and earned $75,000 per year;

- a $34,750,000 policy with an annual premium of approximately $1.2 million covering a key 34 year old operations manager (the "Operations Manager") who had been with Millennium for ten years and earned $150,000 per year;

a $34,875,000 policy with an annual premium of approximately $1 million covering a key 39 year old compliance officer who had been with Millennium for one year and earned $125,000 per year;

a $34,900,000 policy with an annual premium of approximately $1 million covering a key 36 year old operations manager who had been with Millennium for four years and earned $120,000 per year;

a $34,550,000 policy with an annual premium of approximately $1.7 million covering a key 45 year old assistant trader who had been with Millennium for two years and earned $200,000 per year; and

> a $35,000,000 policy with an annual premium of approximately $1.4 million covering a key 37 year old trading analyst who had been with Millennium for one year and earned $200,000 per year.

184. In total, Millennium maintained over $300 million in purported "key man" insurance covering at least ten different employees whose annual salaries averaged $111,000 per year. Englander, the only "key man" identified in Millennium's partnership agreements, was not among them.

185. Subsequently, Millennium obtained an aggregate $204 million in purported "key person" variable life insurance from a different insurance company covering eleven employees. The aggregate annual premium was more than $10 million. Among the insureds were the Analyst, the Programmer and the Operations Manager each of whom remained so vital to Millennium's organization that new variable life insurance policies covering each of theft lives in the amount of $15 million were necessitated.

186. Some "key" employees did serve as insureds and annuitants, including Feeney (twenty-seven annuity contracts or variable life insurance policies) and Stone (twenty-eight annuity contracts or variable life insurance policies). And even Englander himself acted as an annuitant with respect to one annuity contract.

187. Through the false pretenses associated with these annuity and variable life insurance transactions, Millennium got what it was after – "round trips." Among the annuitants and/or variable life insurance policy participants producing the most round trips were:

Annuitant	No. Of Annuity Contracts or Policies	Round Trips	Approximate Transaction Volume	Millennium's Approximate Profit
Feeney	27	1357	$ 4.6 billion	$ 21.6 million
Stone	28	758	$ 960 million	$ 4.5 million
Markovitz	33	2561	$ 3.8 billion	$ 12.3 million
Pillai	26	939	$ 1.7 billion	$ 6.8 million

188. In all, twenty-five different Millennium employees acted as annuitants and/or insureds with respect to numerous variable annuity contracts or variable life insurance policies in the names of at least forty different Millennium shell companies.

1V Late Trading And Deceptive Timing Through D.C. Capital

> dc capital also is a new acct....normal brokerage acct, with the advantage of, ern shall we say, very late mkt trading.

(Source: Markovitz e-mail to his trading assistants dated November 19, 2001.)

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189. D.C. Capital, L.L.C. was during the relevant time a small brokerage firm located in Syosset, Long Island. It was formed by the D.C. Capital Timing Broker and another individual and began operations in 2000. Prior to D.C. Capital's formation, the D.C. Capital Timing Broker worked at various Long Island brokerage firms having questionable reputations.

190. D.C. Capital's "ern..., very late mkt trading" advantage explains a significant part of the reason why Markovitz used a shop as small as D.C. Capital to transact more market timing volume than any of Millennium's timing brokers. There were other reasons as well.

A. D.C. Capital's Entry Into The Market Timing Business

191. D.C. Capital entered the market timing business in mid to late 2000. The D.C. Capital Timing Broker hired a broker with whom he had worked in the past (the "Second D.C. Capital Timing Broker"), and the two established what would become an extremely profitable timing brokerage relationship with Millennium and other market timers.

192. Prior to establishing a relationship with Millennium, D.C. Capital had only one market timer as a client. From shortly after inception through May 2001, D.C. Capital regularly accepted mutual fund orders from this client after the 4 p.m. close of the financial markets for execution at the same day's price. Since D.C. Capital was a small "introducing broker," these transactions were processed through larger, more substantially capitalized "clearing brokers" with which D.C. Capital had relationships.

193. In or about late April or early May 2001, D.C. Capital was looking for a larger clearing platform that would more efficiently process market timing transactions for its existing and potential clients. In connection with an application to a particular clearing broker, D.C. Capital prepared and submitted a business plan. It states:

> DC Capital allows the financial community to place their mutual fund transactions after 4:00 pm EST. The financial community has mostly been restricted from placing their trades after 4:00 pm EST. The majority of the industry requires trades to be placed before 4:00 pm EST. DC Capital allows clients to place their trades up to 5:00 pm EST and in some cases up to 5:15 pm EST. **This service is in high demand allowing the client to gather any information after all of the** US markets **have closed and** still **being able** to receive the NAV for **that day. Earning's [sic] announcements and other news are released between 4:00 and 5:00 which play an important decision making process for the client.**

(Emphasis added)

194. The D.C. Capital Timing Broker and other D.C. Capital employees allegedly

believed they could lawfully accept mutual fund orders after 4 p.m. EST for same-day pricing. This belief was allegedly based upon the advice of D.C. Capital's lawyer who wrote the following in a May 9, 2001 letter relating to unspecified rules of the National Association of Securities Dealers, Inc., a self-regulatory organization:

> You have informed us that certain of your accounts under management purchase and sell mutual funds utilizing the Fund/Sery system on an unsolicited basis. We believe that you can, consistent with NASD rules, accept buy and sell orders that you receive after 4:00 p.m., or any other cut-off time established by the fund, and transmit these orders to the pertinent mutual funds via the Fund/Sery system. By accepting and transmitting these orders, you are not representing that these orders will be executed by the mutual fund. Indeed, your customers are aware that the acceptance or rejection of these mutual fund orders is left to the sole discretion of the mutual fund itself.

195. The D.C. Capital Timing Broker was told that the clearing broker's compliance department had issues with the acceptance of post-4 p.m. orders and a relationship with this clearing firm was not established.

196. Neither the business plan nor the May 9, 2001 letter was shared with Millennium.

B. Millennium's Introduction To D.C. Capital

197. The relationship between Millennium and D.C. Capital was established through Englander. One of the D.C. Capital Timing Broker's business associates was a close friend of Englander. The friend introduced the D.C. Capital Timing Broker to Englander because the friend, who was also a Millennium investor, knew Millennium engaged in a market timing business. The D.C. Capital Timing Broker contacted Englander and a meeting was set so D.C. Capital could pitch for Millennium's market timing business.

198. In or about early 2002, the D.C. Capital Timing Broker and the Second D.C. Capital Timing Broker traveled to Millennium's offices at 666 Fifth Avenue and met with

Englander and Markovitz. During the meeting, the parties discussed whether D.C. Capital had any capacity arrangements with mutual funds. The D.C. Capital Timing Broker and the Second D.C. Capital Timing Broker stated they did not. Markovitz asked what was D.C. Capital's cut-off time. One of the D.C. Capital representatives replied 4:30 p.m. or 5:00 p.m. Markovitz asked whether D.C. Capital had the ability to open numerous accounts. The D.C. Capital Timing Broker and the Second D.C. Capital Timing Broker indicated they did. Millennium also asked about D.C. Capital's clearing broker and requested its financial statements. The D.C. Capital Timing Broker and the Second D.C. Capital Timing Broker indicated that the financials were available publicly.

199. Englander subsequently indicated Millennium could place $50 million in trades through D.C. Capital for use in connection with market timing strategies to be executed by Markovitz.

200. Millennium was concerned about the D.C. Capital Timing Broker's background. After the meeting, Millennium ran a background check on the D.C. Capital Timing Broker. Several days after the meeting, Millennium contacted the D.C. Capital Timing Broker and inquired about the brokerage firms with which the D.C. Capital Timing Broker had been associated prior to forming D.C. Capital. Despite the reputations of these firms, Millennium ultimately got comfortable.

201. Although the accounts were opened with D.C. Capital, the assets were actually held at one of D.C. Capital's clearing brokers, which Millennium viewed as a large reputable firm. Millennium therefore established strict guidelines concerning who could authorize the movement of assets into and out of (or between and among) D.C. Capital accounts. D.C. Capital

could not; only Millennium's senior management could.

202. Later it was determined that D.C. Capital's "wrap fee" for brokering market timing transactions would be a percentage of assets in D.C. Capital accounts. As Millennium ultimately processed substantial market timing volume through D.C. Capital, the relationship became an extremely profitable one. In just over eighteen months, Millennium paid D.C. Capital more than $13.9 million for its services.

C. Millennium's Market Timing Business With D.C. Capital

203. Millennium got what it paid for. In addition to the obvious advantage "errr, very late mkt trading" provided, D.C. Capital engaged in numerous deceptive market timing tactics that enabled Millennium to disguise its association with market timing activities or, in the words of the Second D.C. Capital Timing Broker in an e-mail to Markovitz, "to swoop under the radar screen like a stealth bomber."

204. On behalf of numerous Millennium shell entities, D.C. Capital created approximately one hundred brokerage accounts for Millennium for the purpose of flying under the radar of mutual funds. Multiple registered representative numbers were also associated with these accounts to better "swoop under the radar screen." With D.C. Capital's assistance, despite thousands of account "blocks" by (and/or "stop" communications from) mutual fund companies, Millennium was able to execute more than 20,000 "round trips" in numerous mutual funds in an aggregate transaction volume exceeding $10 billion. Many of these deceptive market timing transactions were also "late trades." Millennium's profits from just over eighteen months of trading through D.C. Capital exceeded $50 million.

D. Millennium Raises Concerns Regarding Late Trading

205. Sometime in early 2002, Englander and Feeney became aware that Markovitz was in fact late trading through D.C. Capital and another brokerage firm. Feeney was uncomfortable. He reviewed mutual fund prospectus provisions concerning the times orders could be placed, forwarded them to Stone and asked Stone for his input. Thereafter, Englander, Feeney and Stone concluded that mutual fund orders needed to be placed prior to the close of the market to receive same-day pricing. As a result, sometime in early May 2002, Englander told Markovitz that he was not to engage in late trading.

206. Thereafter, on or about May 13, 2002, the D.C. Capital Timing Broker attended a meeting at Millennium's offices with Englander, Feeney, Markovitz and Stone. During the meeting, the D.C. Capital Timing Broker claimed that the SEC's "forward pricing rule" see 17 C.F.R. § 270.22c-1) applied only to mutual funds and brokers. Therefore, the D.C. Capital Timing Broker asserted, only D.C. Capital (not Millennium) was at risk if late trading was impermissible. The D.C. Capital Timing Broker further claimed that everyone, including large broker-dealers, was engaging in late trading.

207. In response, Stone stated that even if the forward pricing rule did not apply to Millennium, the representations concerning the times orders were being placed that appeared in clearing agreements between D.C. Capital or its clearing broker and the mutual funds would be false if Millennium were to late trade through D.C. Capital. Therefore, Stone explained to the D.C. Capital Timing Broker, Millennium could be guilty of aiding and abetting violations of the securities laws if D.C. Capital late traded on Millennium's behalf.

208. After the meeting ended and following further discussion among Englander,

Feeney and Stone, Englander again told Markovitz that he was not to engage in late trading.

Markovitz subsequently wrote in an May 20, 2002 e-mail to Englander:

> in my opinion, forces are conspiring quickly and violently to end the timing game. Despite my intentions to keep it alive for as long as possible, the forces are more powerful than me.
>
> Nonetheless, everything i experience on a daily basis from brokers, clearing firms, annuity companies and fund companies is about timing....THAT **IS the game that will make headlines, nothing else.**
> If we **can stomach that headline** risk, the late trade risk — as **you pointed out –** is **a secondary, much more** subtle risk.
>
> **the later trading truly helps me in ways more than you know. To lose it is not good. I would rather not expedite the death of a game that is likely going to die anyway.**

(Emphasis added)

V. Failure To Supervise With Respect To Late Trading

209. Despite Markovitz's expressed desire to keep the benefits of late trading, no procedure was put into place to monitor the times at which Markovitz and his assistants (or any other Millennium inside or outside market timers) were placing trades. Not surprisingly given the lack of oversight, Markovitz did not stop.

210. After a brief period "on the late trading wagon," Markovitz began late trading again through D.C. Capital and at least one other broker-dealer and continued placing late trades up until Millennium's receipt of a subpoena from the Attorney General's Office in late July 2003 seeking documents and information concerning market timing and late trading.

211. And despite the D.C. Capital Timing Broker's claim that "everyone" engaged in "late trading," Millennium made no effort after May 2002 to ascertain whether its other internal and external market timers had engaged in late trading in the past or to instruct them that they

should not do so going forward.

212. On January 17, 2003, Pillai informed Englander that Pillai was also engaged in a late trading strategy. Pillai's strategy involved looking at the performance of certain futures indexes between 4 p.m. and 5 p.m. New York time and then placing market timing trades (or cancelling tentative trades that he had placed prior to 4 p.m.). Englander and Stone told Pillai he could not engage in late trading and he stopped. Still no efforts were made by Millennium to ascertain whether any of its other internal or external market timers were engaged in late trading.

213. After Markovitz's guilty plea became public, a principal at one of Millennium's largest investors (the "Investor") and certain of the investor's employees spoke with Englander. The Investor took detailed notes of the conversation. The Investor's notes reflect that Englander admitted he was "likely guilty of failing to supervise" Millennium's traders.

FIRST CAUSE OF ACTION

214. The acts and practices of the Defendants alleged herein violated Article 23-A of the General Business Law, in that they involved the use or employment of a fraud, deception, concealment, suppression, or false pretense, engaged in to induce or promote the issuance, distribution, exchange, sale, negotiation or purchase within or from this state of securities or commodities.

SECOND CAUSE OF ACTION

215. The acts and practices of the Defendants alleged herein violated Article 23-A of the General Business Law, in that they involved the use or employment of a representation or statement which was false, where the person who made such representation or statement: (i) knew the truth; or (ii) with reasonable effort could have known the truth; or (iii) made no

reasonable effort to ascertain the truth; or (iv) did not have knowledge concerning the representation made, and where such acts or practices were engaged in to induce or promote the issuance, distribution, exchange, sale, negotiation or purchase within or from this state of securities or commodities.

THIRD CAUSE OF ACTION

216. The acts and practices of the Defendants alleged herein violated Article 23-A of the General Business Law, in that Defendants engaged in an artifice, agreement, device or scheme to obtain money, profit or property by a means prohibited by section 352-c of the General Business Law.

FOURTH CAUSE OF ACTION

217. The acts and practices of the Defendants alleged herein violated Article 22-A of the General Business Law in that Defendants engaged in deceptive acts and practices prohibited by section 349 of the General Business Law.

FIFTH CAUSE OF ACTION

218. The acts and practices of the Defendants alleged herein constitute conduct proscribed by section 63(12) of the Executive Law, in that Defendants engaged in repeated fraudulent or illegal acts or otherwise demonstrated persistent fraud or illegality in the carrying on, conducting or transaction of a business.

SIXTH CAUSE OF ACTION

219. The acts and practices of the Defendants alleged herein constitute fraud under the common law of the State of New York.

220. Plaintiff has been irreparably harmed and has no other adequate remedy at law.

WHEREFORE, Plaintiff demands judgment against Defendants as follows:

A. That Defendants be permanently restrained and enjoined from engaging in any fraudulent practices in violation of Article 23-A of the General Business Law and Section 349 of the General Business Law or proscribed by section 63(12) of the Executive Law;

B. That Defendants and any of their agents or others acting on their behalf be permanently restrained and enjoined from conducting deceptive market timing or late trading transactions in any mutual hinds or variable annuities;

C. That Defendants, pursuant to General Business Law §§ 349 & 353(3) and Executive Law § 63(12), pay restitution of monies obtained directly or indirectly by means of, and damages caused directly or indirectly by, the fraudulent acts complained of herein;

D. That Defendants, pursuant to General Business Law §§ 349 & 353(3) and Executive Law § 63(12), disgorge all compensation received for engaging in deceptive market timing and late trading transactions;

E. That Defendants pay civil penalties pursuant to General Business Law § 350-d;

F. That each of the Defendants pay Plaintiff costs and additional allowances in the maximum amount allowable under General Business Law § 353(1) and CPLR § 8303(a)(6);

G. That Defendants pay punitive damages; and

H. That the Court award such other and further relief to Plaintiff as the Court may deem just and proper in the circumstances.

Dated: New York, New York
November 28, 2005

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