TESTIMONY
OF

LINDA CHATMAN THOMSEN, DIRECTOR
DIVISION OF ENFORCEMENT
U.S. SECURITIES AND EXCHANGE COMMISSION

CONCERNING
INSIDER TRADING

BEFORE THE COMMITTEE ON THE JUDICIARY

UNITED STATES SENATE

DECEMBER 5, 2006

U.S. Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549

Testimony Concerning Insider Trading

by Linda Chatman Thomsen
Director, Division of Enforcement
U.S. Securities and Exchange Commission

Before the U.S. Senate Committee on the Judiciary

December 5, 2006

Chairman Specter, Ranking Member Leahy, and Members of the Committee:

Thank you for inviting me to testify today about insider trading involving hedge funds. Our laws against insider trading play an essential role in protecting our securities markets and in promoting investor confidence in the integrity of those markets. Rigorous enforcement of our current statutory and regulatory prohibitions on insider trading is an important part of the Commission's mission.

I am especially pleased to testify together with Associate Deputy Attorney General Ronald Tenpas of the United States Department of Justice, and Richard Blumenthal, Attorney General of the State of Connecticut. The Commission, as you know, is a civil enforcement agency and we use civil sanctions to address insider trading. However, insider trading may also violate federal criminal law, as well as state securities regulations and other state laws. The respective histories of the SEC and the Department of Justice, as well as those of state attorneys general and securities regulators, demonstrate our collective commitment to prosecuting insider trading, civilly and criminally, under federal and state law. Our respective histories also demonstrate our collective commitment to working with each other.

Proving An Insider Trading Case

When I last appeared before this Committee a few months ago, I noted that insider trading by hedge funds was an area of significant concern to the Commission, the Enforcement Division, and this Committee. Insider trading by hedge funds remains a substantial concern to the Division, and represents a significant focus of our current enforcement efforts. As suggested by your staff, I will discuss the process we follow in bringing insider trading cases in general, and also speak to cases involving insider trading by hedge funds.

Over the years, investigating and prosecuting insider trading violations has remained a central and important element of our enforcement mission. The Division pursues these cases day in and day out, and has developed unparalleled expertise in this area. Basically, the staff must prove that a trade was made on the basis of material, non-public information, with the requisite intent to violate the law, and that the information was used or obtained in violation of a duty to the source of the information. That's quite a mouthful, even for a lawyer, so it may be helpful if I describe in more detail, the three

key legal requirements that must be met for the SEC to bring a civil insider trading case, which are:

1) access to material, non-public information;

2) scienter (or culpable intent); and

3) breach of a duty to the source of the information.

Before I detail these legal requirements, however, let me step back and discuss some background regarding our insider trading investigations. Insider trading leads come from a host of sources, not only market surveillance but also the media, public tips, and information developed in our own inspections and investigations. Identifying suspicious trading is an essential starting point, but it is only the first step in compiling a viable case. While the SEC's Enforcement Division has brought hundreds of successful insider trading cases, there are also many investigations that are opened and later closed without enforcement action. We may open an investigation based on suspicious trading and all of the circumstances may look troubling, but after a thorough look, we may discover no evidence of insider trading or not enough evidence to prove there has been a violation of law. Because an investigation may not lead to an enforcement action, we are always mindful that public disclosure of the mere fact of an SEC investigation may unfairly impugn the reputations of the entities and individuals whose conduct may be exonerated. For this reason, as a matter of long-standing Commission policy, our investigations are conducted on a confidential basis and, as a general matter, we do not confirm or deny the existence of any ongoing investigations.

One of the challenges in successfully prosecuting insider trading is that so much of the relevant activity—trading—is legitimate and must be protected. Trading based on one's own research and financial acumen or strategies is not only legitimate but encouraged. The problem arises only when trades become unlawful because they are based on material non-public information obtained through a breach of duty to the source of the information.

As the law of insider trading has developed over time, it has come to impose legal requirements intended to distinguish legitimate conduct from illegitimate conduct. As I mentioned a moment ago, the law requires that the information be confidential and non-public. If so many people already know the information that it crosses the tipping point where it can be deemed public—based on prior media reports, for instance—there is no violation. The staff must also show scienter—a culpable state of mind or intent to violate the law. In other words, the tipping or trading must be undertaken with culpable intent to commit a violation, and not as the result of an inadvertent slip or innocent mistake. Finally, the staff must also show a violation of duty to the source of the information. The duty to the source may be easy to prove against a tipper who passes on information in breach of a confidentiality agreement. But if information is passed along a chain of tippees, it may become harder to prove that a trader who obtained the information third- or fourth-hand had any duty to the source, or knowledge of the original tipper's duty to the source. Though each of these legal requirements must be established in every insider

trading case, they are important because they help to distinguish unlawful trading from the much larger universe of lawful trading.

Insider trading can be, and usually is, accomplished within a very small group or even by a single individual. The communications that result in insider trading do not necessarily generate much of a paper trail. The executive working on due diligence for a confidential deal may meet his brother-in-law in a public park on his lunch hour and pass along a tip. Because there are so few people involved, there may not be witnesses or bystanders who will come forward and report the tipping. Moreover, those who know about the tip may become participants in a scheme because the potential (though illegal) rewards are enormous.

Despite these challenges, our staff has become particularly adept at sifting through all available forms of evidence, including phone records, emails, instant messages, and the electronic footprints of internet protocol data. Our staff culls through trading records, interviews and takes the testimony of witnesses, and reviews bank and brokerage statements. With these tools and resources, our staff has built solid, credible enforcement actions against hundreds of wrongdoers.

Proving Insider Trading In the Context of Hedge Funds

Investigating potential insider trading by hedge funds presents additional challenges because of their high volume trading and proprietary trading strategies. Because they often have substantial assets under management, hedge funds may place extremely large trades in many different securities on a daily basis. The huge volume of trading by hedge funds across a broad range of securities may generate any number of transactions that appear to be unusual or suspicious, but for some hedge funds these trades may be typical. When the SEC approaches a hedge fund with evidence of a large and suspicious trade in advance of a public announcement by a company, the hedge fund often replies that it placed trades of the same magnitude in the same security on many different occasions—and the trading records generally support that claim.

Tracking a hedge fund's trading in a specific security may also be challenging. It is not uncommon for hedge funds to use the services of multiple prime brokers—registered broker-dealers that facilitate trades and other transactions on behalf of hedge funds. A hedge fund may break up a single large trade into many smaller trades to be facilitated through a number of prime brokers over time because, for example, the hedge fund may want to make its trading less obvious in the market, often to protect its proprietary trading strategy. Thus, to develop an accurate composite view of a hedge fund's trading in a particular security, it may be necessary to review records from all of its prime brokers.

The prime brokers provide the SEC with a window into the trading activities of the hedge funds they serve, but it is admittedly a limited window. While a prime broker has information about the transactions it performs for a hedge fund, it generally has little information about activities the hedge fund may be conducting through other prime brokers. Nonetheless, the Enforcement Division remains optimistic about prime brokers as a source of leads regarding unlawful insider trading.

While the SEC has access to the trading records of prime brokers and receives referrals from the SROs regarding suspicious trading executed through their markets, the available documents are generally organized according to the security involved in the suspicious transactions (e.g., XYZ Company), not the identity of the trader. Similarly, the SROs' surveillance systems are set up to trigger alerts based on aggregate trading parameters regarding a particular security, and not based on the identity of the trader. A referral from an exchange usually identifies the issuer of the security involved (which might have announced a merger or other major transaction) and a list of identified traders, which may include one or more hedge funds or accounts trading on behalf of hedge funds. As a result, referrals about suspicious trading by a particular hedge fund appear like random puzzle pieces, but whether the pieces are part of a larger pattern is far from obvious. One SRO may report suspicious trading in a security by a specific hedge fund, among other traders, on one day, while another SRO may report suspicious trading in a different security by the same hedge fund, again among other traders, on a different day. The SEC presently does not have an electronic system to aggregate referrals based on the identities of the specific traders involved, but we anticipate implementing a new case tracking system by mid-2007 that will enable us to compile all referrals from different exchanges and different time periods by trader.

The identification of suspicious trading and resulting referrals are only the start of the necessary detective work by the SROs and the SEC. The SEC and the SROs gather and analyze the trading records and survey employees of the issuer about any relationship or association they may have with a list of known traders. The objective is to eliminate traders who did not have access to inside information, and more importantly, to establish links between known traders and potential sources of inside information. In the course of an enforcement investigation, the staff's search for access to inside information is meticulous, time-consuming, and sometimes proves to be inconclusive, but all potential leads are carefully considered and examined.

The SEC's Investigation of Potential Insider Trading by Pequot

I know our investigation of potential insider trading by a well-known hedge fund, Pequot Capital Management, has piqued the Committee's interest. A former SEC attorney has alleged that the investigation was impeded and the attorney was terminated because he sought to take testimony from a prominent individual. Speaking for the Division of Enforcement, I want you to know that these allegations are simply not true.

Although it is uncomfortable to discuss an individual's job performance in detail in a public setting, the former SEC employee's false allegations against the Enforcement Division have made the facts surrounding his termination a public issue. Therefore, I feel compelled to share with you the Enforcement Division's perspective on his performance problems and his resulting termination. After an unhappy probationary period of employment, the former SEC employee was terminated on September 1, 2005 because of "his inability to work effectively with other staff and his unwillingness to operate within the Securities and Exchange Commission (SEC) process." The SEC's termination letter is attached hereto. When the staff attorney was hired, he was required to serve a one-year probationary or trial period during which his employment could be terminated for any

reason or no reason, but there were indeed many reasons in this particular case. He had continued personality conflicts with other staff attorneys, resisted standard supervision, and ignored the SEC's chain of command. Despite these problems, the SEC attempted to accommodate him and to ameliorate the problems he caused in his work groups. During his brief tenure, he was, at his request, transferred from his original supervisor to a supervisor he requested, about whom he now bitterly complains. He also requested, and received, official time to pursue an unsuccessful age discrimination claim against the SEC for failing to hire him on 22 prior applications. The EEOC's opinion denying those claims is attached; the former employee is appealing the decision.

During his tenure, the former employee demonstrated his own dissatisfaction with his employment by twice leaving the office abruptly during the workday after disagreeing with other attorneys, and on a third occasion, by actually tendering his written resignation, only to rescind it some time later. After assuming primary responsibility for the Pequot investigation for several months in 2005, the former employee announced he would not draft the customary memorandum summarizing the investigation he now so publicly discusses. With respect to the substance of his work, he issued – without his supervisors' review or approval – subpoenas that violated federal privacy law, which were withdrawn as soon as his supervisors learned of them. But for the corrective actions of his SEC supervisors, the staff attorney's work product could have been extremely damaging to the SEC, and his continued resistance to supervision created a substantial risk of future error. After the SEC expended considerable efforts in attempts to make the employment relationship work, we decided not to extend his employment beyond the one-year probationary period.

As to the potential insider trading matters at issue in the Pequot case, they were thoroughly investigated. The investigation was ultimately conducted in large part by staff other than the one former attorney who is now heard to complain and was continued long after he left the agency. Between February 2002 and April 2005, the Enforcement Division received a total of 15 SRO referrals regarding various transactions in which Pequot, among others, was identified as a trader. After preliminary screening by two senior supervisors, 13 of these transactions were forwarded on to enforcement staff for further review and consideration, including 10 that were forwarded to staff working on the Pequot investigation. The GE/Heller transaction investigated by the former employee was not the subject of an SRO referral, and our closing of the matter was consistent with the NYSE's original decision to close the matter in 2002. After reviewing the suspicious trading at issue, the NYSE decided not to refer the matter to the SEC for further investigation, but instead sent the Commission a closing memorandum dated January 30, 2002, for informational purposes only, noting that "the deal was expected and the size did not appear out of character." Although the SEC's Pequot investigation reviewed that transaction and many others, we did not find sufficient evidence to support an enforcement action. As a result, the investigation was closed by the Enforcement Division due to lack of evidence, and thus we will not be asking the Commission to take any further action. Because of the public attention this case has received, the Commission has authorized the Division to make its closing memorandum available to

the public, and it is attached to my testimony. I think you will find it a useful summary of the many hours of hard work that went into this investigation.

Finally, Mr. Chairman, the three supervisors working on the Pequot investigation, who collectively have decades of experience and who have been involved in some of our toughest cases, were not influenced by who any of the particular people involved in the investigation were, but rather by the facts and the evidence. This is consistent with the finest traditions of this agency. We follow the facts, and if those facts take us to John or Jane Doe or some more famous John or Jane, so be it. We have gathered evidence from and about, and in some instances we have sued, captains of industry, Presidential cabinet members, Members of Congress, and celebrities, as well as thousands of other far less well known people. Indeed, a long list of prominent and not so prominent individuals would undoubtedly testify that the Enforcement Division does not pull its punches. I want to assure the Committee that we are passionate about our work and will pursue it with vigor, skill and fairness.

That concludes my testimony. I would be glad to answer any questions you may have.

Attachments

ATTACHMENT 2

MEMORANDUM

VIA: Federal Express, Certified and First Class Mail

TO: Gary J. Aguirre

FROM: Linda Chatman Thomsen
Director, Division of Enforcement

DATE: September 1, 2005

SUBJECT: Notice of Termination During Trial Period

This is to inform you that your employment as a General Attorney (SI), Enforcement Division, will be terminated during your trial period based upon your demonstrated inability to work effectively with other staff members and your unwillingness to operate within the Securities and Exchange Commission (SEC) process. Your termination from the SEC and from the Federal service will be effective at the close of business on Friday September 2, 2005.

You began your employment with the Commission on September 7, 2004. As you were advised at the time of your appointment, an employee who is given a career conditional appointment, as you were, must serve a one-year trial period. It is during this time that an employee has to demonstrate fully his/her qualifications for continued employment.

Several times throughout your trial period, your supervisors advised you that your conduct was inappropriate. You were permitted to transfer from one Assistant Director group to another after assuring your Associate Director that problems that had occurred, including personality conflicts and resistance to standard supervision, would not recur. However, you have continued to have conflicts with other staff attorneys, your branch chief, and a Trial Unit attorney assigned to your primary case responsibility. You have continually expressed dissatisfaction with the supervisory structure and ignored the chain of command in the Division. On one occasion, you submitted (and later withdrew) your resignation to your Associate Director, and indicated that you were uninterested in participating in preparation of your primary case assignment beyond its investigatory stage. While your substantive work generally has been good, the problems that have occurred in other areas are so significant that they far outweigh the value of that work.

During the last several months, your Associate Director, your Assistant Director, and your branch chief have met with you on several occasions to explain to you the importance of working together with other staff members to achieve consensual goals and the importance of operating within the SEC process.

Since those meetings, your conduct has not improved to the level that warrants retention beyond your trial period. Therefore, your employment with the SEC will be terminated during your trial period, effective September 2, 2005 at 5:00 p.m., in accordance with the provisions of 5 CFR 315.804.

I have reviewed the situation with your supervisors, and this decision represents the consensus reached among them. You may appeal this action to the Merit Systems Protection Board (MSPB) only if you believe it was based on partisan political reasons or marital status. Any such appeal must be submitted in writing, not later than thirty days after the effective date of this action, to the Merit Systems Protection Board, Washington, D.C. Regional Office, 1800 Diagonal Road, Suite 205 Alexandria, VA 22314-2480; e-mail: washingtonregion@mspb.gov.; Fax: (703) 756-7112. Appeal forms are attached. You can access the relevant regulations at www.mspb.gov.

If you have any questions about this notice or your rights, please contact Linda Borostovik, Human Resources Specialist, at 202-551-7871. Although she may not represent you, Ms. Borostovik is available to answer questions you may have regarding your attendant rights. In addition, we need to coordinate your obtaining personal items from Station Place and returning your laptop, token, identification badge, and office key. You may contact Chuck Staiger at 202-551-4990 to arrange to come into the office for your personal belongings and the return of Commission items or to use a courier service for this purpose.

Attachment: MSPB Appeal Forms

EQUAL EMPLOYMENT OPPORTUNITY COMMISSION
WASHINGTON FIELD OFFICE
1801 L Street, N.W., Suite 100
Washington, D.C. 20507

Gary Aguirre, Complainant, v. William H. Donaldson, Chairman, U.S. Securities and Exchange Commission, Agency.	)	EEOC No. 100-2005-00413X Agency No. 155120631-48 **Date: June 14, 2006**

DECISION

This Decision is being issued without a hearing, pursuant to 29 C.F.R. § 1614.109(g)(3) (2005). On June 28, 2005, I issued a Notice of Intent to Issue a Decision Without a Hearing (Notice). On July 13, 2005, the Agency issued a response to my Notice by filing a Motion for Summary Judgment Without a Hearing and Memorandum in Support. Complainant filed a Memorandum of Points and Authorities in Opposition for Summary Judgment, on August 15, 2005. The remaining procedural history is contained in the case file and the Investigative Report ("IR") and will not be reiterated. The record before me consists of the IR and the parties' submissions.[1]

[1] On August 15, 2005, Complainant filed a Declaration and Application for Extension of Page Length to Motion for Summary Judgment and Motion to Strike Inadmissible Evidence Offered in Support of Summary Judgment. Complainant's request for an extension of page length is **GRANTED**. Complainant's request to strike is **DENIED**.

On July 13, 2005, the Agency filed a Motion for Leave to File a Motion for Summary Judgment in Excess of Fifteen Page Limit. The motion is **GRANTED**. On August 25, 2005, the Agency filed an Opposition to Complainant's Declaration and Application for Extension of Page

(continued...)

CLAIMS

Whether the Agency discriminated against Complainant on the bases of his race (Caucasian), National Origin (Hispanic), sex (male), and age (DOB: 03/07/40), when:

(1) the Agency failed to select him for the following Vacancy Announcements:

a. 03-268-SW
b. 04-034-DC
c. 04-077-MK
d. 04-083-DJ
e. 04-88-MB
f. 04-128-MK
g. 04-060-DP (re-posted as 04-154)
h. 03-256-TR
i. 04-069-DC
j. 03-206-DC
k. 03-208-DC
l. 03-251-DC
m. 04-076-DP;

(2) the Agency failed to select him for an SK-14 position in the San Francisco District Office, as advertised in the Legal Career Center's May 30, 2003 posting;

(3) the Agency failed to select him for a position in the SEC's Northeast Regional Office in response to the special application he submitted on March 1, 2004; and

(4) the Agency cancelled Vacancy Announcement 04-027-DP without filling the position.

FINDINGS AND ANALYSIS

A. THE GOVERNING LAW FOR SUMMARY JUDGMENT

The EEOC's regulations on summary judgment are patterned after Rule 56 of the Federal Rules of Civil Procedure, which provides that a moving party is entitled to summary judgment if

---

[1](...continued)
Limit or in the Alternative, Agency's Motion for Leave to File a Reply to Complainant's Opposition to the Agency's Motion for Summary Judgment. The Agency requests are **DENIED**.

there is no genuine issue as to any material fact, and the moving party is entitled to judgment as a matter of law. There is no genuine issue of material fact where the relevant evidence in the record, taken as a whole, indicates that a reasonable factfinder could not return a verdict for the non-moving party. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986); *Matsushita Elec. Indus. Co. v. Zenith Radio*, 475 U.S. 574, 587 (1986).

B. FACTS

1. Complainant practiced law from 1967 until 1995.

2. Complainant was the senior partner in a small law firm from 1984 to 1995.

3. Complainant retired from active legal practice in 1995 to attend film school.

4. Subsequently, Complainant formed a film company and engaged in some part-time civil litigation consulting work between 1996 to 2000. The consulting work took 30% of his time.

5. In 2001, Complainant returned to law school and received an L.L.M from the Georgetown University Law Center.

6. Complainant applied for an SK-16 Senior Trial Attorney position with the U.S. Securities and Exchange Commission's (SEC) Midwest Regional Office, Vacancy Announcement No. 03-268-DW. The position was opened in October 2003.

7. The applications for the position were screened by a Human Resources (HR) Specialist, who decided not to certify Complainant as being minimally qualified. Thereafter, Complainant contacted the HR Specialist via telephone and after the conversation, she decided to forward Complainant's application to the selecting official for consideration.

8. Senior Associate Regional Director, Midwest Regional Office, and selecting official

for the position, Robert Burson (Caucasian, American/Irish/English, male, DOB: 4/26/54), selected two candidates for the position. Complainant was not selected.

9. Complainant applied for an SK-14, General Attorney position with the SEC's Securities Industry Division, Vacancy Announcement No. 04-034-DC.

10. HR received the applications for the position, screened them and certified sixty-four candidates, including Complainant, as being minimally qualified for the position.

11. James Clarkson (Caucasian, White, male, DOB: 3/1/42), Director of Regional Office Operations in Enforcement, the selecting official for the position, selected Francisco Medina from the certificate without conducting an interview. Clarkson interviewed Medina a few months before the vacancy announcement was posted for another position (not presently at issue) and invited Medina to apply for General Attorney position 04-034-DC.

12. Complainant applied for an SK-17, Supervisory Trial Attorney position with the SEC's Southeast Regional Office in Miami, Vacancy Announcement No. 04-077-MK.

13. HR received the applications for the position, screened them and certified thirteen candidates, including Complainant, as being minimally qualified for the position.

14. Associate Regional Director and selecting official, Glenn Gordon (Caucasian, American/Eastern European Descent, White, male, DOB: 6/5/61), reviewed the certificate and resumes and identified three candidates for interviews. Complainant was not selected for an interview. Gordon, Peter Bresnan and Teresa Verges interviewed the candidates. Robert Levenson was selected for the position.

15. Complainant applied for an SK-14, General Attorney position with the SEC's Fort Worth District Office, Vacancy Announcement No. 04-083-DJ.

16. HR received the applications for the position, screened them and certified twenty-three candidates, including Complainant, as being minimally qualified for the position.

17. Associate District Administrator and selecting official, Spencer Barasch (Caucasian, American, male, DOB: 11/27/57), and other managers reviewed the certificate and identified applicants for interviews. Complainant was not interviewed.

18. Two individuals were selected for the position, Jennifer Brandt (Caucasian, female) and Jay Reddien (Caucasian, male). Reddien declined the offer and a third offer was extended to Jason Lewis (Native American, male), who accepted the offer.

19. Complainant applied for an SK-16, Senior Special Counsel position with the SEC's Division of Market Regulation, Washington, D.C., Vacancy Announcement No. 04-088-MB.

20. HR received the applications for the position, screened them and certified thirty-six candidates, including Complainant, as being minimally qualified for the position.

21. Associate Directors David Shillman (Caucasian, American, male, DOB: 9/9/60) and Elizabeth King (American, White, female, DOB: 12/31/66), the selecting officials, reviewed the applicants and identified eleven applicants for interviews. Complainant was not interviewed. John Roeser (Caucasian, male) and Michael Gaw (Asian, male) were selected for the position.

22. Complainant applied for an SK-16, Trial Attorney position with the SEC's Securities Industry Division, Vacancy Announcement No. 04-128-MK.

23. HR received the applications for the position, screened them and certified forty-five candidates, including Complainant, as being minimally qualified for the position.

24. Glenn Gordon, Robert Levenson (Caucasian, White, male, DOB: 11/12/57), and Christopher Martin (Caucasian, American, male, DOB: 10/27/70), were members of the

interview panel. Nine applicants, including Complainant, were interviewed by the panel.

25. Gordon was the selecting official for the position.

26. Complainant was not selected for the Trial Attorney position.

27. Complainant applied for an SK-12/13/14 Advisor position with the SEC's Securities Industry Division, Vacancy Announcement No. 04-060-DP.

28. HR received the applications for the position, screened them and produced a certificate for the Division of Corporate Finance for further consideration. Complainant was not included in the certificate.

29. The Attorney Advisor position was open only to SEC employees.

30. Complainant applied for an SK-16, Trial Attorney position with the SEC's Northeast Regional Office, Vacancy Announcement No. 03-256-TR.

31. HR received the applications for the position, screened them and certified sixty candidates, including Complainant, as being minimally qualified for the position.

32. Barry Rashkover (protected categories unknown), Associate Regional Director, was the selecting official.

33. Ten applicants were interviewed for the position.

34. David Markowitz was selected for the position.

35. Complainant applied for an SK-16, Trial Attorney position with the SEC's Enforcement Division, Washington, D.C., Vacancy Announcement No. 04-069-DC.

36. HR received the applications for the position, screened them and certified eighty-eight candidates, including Complainant, as being minimally qualified for the position.

37. A panel consisting of three members, Ken Miller, Suzanne Romajas, and Rick

Simpson, reviewed the certificate and referred seventeen applicants for interviews to the selecting official, Kornblau. Complainant was not referred to the selecting official for an interview.

38. Complainant applied for a Trial Attorney position, Vacancy Announcement No. 03-206-DC, with the SEC's Enforcement Division, in Washington, D.C.

39. Complainant was included in the Excepted Service Attorney Selection Certificate (certificate) for the position as being minimally qualified for the position.

40. The certificate listed one hundred and thirty-seven applicants as minimally qualified for the position.

41. A panel consisting of three Enforcement employees reviewed the certificate and interviewed twenty-two of the certified applicants, including Complainant.

42. Eight candidates were referred to the selecting official, David Kornblau (Caucasian, American, male, DOB: 4/18/61), Chief Litigation Counsel, Enforcement, by the panel. Complainant was initially not included. However, one of the panel members referred Complainant's resume to Kornblau, because he deemed it "unusual." IR, F-2 at 14.

43. All nine candidates were interviewed by Kornblau and Peter Bresnan (Caucasian, Irish/German/Hungarian/Jewish, male, DOB: 3/24/55), Deputy Chief Litigation Counsel.

44. Six candidates were selected for the 03-206-DC positions. Complainant was not one of the candidates selected.

45. Complainant applied for an SK-14, General Attorney position with the SEC's Securities Industry Division, San Francisco District Office (SFDO), Vacancy Announcement No. 03-208-DC.

46. HR received the applications for the position, screened them and certified nineteen candidates as being minimally qualified for the position. Complainant was not included in the certificate.

47. Robert Mitchell, Assistant District Administrator for Enforcement, selected Jina Choi for the General Attorney position. Mitchell knew Choi, therefore, she was not interviewed for the position.

48. Complainant applied for an SK-17, Supervisory Trial Attorney position with the SEC's Pacific Regional Office, Vacancy Announcement No. 03-251-DC.

49. HR received the applications for the position, screened them and certified twenty-one candidates, including Complainant, as being minimally qualified for the position.

50. Associate Regional Directors, Sandra Harris (Caucasian, Irish/German/Romanian/Dutch/Native American, female, DOB: 7/12/58) and Randall Lee (Asian, American, male, DOB: 8/15/61), identified seven applicants for interviews. Complainant was not selected for an interview.

51. Michael Piazza (Caucasian, male, over 40) was selected for the position.

52. Complainant applied for an SK-13/14, Attorney-Advisor position with the SEC's Securities Industry Division, Office of International Affairs, Washington, D.C., Vacancy Announcement No. 04-027-DC.

53. HR received the applications for the position, screened them and issued a certificate listing the applicants who were minimally qualified for the position. Complainant was not included in the certificate.

54. Complainant was not selected for the position.

55. Complainant applied for a non-posted Staff Attorney position with the Northeastern Regional Office.

56. Complainant was interviewed by several employees in the office, including Christopher Castano (Staff Attorney), Bennett Ellenbogen (Trial Attorney) and Leslie Kazon. Complainant's file was forwarded to Deputy Regional Director, Edwin Nordlinger, for further consideration.

57. Complainant was not selected for a position.

58. On February 18, 2004, the Agency canceled Vacancy Announcement No. 04-027-DP, SK-16 Attorney-Advisor, Securities Industry, Division of Corporate Finance. The Vacancy Announcement was set to close on February 25, 2004.

59. Complainant is currently employed as an SK-14 Trial Attorney in the SEC's Division of Enforcement in Washington, D.C.

C. CONCLUSIONS OF LAW

To establish a *prima facie* case of disparate treatment in a nonselection case, a Complainant may show: (1) that he/she is a member of a group protected from discrimination; (2) that he/she applied for and was qualified for the position at issue; and (3) that he/she was rejected under circumstances which give rise to an inference of unlawful discrimination, *e.g.*, the Agency continued to seek applicants or filled the positions with persons who were not members of Complainant's protected group. *McDonnell Douglas Corp. v. Green*, 411 U.S. 792, 802 (1973), n.13.

If a *prima facie* case is established, the burden shifts to the Agency to articulate a legitimate, non-discriminatory reason for the challenged action. *Texas Dep't of Cmty. Affairs v.*

Burdine, 450 U.S. 248, 253-54 (1981); *McDonnell Douglas*, 411 U.S. at 802. Complainant may then show that the explanation offered by the Agency was not the true reason, but a pretext for discrimination. *Burdine*, 450 U.S. at 256; *McDonnell Douglas*, 411 U.S. at 804. The ultimate burden of persuading the trier of fact that the Agency discriminated against the Complainant always remains with the Complainant. *St. Mary's Honor Ctr. v. Hicks*, 509 U.S. 502, 506-07 (1993); *United States Postal Serv. Bd. of Governors v. Aikens*, 460 U.S. 711, 715 (1983).

Although the initial inquiry in a discrimination case usually focuses on whether the Complainant has established a *prima facie* case, following this order of analysis is unnecessary when the Agency has articulated legitimate, nondiscriminatory reasons for its actions. *See Washington v. Dep't of the Navy*, EEOC Petition No. 03900056 (May 31, 1990). In such cases, the inquiry shifts from whether the Complainant has established a *prima facie* case, to whether he has demonstrated by a preponderance of the evidence that the Agency's reasons for its actions were merely a pretext for discrimination. *Id. See United States Postal Service Board of Governors v. Aikens*, 460 U.S. 711, 714-17 (1983). In this case, I find that the Agency has articulated legitimate, nondiscriminatory reasons for its actions.

ARTICULATED NONDISCRIMINATORY REASONS

1. Vacancy Announcement No. 03-268-SW

Robert Burson, selecting official, indicated that he was looking for a candidate who could manage and conduct complex trials, who possessed practical knowledge of the securities laws, had excellent writing and pretrial skills, and exhibited strong interpersonal skills. Burson stated that he selected Thomas Szomba, based on his trial experience at SEC and the U.S. Attorney's Office as a federal prosecutor, and his success in trying complex securities cases. Burson also

stated that he selected Jarrett Becker based on his solid litigation experience, which included white collar criminal defense in the area of securities and non-securities. Burson also added that Becker had pre-trial and trial experience as first and second chair.

2. **Vacancy Announcement No. 04-034-DC**

James Clarkson, Director of Regional Office Operations in Enforcement and selecting official, stated that he selected Francisco Medina, a Hispanic male, for the position due to his superior qualifications. Clarkson indicated that he had previously interviewed Medina for another position and that he considered him a suitable candidate for the position in question. According to Clarkson the selectee had strong credentials, as he had previous experience working in two major law firms, possessed strong academic and professional backgrounds, and served as Associate General Counsel with Citigroup, Inc.

3. **Vacancy Announcement No. 04-077-MK**

Glenn Gordon attested that he was looking for a candidate who could be responsible for supervising the trial unit, demonstrated knowledge of securities laws, had strong writing and editorial skills, and could manage others. Gordon further attested that he did not select Complainant for an interview because his application did not show that he possessed the practical securities related experience necessary for the position. Gordon explained that Complainant's prior legal experience mainly dealt with state court, which is different from SEC's federal court practice. Gordon also indicated that Complainant did not possess the background and experience necessary to supervise other SEC trial attorneys. According to Gordon, the selectee had prior experience in the trial unit, had a strong background in securities law, possessed excellent writing skills, and had the ability to edit and review the work of other attorneys. Gordon also indicated

that the selectee had prior experience working on high profile cases and he had an excellent reputation within the office as well as among opposing counsel.

4. **Vacancy Announcement No. 04-083-DJ**

Spencer Barasch, selecting official, attested that he wanted a candidate who could be responsible for investigating potential federal securities law violations, summarizing findings and recommending potential action. Barasch indicated that he was looking for a candidate who was smart, possessed the relevant securities experience, and could effectively deal with several layers of bureaucracy. Barasch further attested that in his experience applicants who worked in larger firms and corporations performed better in the SEC office environment than applicants without that type of background. According to Barasch, Complainant came from a solo practice and a small firm background and was therefore, not a good fit for the unit. The selectees, however, all came from large Dallas area law firms and had securities-related investigatory experience. Further, Barasch stated that Complainant had not practiced law for some time and his most recent litigation experience involved legal areas unrelated to securities law. Barasch indicated that in his opinion, litigators such as Complainant, who were more independent, usually did not take well to the intense monitoring and supervision required for the position.

5. **Vacancy Announcement No. 04-088-MB**

Elizabeth King and David Shillman, the selecting officials, attested that they did not recall reviewing Complainant's resume. King and Shillman, however, asserted that they were looking for a candidate who had relevant experience specifically in the area of market oversight, or possessed other related securities experience. Shillman indicated that the two candidates selected had prior experience working in his SEC division, performed excellent work, and he

considered their professional skills and experience as best suited for the position.

6. **Vacancy Announcement No. 04-128-MK**

Levenson, who coordinated the hiring for this position and was a member of the interview panel, stated that he was looking for a candidate who had conducted numerous depositions, argued complex motions in court, had good writing skills, possessed considerable civil litigation experience, preferably in complex commercial fraud cases, and a solid pre-trial experience dealing with complex litigation. Levenson indicated that Complainant's qualifications did not compare to those of the selectees. Specifically, Complainant's writing sample did not reflect in-depth legal analysis and his prior trial experience did not involve the type of complex litigation the SEC is involved in. According to Gordon, selecting official and member of the interview panel, the panel concluded that Complainant's prior trial experience was not relevant to the SEC's case load. For instance, Complainant's prior trial experience involved plaintiff's litigation, construction law and personal injury related work. Finally, Martin, member of the interview panel, attested that he thought Complainant was not a strong candidate for the position because other selectees had more SEC related work experience and exhibited stronger writing skills.

7. **Vacancy Announcement No. 04-060-DP (re-posted as 04-154)**

Deborah Perkins, Human Resources Specialist, indicated that the position in question was only available to current SEC employees. Perkins indicated that Complainant did not make the certification list because at the time, Complainant was not an SEC employee.

8. **Vacancy Announcement No. 03-256-TR**

Barry Rashkover, selecting official, attested that he selected David Markowitz because of

his superior work as attorney and former branch chief at the SEC, including his work related to investigating and securing emergency relief in federal court to halt an on-going securities fraud scheme in 2002. Rashkover also stated that the selectee had a strong securities law background and previously litigated in a large New York law firm.

9. Vacancy Announcement No. 04-069-DC

Romajas, a member of the screening panel, attested that she did not recommend Complainant for an interview because she considered other applicants to be better qualified and indicated that the panel did not discuss Complainant because the panel chose to discuss only their top candidates. According to Romajas, seven candidates were selected, four accepted offers and three declined. Simpson and Romajas both indicated that the seven candidates selected possessed superior qualifications. Simpson and Romajas explained that the selectees were current SEC or Justice Department employees, or litigated in large law firms and had relevant trial experience. Simpson and Romajas further stated that, unlike the selectees, Complainant did not possess any government or current large law firm experience in a pertinent area, factors highly valued in the unit.

10. Vacancy Announcement No. 03-206-DC

Kornblau attested that in his opinion, Complainant was not as qualified for the position as the other applicants. Kornblau stated that Complainant was initially not considered for the position by the panel members because they did not deem him to be a strong candidate. Kornblau explained that one of the panel members referred Complainant's resume to him because he thought it was "unusual." IR, F-2 at 14. After the referral was made, Kornblau spoke to the panel members about the situation and was told by panel member Mejia, among other things, that

he had concerns about the fact that Complainant had not litigated or tried a case in many years and that he had some concerns about Complainant's personality. Kornblau stated that he discussed the issue with Bresnan and that they both decided to go ahead and interview Complainant.

According to Kornblau, based on the comments made by Complainant at the interview, he concluded that he would be unable to work well with other employees, including attorneys with less experience. Kornblau explained that Complainant raised concerns with respect to his possible arrogance in dealing with the junior investigative staff, which is a problem that Kornblau was trying to avoid. Kornblau also stated that he found Complainant to be arrogant "in terms of his own experience, background and abilities" and that he "displayed a sense of entitlement to the position." IR, F-2 at 16-23.

Bresnan attested that he found Complainant to be arrogant and "self-important." IR at 13-16. Bresnan also asserted that he found several factors that weighed negatively against Complainant, such as, lack of prior SEC trial experience; failure to demonstrate that he was able to effectively work with his peers; and the fact that he had not practiced law in several years.

11. Vacancy Announcement No. 03-208-DC

Marc Fagel, SFDO Branch Chief and member of the hiring committee, stated that he reviewed all the forwarded applications and determined that Jina Choi, a former SFDO employee, possessed superior qualifications and professional experience. Fagel further indicated that because he and the selecting official, Robert Mitchell, knew the selectee well, they decided not to interview her. According to the Agency, the SEC has no record that Complainant applied for the position.

12. Vacancy Announcement No. 03-251-DC

The PRO Associate Regional Directors did not interview Complainant for the position. Lee stated that Complainant was not interviewed because during his interview for another PRO position he "stated unequivocally that he was not interested" in the position in question and that "he did not wish to be considered for it." ROI, Tabs f-12 at 16-24, 27-30. According to Lee, because of Complainant's lack of interest in working in the Los Angeles office and in mentoring less experienced attorneys, he concluded that Complainant was not a good match for the Los Angeles office and for the position in question.

13. Vacancy Announcement No. 04-076-DP

Perkins, Human Resources Specialist, stated that Complainant was not included in the certificate of minimally qualified applicants because he did not possess the required international securities experience. Perkins further stated that Complainant's application stated that he had "little, but some actual experience in working international law." ROI, Tab F-21A; F-21D. Moreover, the selectee, Su Ping Lu, had extensive international law and securities experience.

14. The San Francisco District Office Position

Judith Anderson, Senior Special Counsel with the SFDO, stated that the SFDO did not advertise any SK-14 attorney positions during the time period in question. Anderson stated that the position advertised during the time period in question was an SK-13 attorney position that was advertised in the local newspaper and that the Legal Center copied it to its website. Anderson explained that there is a different hiring procedure for positions below the SK-14 level, and that it is less formal. Anderson also stated that the Agency does not have any records of Complainant's application for the position in question.

15. The Northeast Regional Office Position

Bennett Ellenbogen, member of the interview panel, stated that Complainant was considered to be qualified for the position and that his interview was generally positive. Ellenbogen also indicated that Complainant's qualifications were not as outstanding as those of the other candidates. Ellenbogen stated that he had some hesitation in recommending Complainant for the position, but not strong enough to have opposed extending an offer.

Leslie Kazon, member of the interview panel, attested that with respect to selecting Complainant she was "on the fence." ROI, F-30B. Kazon described Complainant as an experienced litigator, smart, effective and results oriented. Kazon, however, was concerned about Complainant's inexperience and lack of knowledge of securities law and "a certain California informality that might bode ill." Id.

16. Vacancy Announcement No. 04-027-DP

Deborah Perkins, the Specialist who handled the announcement, and Jeanine Lauth, Human Resources Director for Corporate Finance, explained that this posting was canceled on February 18, 2004, prior to the February 25, 2004 closing date, because the posting's wording was too vague. According to Perkins and Lauth, the selecting official had no knowledge of who the applicants were because the applications had not yet been referred to the selecting official at the time of the cancellation.

PRETEXT

I find that Complainant was unable to establish that the Agency's proffered reasons for the nonselections were a pretext for unlawful discrimination. In a nonselection case, pretext may be demonstrated where the Complainant's qualifications are shown to be plainly superior to those

of the selectee(s). *See Bauer v. Bailar*, 647 F.2d 1037, 1048 (10th Cir. 1981). To do so, Complainant would have to show that his education and work experience were so plainly superior to those of the selected candidates "as to virtually jump off the page and slap us in the face." *Odom v. Frank*, 3 F.3d 839 (5th Cir. 1993). *See Dobson v. Dep't of Interior*, EEOC No. 01933095 (June 30, 1994). Complainant, however, has failed to proffer evidence to show that his qualifications were clearly superior to those of the selected candidates. In fact, the record shows that Complainant lacked the securities related experience necessary to perform in most of the positions in question. In addition, the record shows that Complainant was not recently involved in litigation or tried cases several years prior to his application for employment with the SEC. Furthermore, unless a candidate can show that he has observably superior qualifications, "[e]mployers generally have broad discretion to set policies and carry out personnel decisions and should not be second guessed be a reviewing authority absent evidence of unlawful motivation." *Holley v. Dep't of Veterans Affairs*, EEOC Request No. 05950842 (November 13, 1997).

Complainant avers with respect to the 03-206-DC Trial Attorney position, that comments made by the selecting official, Kornblau, constitute evidence of age based discrimination. Complainant alleges that at the interview for the position Kornblau stated to him "[y]ou really took a different way of getting here." IR, F-1. Kornblau attested that he did not recall making the comment. The second comment allegedly made by Kornblau was where he asked Complainant why he did not apply to the General Counsel's or Chief Counsel's Office. Complainant argues that this comment shows that Kornblau was looking for someone younger or less experienced than Complainant for the position. Lastly, the third comment allegedly made by

Kornblau was after Complainant was hired by the Agency. According to Complainant, Kornblau stated to a fellow staff member that another person appeared to look younger than his/her twenty-two years of experience. Complainant avers that the comment is indicative of Kornblau's sensitivity to age. I find that the three comments are not indicative of age discrimination. In fact, the third comment was made after Complainant was hired by the Agency and is totally unrelated to the hiring for the position. Even assuming these comments were indicative of age discrimination, they are at most isolated or stray comments and are not legally sufficient to show pretext. *See Woythal v. Tex-Tenn Corp.*, 112 F.3d 243 (6th Cir. 1997) (It is insufficient to support an inference of age discrimination with just personal belief, conjecture and mere speculation.).

DECISION

For the reasons set forth above, I find that Summary Judgment is appropriate and that Complainant failed to produce evidence that could prove that the Agency discriminated against him.

Frances del Toro
Administrative Judge

NOTICE TO THE PARTIES

TO THE AGENCY:

Within forty (40) days of receiving this decision and the hearing record, you are required to issue a final order notifying the complainant whether or not you will fully implement this decision. You should also send a copy of your final order to the Administrative Judge.

Your final order must contain a notice of the complainant's right to appeal to the Office of Federal Operations, the right to file a civil action in a federal district court, the name of the proper defendant in any such lawsuit, the right to request the appointment of counsel and waiver of court costs or fees, and the applicable time limits for such appeal or lawsuit. A copy of EEOC Form 573 (Notice of Appeal/Petition) must be attached to your final order.

If your final order does not fully implement this decision, you must simultaneously file an appeal with the Office of Federal Operations in accordance with 29 C.F.R. 1614.403, and append a copy of your appeal to your final order. See *EEOC Management Directive 110, November 9, 1999, Appendix O. You must also comply with the Interim Relief regulation set forth at 29 C.F.R. § 1614.505.*

TO THE COMPLAINANT:

You may file an appeal with the Commission's Office of Federal Operations when you receive a final order from the agency informing you whether the agency will or will not fully implement this decision. 29 C.F.R. § 1614.110(a). From the time you receive the agency's final order, you will have thirty (30) days to file an appeal. If the agency fails to issue a final order, you have the right to file your own appeal any time after the conclusion of the agency's (40) day period for issuing a final order. *See* EEO MD-110, 9-3. In either case, please attach a copy of this decision with your appeal.

Do not send your appeal to the Administrative Judge. Your appeal must be filed with the Office of Federal Operations at the address set forth below, and you must send a copy of your appeal to the agency at the same time that you file it with the Office of Federal Operations. In or attached to your appeal to the Office of Federal Operations, you must certify the date and method by which you sent a copy of your appeal to the agency.

WHERE TO FILE AN APPEAL:

All appeals to the Commission must be filed by mail, hand delivery or facsimile.

BY MAIL:

Director, Office of Federal Operations

Equal Employment Opportunity Commission
P.O. Box 19848
Washington, D.C. 20036

BY PERSONAL DELIVERY:

Director, Office of Federal Operations
Equal Employment Opportunity Commission
1801 L Street, NW
Washington, D.C. 20507

BY FACSIMILE:

Number: (202) 663-7022

Facsimile transmissions of more than ten (10) pages will not be accepted.

COMPLIANCE WITH AN AGENCY FINAL ACTION

Pursuant to 29 C.F.R. § 1614.504, an agency's final action that has not been the subject of an appeal to the Commission or a civil action is binding on the agency. If the complainant believes that the agency has failed to comply with the terms of this decision, the complainant shall notify the agency's EEO Director, in writing, of the alleged noncompliance within 30 days of when the complainant knew or should have known of the alleged noncompliance. The agency shall resolve the matter and respond to the complainant in writing. If the agency has not responded to the complainant, in writing, or if the complainant is not satisfied with the agency's attempt to resolve the matter, the complainant may appeal to the Commission for a determination of whether the agency has complied with the terms of its final action. The complainant may file such an appeal 35 days after serving the agency with the allegations of non-compliance, but must file an appeal within 30 days of receiving the agency's determination. A copy of the appeal must be served on the agency, and the agency may submit a response to the Commission within 30 days of receiving the notice of appeal.

EQUAL EMPLOYMENT OPPORTUNITY COMMISSION
WASHINGTON FIELD OFFICE
1801 L Street, N.W., Suite 100
Washington, D.C. 20507

Gary Aguirre,	)	
Complainant,	)	EEOC No. 100-2005-00413X
v.	)	Agency No. 155120631-48
William H. Donaldson, Chairman, U.S. Securities and Exchange Commission,	)	**Date: June 14, 2006**
Agency.	)	

ORDER ENTERING JUDGMENT

For the reasons set forth in the enclosed Decision dated June 14, 2006, judgment in the above-captioned matter is hereby entered. A Notice To The Parties explaining their appeal rights is attached.

This office is also enclosing a copy of the hearing record for the Agency and a copy of the transcript for complainant and/or his/her representative.

This office will hold the report of investigation and the complaint file for sixty days, during which time the Agency may arrange for their retrieval. If we do not hear from the Agency within sixty days, we will destroy our copy of these materials.

It is so ORDERED.

For the Commission:

Frances del Toro
Administrative Judge

Enclosures

CERTIFICATE OF SERVICE

For timeliness purposes, it shall be presumed that the parties received the foregoing documents within five (5) calendar days after the date they were sent *via* first class mail. I certify that on June 14, 2006, the foregoing documents were sent *via* first class mail to the following:

Garry T. Aguirre
1528 Corcoran St., N.W.
Washington, D.C. 20009

Juanita C. Hernandez
Office of General Counsel
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-9612

Deborah Balducchi, Director
EEO Office
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-0212

Frances del Toro
Administrative Judge

SEC DIVISION OF ENFORCEMENT
Case Closing Report

Run on 11/30/2006

Case No.: HO-09818 **Case Name:** ELITE INFORMATION GROUP, INC.

The undersigned has been designated by the Director of the Division of Enforcement to exercise delegated authority to terminate and close all investigations authorized by the Commission pursuant to Section 20 of the Securities Act of 1933 [15 U.S.C. 77t], Section 21 of the Securities Exchange Act of 1934 [15 U.S.C. 78u], Section 18 of the Public Utility Holding Company Act of 1935 [15 U.S.C. 79r], Section 42 of the Investment Company Act of 1940 [15 U.S.C. 80a-41], and section 209 of the Investment Advisers Act of 1940 [15 U.S.C. 80b-9].

I hereby close this case, pursuant to delegated authority.

Peter N. Bresnan
Signature

Deputy Director
Title

11/30/06
Date

SEC DIVISION OF ENFORCEMENT
Case Closing Recommendation

Run on 11/30/2006

Case No.: HO-09818 **Case Name:** ELITE INFORMATION GROUP, IN

Case Closing Recommendation Narrative:

PEQUOT CLOSING MEMORANDUM HO-9818

This investigation involved a number of potential federal securities law violations by hedge fund adviser Pequot Capital Management ("Pequot"). In January 2005, the staff obtained a formal order of investigation from the Commission, authorizing the staff to issue subpoenas for documents and witness testimony. Thereafter, the staff issued more than 100 subpoenas requesting documents and took the testimony of 19 individuals (1). The staff also made numerous informal document requests, interviewed six individuals, and participated in two proffer sessions with the Federal Bureau of Investigation and the office of the U.S. Attorney for the Southern District of New York ("Southern District"). The potential violations investigated break down into three major categories: 1) potential insider trading by Pequot in a number of securities, including General Electric ("GE"), Heller Financial ("Heller"), Microsoft Corporation ("Microsoft"), AstraZeneca PLS ("Astra") and Par Pharmaceuticals ("Par"); 2) potential insider trading ahead of PIPE offerings; and 3) potential market manipulation. Each is addressed below.

1) Insider Trading

A.□ Trading ahead of the GE acquisition of Heller

Background: On July 30, 2001, it was publicly announced that GE had acquired Heller, causing a sharp rise in the stock price of Heller and a small decline in the stock price of GE. Pequot began accumulating Heller common stock on Monday July 2, 2001 (2) and started selling short GE stock on July 25, 2001. By closing out these positions after the merger announcement, Pequot realized a profit of nearly $17 million on Heller and approximately $1.9 million on GE (3).

In May 2005, Arthur Samberg, the head of Pequot and the individual responsible for making the trading decisions in both Heller and GE stock, initially testified to the staff that he did not remember why he decided to make the trades, but in subsequent testimony he referred to publicly available information about Heller at the time he made the trades as the basis for placing the Heller trades. However, Samberg acknowledged he was unsure whether he had actually seen this information before he made the trades.

Investigatory Steps: During the summer of 2005, the investigation focused on whether John Mack, who had a personal relationship with Samberg, as well as a number of business relationships with Pequot (4), provided Samberg with inside information about the merger ahead of the public announcement. Emails indicate that Mack and Samberg often communicated during this time and suggest that Mack spoke by telephone with Samberg about a potential investment the night of Friday, June 29, 2001, the business day before Pequot began purchasing Heller, but that the conversation related to an unrelated non-public company. Credit Suisse First Boston ("CSFB"), an investment banking firm and an adviser to Heller in the transaction, hired Mack as its CEO on July 12, 2001, ten days after Pequot began to buy Heller stock. However, counsel for CSFB advised the staff that the CFO of CSFB who met with Mack before Mack joined CSFB did not have deal information on specific pending deals on which CSFB was working. In addition, until March 2001, Mack had been the CEO of Morgan Stanley Inc., which advised GE on the transaction, but records the staff obtained show that Morgan Stanley's first contact with GE regarding a potential transaction with Heller occurred in April 2001, after Mack had already left the firm.

By November 2005, having taken the testimony of Samberg twice, interviewed Samberg's former partner, and obtained email, chronologies, documents, and information regarding Mack from several sources, including CSFB, Morgan Stanley, and Pequot, the staff had found no evidence that Mack had any information about the merger before he joined CSFB on July 12.

Starting in September 2005, the staff focused on identifying other potential tippers who could have provided Samberg information about the GE/Heller transaction. The staff reviewed Samberg's calendar to identify who he met with at the time of Pequot's trading. The staff also obtained from Pequot a list of people hired in 2001 and identified several people on that list who had connections with GE, Heller, or broker dealers involved in the merger. The staff also reviewed the emails obtained from Pequot to identify other potential tippers. The staff then compiled information about each person identified, including searching for relevant documents in the database of emails provided by Pequot.

When this research was complete, the staff evaluated whether to take the testimony of any of these potential tippers. The staff determined that while it had identified people with significant connections to Pequot or Samberg or both, there was no evidence that any knew about the merger in advance of its public announcement. Conversely, those who knew about the deal did not have sufficient connection to Pequot and/or contact with Samberg or Pequot during the relevant time period. Thus, the staff had identified a large number of potential tippers, but no likely tippers. Without any evidence suggesting that any of these people were the tipper, the staff decided taking any of their testimony would not be fruitful. At this same time, around December 2005, the focus of the insider trading case shifted to Microsoft, where it remained until June 2006.

Beginning in June 2006, the staff considered whether to take any additional investigatory steps regarding the GE/Heller trading. Ultimately, the staff took the testimony of six witnesses, and received documents requested by subpoena from each. On July 27, 2006, the staff took the testimony of two CSFB employees, a former CFO and a company lawyer, who were both involved in recruiting Mack. Both denied knowing about the merger before it was publicly announced, let alone telling Mack anything about it, and the documentary evidence did not contradict their denials. On August 1, 2006, the staff took the testimony of Mack. Mack denied knowing about the merger before he became CSFB's CEO in mid-July 2001 and denied having any discussions with Samberg or anyone else at Pequot about the merger before it was announced. He further denied having discussions with anyone at Morgan Stanley in 2001 about GE, Heller, or the GE merger with Heller. On August 17, 2006, the staff took the testimony of the head trader at Pequot who executed the trades in both Heller and GE at Samberg's direction. The head trader testified that he did not recall anything about the trades but that the size of the investment in Heller was not unusual. On September 7, 2006, the staff took the testimony of the head trader's assistant at Pequot at the time of the transactions. The assistant testified that his role at Pequot was largely administrative at that time, and he could not remember any involvement in the GE/Heller trading. On September 8, 2006, the staff took the testimony of an analyst at a brokerage firm who provided analyst coverage on Heller during the relevant time period, appeared to have met with Pequot in June 2001 shortly before Samberg started buying Heller, and went to work at Pequot in early 2002. The analyst denied having any inside information about the merger transaction before it was announced and we have found no evidence to the contrary.

Moreover, although he was scheduled to meet with Pequot in June 2001, it appears from the analyst's personal calendar and testimony that the meeting was cancelled.

Conclusion: The staff has been unable to find any evidence that Pequot had information regarding the merger between GE and Heller before the merger was publicly announced, much less that anyone tipped Pequot or Samberg about the merger in advance of its announcement. The staff's investigation found that it is extremely unlikely that Mack tipped Samberg about the merger between GE and Heller, having found no evidence that Mack knew about the merger before Samberg started purchasing Heller stock. Moreover, emails Samberg sent evidence that Samberg did not even know about Mack joining CSFB until after it was publicly announced (5). It is unlikely that Mack told Samberg about confidential information about the merger if he learned it in connection with being recruited by CSFB, without revealing his impending employment.

There is additional evidence that casts doubt on the possibility that Pequot traded on the basis of non-public information in regard to its trading in GE and Heller. Although Pequot made a substantial profit purchasing Heller ahead of the announced merger, the size of its position in Heller was not atypical for Pequot (6) and Pequot purchased other financial stocks around the same time as the Heller purchases, clearly following the financial sector, not just Heller (7). Moreover, according to its trading records, during 2001 Pequot shorted GE stock on several different occasions (8).

B.□Trading in Microsoft

Background: In April 2001, David Zilkha, a Microsoft employee, went to work as an analyst at Pequot. Even before he officially started work at Pequot, Zilkha started providing Samberg with information about Microsoft by email, including information attributed to Microsoft employees (9). Around the same time, Samberg started buying Microsoft options, which increased in price throughout this period. In emails from this time, Samberg repeatedly gave Zilkha credit for profits Pequot made in trading Microsoft, but did not identify the specific profits or trades.

Investigatory Steps: Beginning in June 2005, and continuing thereafter, the staff provided the Southern District with information about Pequot's trading in Microsoft. In the fall of 2005, the FBI located Zilkha and interviewed him twice. On December 14, 2005 the staff participated in a proffer session with the Southern District with Zilkha. Zilkha proffered that he had obtained information from Microsoft employees and provided it to Samberg, but did not believe the information was either material or confidential.

On January 23, 2006, the staff took Samberg's testimony regarding the Microsoft trading. Samberg testified that he could not remember why he placed the trades, downplayed Zilkha's role in his trading, and denied receiving any material non-public information concerning Microsoft. On February 10, 2006, the staff conducted a second joint proffer with the Southern District with Zilkha. Zilkha proffered the names of the Microsoft employees he believed provided him with information in April 2001. Also during this time, the staff reviewed the results of subpoenas issued to Zilkha and Microsoft.

By March 2006, the staff had focused on two pieces of information Zilkha provided to Samberg by email. The first email, dated April 17, 2001, stated that a Microsoft employee had told Zilkha, a few days before a Microsoft earnings announcement, both that the controller for one of Microsoft's divisions was more "relaxed" about earnings than in previous quarters and that this information suggested the earnings news would be positive. Two days later, on April 19, Samberg purchased Microsoft call options and sold short Microsoft put options. Later that day and after the market close, Microsoft announced that its earnings had significantly exceeded analysts' expectations. The following day, April 20, Pequot sold its call options and closed out its short position in the put options, realizing a profit of approximately $1.6 million The second email, dated April 27, 2001, stated that a Microsoft employee had told Zilkha that a rumor regarding a delay in the release of a Microsoft product was untrue. The next trading day, April 30, Samberg purchased call options in Microsoft. Two days later, May 2, Microsoft stock rose and Pequot sold the purchased options, realizing a profit of approximately $530,000.

The staff interviewed by telephone the person Zilkha identified as the source of the first tip, but she denied even knowing Zilkha, and told the staff she would never have told anyone that type of information. The FBI was unable to locate the alleged source of the second tip, who had left Microsoft and was believed to be living in Brazil. The staff interviewed two other Microsoft employees identified by Zilkha as his sources for other information he provided to Samberg around the time Pequot traded in Microsoft, and both categorically denied providing him with any information. At the end of March, the staff obtained four month tolling agreements from Pequot, Samberg and Zilkha.

The tolling agreement applied to all matters under investigation, including the Microsoft transactions.

In April 2006 the staff learned more about the product delay that was the subject of the second tip. First, the staff learned that other events, not related to the product delay rumor, caused a sharp increase in Microsoft's share price a few days after Zilkha provided the information to Samberg. Moreover, the staff learned that information relevant to both the earnings announcement and the product delay had been provided to Pequot by Goldman Sachs ("Goldman") in advance of Goldman publishing the information and before Pequot's trades. To examine whether Goldman's actions were themselves improper, the staff obtained information from Goldman and in early June took the testimony of two Goldman employees. Both told the staff that during this time they regularly provided research information to Goldman customers in advance of publishing this information, and that Goldman policy explicitly allowed this practice.

Conclusion: While the emails from Samberg praising Zilkha for his work on Microsoft suggest that Samberg may have used information from Zilkha to trade in Microsoft options, there is insufficient evidence to bring a case based on this conduct. The staff could only identify two tips that were related to profitable trading by Pequot in Microsoft. The first, the information about a controller being relaxed is vague, and the alleged source denies providing the information to Zilkha. Moreover, the information Pequot received from Goldman around the same time as Zilkha's tip about the same earnings announcement gives Samberg a justification for his trading. The second, the information about the product delay, did not drive the rise in Microsoft's stock price. Finally, the staff determined there was nothing illegal about Goldman giving its clients, including Pequot, information it developed internally, before that information was publicly disseminated.

□C.ATrading in AstraZeneca and Par Pharmaceutical

Background: The staff also investigated Pequot's trading in AstraZeneca ("Astra") and Par Pharmaceutical ("Par"). On October 11, 2002, a federal district court issued an opinion upholding patents of Astra and declaring that Par infringed upon those patents. The court decision caused the shares of Astra to increase in price by 12% and the shares of Par to decrease in price by 21%. The staff's initial inquiry into the trading indicated that shortly before the court announced its decision, Pequot reversed its trading pattern in both stocks.

Investigatory Steps: The staff learned that the Southern District had conducted an investigation regarding whether a judicial law clerk had leaked the outcome of the patent case. That investigation had ended because the Southern District was unable to identify anyone who profited from the tip or whether there even was a tip. The staff reviewed the formal written statements prepared by the FBI from that investigation and reviewed Pequot emails but was unable to find any links between Pequot and the people interviewed in that investigation.

In November 2005, the staff examined Pequot's trading records and determined that the staff's initial inquiry presented an incomplete and misleading picture of Pequot's trading in the stocks of Astra and Par. Although from August 23, 2002 through September 25, 2002, Pequot did reverse a significant portion (approximately $18 million) of a short position it had established in Astra, Pequot was adding to its position in Par during part of the same time period (September 6 through September 11), purchasing approximately 200,000 shares of Par common for approximately $4.8 million. Pequot did not begin to reverse its long position in Par until September 27, 2002, after it had stopped reversing its Astra short position. Moreover, on October 11, 2002, the date the court decision was made public, Pequot still held a long position in Par (close to $2 million) and a significant short position in Astra (more than $6 million) (10). Both of these positions proved to be losing positions and it would have made no economic sense to maintain either of them if Pequot had inside information regarding the upcoming decision in the patent case. Finally, during 2002, from February on, Pequot traded in and out of Par and Astra.

Conclusion: It seems unlikely that Pequot had inside information about the court decision because it made investment decisions contrary to that information in the weeks leading up to the decision. Accordingly, we stopped pursuing this aspect of the investigation.

2)□Private Investments in Public Equities ("PIPES")

Background: This aspect of the investigation concerned potential insider trading by Pequot in the common stock of companies issuing PIPES ahead of the public announcement of the PIPES. The public announcement of a PIPE often causes the price of issuer's stock price to fall, making it advantageous to sell short the stock of companies who issue PIPE securities before the transactions are publicly announced. Such trading may violate the law against insider trading. The Pequot PIPE investigation was initially opened by the SEC's Northeast Regional Office ("NERO") but during the fall of 2005 transferred to the Washington office for efficiency purposes.

Investigatory Steps: Initially, the staff evaluated and reviewed Pequot's response to a subpoena issued by NERO with respect to Pequot's PIPE transactions. The staff then examined Pequot's trading activity in 101 PIPE transactions over a four year period beginning in 2001. The staff specifically examined Pequot's trading data to determine whether Pequot sold short prior to the public announcement of any PIPE it purchased. Of the 101 PIPES purchased by Pequot, the staff found that Pequot shorted ahead of the public announcements of 11, but the stock prices for 8 of the 11 did not decline materially after the announcements of the PIPE. For the three remaining issuers, Pequot sold short the issuer ahead of the public announcement but in all three cases its short selling activity occurred more than seven weeks before the PIPE was publicly announced. This would make it difficult to show that the short selling was based on material nonpublic information concerning the PIPE offering, the trading having occurred so far in advance of the public announcement of the offering (11).

Conclusion: Because the staff was unable to find instances where Pequot short sold shares within seven weeks, ahead of a public announcement of a PIPE offering in which they participated in and in which there was a material decline in the share price of the issuer, the staff stopped pursuing this aspect of the investigation.

3)□Market Manipulation

Background: During the fall of 2005 the staff began to closely evaluate two separate but similar trading practices engaged in by Pequot. The first involved Pequot's selling shares it received in numerous initial public offerings ("IPOs") and simultaneously purchasing the same number of shares soon after the shares began trading in the open market. This trading suggested that Pequot may have engaged in a manipulative trading practice because it appeared as if the trades did not involve a change in beneficial ownership (wash sales)(12). The second involved Pequot executing an agency cross trade, one side of which was a short sale and the other side was a purchase of the same security. The short sale and the buy were for the same number of shares and price and were executed simultaneously. The trade was reported as an agency cross; however, the Pequot trade blotter shows that the same Pequot funds executed both the sales and the purchases, causing no change in beneficial ownership. Again this trading was suggestive of manipulative trading.

SEC DIVISION OF ENFORCEMENT
Case Closing Recommendation

Run on 11/30/2006

Investigatory Steps: The staff requested a written explanation from Pequot regarding their apparent wash sale trading and sent a follow-up subpoena to Pequot for additional information on the trading practices after receiving Pequot's explanation. Pequot provided an extensive written response explaining that its trading occurred to transfer beneficial ownership of the stocks acquired in IPOs from one class of fund investors (those eligible to participate in the offering) to another class of investors (those ineligible to participate), and was specifically sanctioned under an NASD interpretation. This explanation was consistent with Samberg's testimony concerning this practice. The staff then reviewed Pequot's supporting documentation and certifications concerning Pequot's compliance with the NASD rule and found that the documentation was consistent with Pequot's assertion that it was transferring beneficial ownership of the securities from one class of investors to another.

The staff met several times with staff from the Division of Market Regulation ("Market Regulation") concerning whether Pequot's agency cross trades violated the federal securities laws. Market Regulation recommended that the staff first evaluate the market impact from Pequot's cross trading (13). The staff then analyzed the market impact from Pequot's cross trading activity in 92 securities -- 5 New York Stock Exchange issuers; 7 American Stock Exchange issuers; 22 Nasdaq National Market System issuers; 29 Nasdaq Small Cap issuers; and 29 Over the Counter Bulletin Board issuers -- and found that there was no significant impact on both the market price and volume for any of the stocks by the cross trading activity, making it difficult to prove market manipulation by Pequot.

Conclusion: For the reasons discussed above, the staff did not pursue further the market manipulation aspects of the investigation.

There are presently outstanding FOIA requests for this matter, in addition there was a denial of a request on November 1, 2006.
All files related to the case have been retained.

Termination letters are appropriate in this case and will be sent to Pequot Capital Management, Arthur Samberg, and John Mack.

The Branch Chief, Robert B. Hanson and the Assistant Director, Mark Kreitman, have reviewed and approved this form.

Footnotes:

(1) Pequot alone made available approximately 19.8 million pages of electronic email and produced 161,500 pages of hard copy documents. The staff also issued numerous document subpoenas to broker dealers, issuers, individuals, and service providers. The hard copy documents collected in the investigation fill approximately 95 banker boxes.
(2) Pequot's brokerage firm used the name "Indian Capital Management" in its internal system to refer to these trades. Pequot employees were not aware that this was done, and neither Pequot nor the brokerage firm where the trades were placed was able to provide any explanation as to why the trades were not placed using the Pequot name. The staff did not discover any reason for the use of this name, nor, since the name was used internally by the brokerage firm, any advantage Pequot derived from its use.
(3) Pequot closed out its GE short position approximately two weeks after the merger announcement. Had it closed out the position the day after the merger announcement, its profit on the GE trades would have been approximately $900,000.
(4) Mack, his wife, and a foundation Mack controlled made significant investments in a number of Pequot funds. Mack also participated with Pequot in at least two private company investments in 2001.
(5) Similarly, email traffic between Samberg and his wife evidences that Samberg did not know that Mack was going to resign from Morgan Stanley until after the resignation was publicly announced in January 2001. Approximately two months after the public announcement, Mack officially left Morgan Stanley.
(6) Pequot has publicly stated that during the period of the staff's review, it conducted over 136,000 trades. Moreover, the size of the position Pequot accumulated in Heller was equal to approximately one and a half percent of the total assets Samberg traded in 2001. Pequot records reflect that in 2001 Pequot took positions in numerous companies in percentages approximately equal to or greater than that amount.
(7) For example, on July 2, 2001, Pequot purchased 220,900 shares of stock in American Express Inc. On July 11, 2001, Pequot had trading positions in at least twelve different financial stocks.
(8) For example, from September 26 through October 5, 2001, Pequot established a short position in GE of approximately $30 million.
(9) Zilkha used tne name of only one of these individuals in emails, the remaining individuals were only identified by their generic position at Microsoft.
(10) The staff initially believed that Pequot failed to list its holding of 213,000 Astra shares on its Form 13F filed for the period ended September 30, 2002. However, Pequot trading records show that Pequot purchased Astra shares to cover existing short positions, but did not in fact own any Astra shares as of September 30, 2002.
(11) Because the staff did not find any instances in which Pequot traded on material nonpublic information ahead of the PIPE offerings, it did not evaluate whether Pequot breached a duty of trust or confidence with respect to its trading ahead of the offerings.
(12) Section 9(a)(1) of the Exchange Act prohibits certain manipulative practices, including wash sales and matched orders, when such transactions are done for the purpose of creating the false or misleading appearance of active trading in a security listed on a national securities exchange, or a false or misleading appearance with respect to the market for any such security. Section 9(a)(2) prohibits the manipulation of prices of securities listed for trading on a national exchange, and makes it unlawful for a person to engage in a series of transactions that creates actual or apparent activity or depresses the stock's price when done for the purpose of inducing others to buy or sell the security. Manipulative practices under Section 9(a) also violate Section 10(b) and Rule 10b-5 of the Exchange Act for both exchange-listed securities and over-the-counter securities. To establish a violation of Sections 9(a)(1) and 9(a)(2) specific manipulative intent must be proven.
(13) The Supreme Court has stated that manipulation "connotes intentional or willful conduct designed to defraud investors by controlling or artificially affecting the price of securities." Ernst & Ernst v. Hochfelder, 425 U.S. 185, 199 (1976) (emphasis added).

SEC DIVISION OF ENFORCEMENT
Case Closing Recommendation

Run on 11/30/2006

Representations

A. FOIA

After consultation with FOIA/PA Branch, it was determined that the FOIA status of these case files is as follows (Check one):

- ☐ No FOIA concerns exist as of _____.
- ☐ FOIA request filed on _____ is pending without decision. Category F Material will be retired with balance of file.
- ☒ FOIA request was denied on 11/1/06. Category F Material will be marked to be discarded six years after decision date.
- ☐ FOIA determination was appealed and decided on _____. Category F Material will be marked to be discarded six years after decision date.

B. Category E Records

- ☐ The files contain no Category E Records.
- ☒ A copy of the index for all designated Category E (Miscellaneous) Records is attached. All records for this case have been maintained by the General Counsel's office and the Division of Enforcement.

C. Termination Letters

- ☐ No termination letters are required.
- ☒ Termination letters will be sent to the parties listed in the case narrative.

D.

- The files relating to this case have been prepared for disposition in accordance with procedure in the memorandum, *Disposition of Records Upon the Closing of Cases* (August 20, 1993).
- Except as set forth, no access requests or protective orders are outstanding: _____
- No objection is made to eventual destruction of the files. [Consult with the Office of Chief Counsel concerning designation of any case files for Archival retention].

Based on the representations made above, the undersigned recommend(s) the closing of this case.

Signatures:

Attorney	Date 11/30/06
Branch Chief	Date 11/30/06
Asst Dir/Asst Reg Adm/ Asst Dist Adm	Date

Attach a copy of the Case Summary Report and submit this form to the Office of Chief Counsel.

SEC DIVISION OF ENFORCEMENT
Investigation Summary

Inv. No:	HO-09818-A	**Inv. Name:**	TRADING IN CERTAIN SECUF
Branch Chief:	HANSON, ROBERT B	202-551-4497	40423
Primary Staff:	EICHNER, JAMES A	202-551-4928	40421
Status:	Closed	**Open Date:**	01/14/2004
Last Event:	11/30/2006	MUI/Investigation Status Change	
Formal Order Date:	01/06/2005	**Close Date:**	11/30/2006

Possible Violations:

34 §10B	Fraud
34 §14E	Tender Offer Fraud
34 R10B-05	Fraud
34 R14E-03	Tender Offer Insider Trading

Origins:
REFRD FROM SRO-NOT V
MKTSURV

Keywords:
FRAUD IN OFFER/SALE/PURCHASE

Trading Markets:
NASDAQ

Types of Security:
COMMON STOCK

MUI:	**MUI Case No.:** MHO-09818	**MUI Case Name:**	ELITE INFORMATION GROUP, INC.
	MUI Status: Closed/Investigation Opened	**MUI Open Date:**	11/14/2003
		MUI Close Date:	01/14/2004