

**Insider  
Trading:  
2009  
Review**

By any measure, 2009 was a big year for insider trading. News of large insider trading rings involving high-profile individuals and millions of dollars dominated the headlines. A simple Google search for “insider trading” and “2009” generates more than 2.2 million hits. The same search for “2008” returns nearly a million fewer hits. Not since the Ivan Boesky-related scandals of the 1980s has insider trading commanded as much attention. And just in time, Gordon Gekko is back in Oliver Stone’s sequel to *Wall Street*.

Despite the renewed attention, insider trading—trading while in possession of material nonpublic information in breach of a duty—is not a new crime. Information has always been and remains a precious commodity on Wall Street and on Main Street. But 2009 saw some new twists on the old theme: wiretaps, credit default swaps, hedge funds, SEC cooperation agreements, and rapid fire subpoenas were just a few of the somewhat novel aspects of insider trading cases in 2009.

## Overview of Insider Trading Law

Trading by insiders includes both legal and illegal conduct. The legal version occurs when a corporate insider buys and sells the stock of his or her own company and discloses such transaction to the SEC. Legal trading also includes, for example, someone trading on information he or she overheard between strangers sitting on a train or when the information was obtained through a non-confidential business relationship. The illegal version occurs when a person buys or sells a security in breach of a fiduciary duty or relationship of trust while in possession of material, nonpublic information.

Two primary theories of insider trading have emerged over time. First, under the “classical” theory, the Exchange Act’s anti-fraud provisions apply to prevent corporate “insiders” from trading on secret information taken from the company in violation of the insiders’ fiduciary duty to the company and its shareholders.<sup>1</sup> Second, the “misappropriation” theory applies to prevent trading by a person who misappropriates information from a party to whom he or she owes a fiduciary duty—such as the duty owed by employee to employer or by lawyer to client.<sup>2</sup>

In 2000, the SEC adopted Rule 10b5-2 in an attempt to extend the boundaries of fiduciary duties for purposes of insider trading cases brought under the misappropriation theory.<sup>3</sup> Rule 10b5-2 provides “a non-exclusive definition of circumstances in which a person has a duty of trust or confidence for purposes of the ‘misappropriation’ theory of insider trading under Section 10(b) of the Exchange Act and Rule 10b-5.”<sup>4</sup> The Rule provides that “a ‘duty of trust or confidence’ exists in the following circumstances,” among others:

- (1) Whenever a person agrees to maintain information in confidence;
- (2) Whenever the person communicating the material nonpublic information and the person to whom it is communicated have a history, pattern, or practice of sharing confidences, such that the recipient of the information knows or reasonably should know that the person communicating

the material nonpublic information expects that the recipient will maintain its confidentiality; or

- (3) Whenever a person receives or obtains material nonpublic information from his or her spouse, parent, child, or sibling.<sup>5</sup>

The rule also provides an affirmative defense where the defendant is able to establish that the facts and circumstances of the family relationship demonstrate no reasonable expectation of confidentiality.<sup>6</sup>

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Under either theory, the law holds both the insider having the information (the “tipper”) and the one receiving the information (the “tippee”) equally liable, as long as the tippee has knowledge of the tipper’s breach of duty. While the interpretation of the scope and applicability of Section 10(b) and Rule 10b-5 to insider trading is constantly evolving, and 2009 saw some developments in this area (described below), the anti-fraud provisions provide powerful and flexible tools to address efforts to capitalize on nonpublic information.

Section 14(e) of the Exchange Act and Rule 14e-3 also prohibit insider trading in the limited context of tender offers. Rule 14e-3 defines “fraudulent, deceptive, or manipulative” as the purchase or

sale of a security by *any* person with material information about a tender offer that he or she knows or has reason to know is nonpublic and has been acquired directly or indirectly from the tender offeror, the target, or any person acting on their behalf, unless the information and its source are publicly disclosed before the trade.<sup>7</sup> Under Rule 14e-3, liability attaches regardless of a pre-existing relationship of trust and confidence. Rule 14e-3 creates a “parity of information” rule in the context of a tender offer. Any person – not just insiders – with material information about a tender offer must either refrain from trading or publicly disclose the information.

While most insider trading cases involve the purchase or sale of equity instruments (such as common stock or call or put options) or debt instruments (such as bonds), civil or criminal sanctions apply to insider trading in connection with any “securities.” What constitutes a security is not always clear, especially in the context of novel financial products. At least with respect to security-based swap agreements, Congress has made clear that they are covered under anti-fraud statutes. In 2000, Congress passed the Commodity Futures Modernization Act (“CFMA”), which amended Section 10(b) of the Exchange Act to extend the rules promulgated by the SEC under Section 10(b) to prohibit fraud, manipulation, and insider trading, and cases decided under Section 10(b), to “security-based swap agreement[s] (as defined in section 206B of the Gramm-Leach-Bliley Act).”<sup>8</sup> Section 206B of the Gramm-Leach-Bliley Act defines a “security-based swap agreement” as a “swap

agreement . . . of which a material term is based on the price, yield, value, or volatility of any security or any group or index of securities, or any interest therein.”<sup>9</sup>

The consequences of being found liable for insider trading can be severe. Individuals convicted of criminal insider trading can face up to 20 years imprisonment per violation, criminal forfeiture and fines up to \$5,000,000 or twice the gain from the offense. A successful civil action by the SEC may lead to disgorgement of profits and a penalty not to exceed the greater of \$1,000,000, or three times the amount of the profit gained or loss avoided. In addition, individuals can

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be barred from serving as an officer or director of a public company, or in the case of licensed professionals such as attorneys and accountants, from serving in their professional capacity before the Commission. It is also not uncommon for individuals or companies involved with government insider trading actions to face private suits.

Section 20A of the Exchange Act gives contemporaneous traders a private right of action to bring a civil lawsuit against anyone trading while

in possession of material nonpublic information.<sup>10</sup> Although Section 20A gives an express cause of action for insider trading, the limited application and recovery afforded under the statute make Section 20A an unpopular choice for private litigants. Rather, most private securities claims for insider trading are brought under the implied rights of action found in Rule 10b-5 and Rule 14e-3.

## 2009 Enforcement Activity

In 2009, the SEC filed 35 new insider trading actions and the DOJ brought criminal charges involving insider trading against 31 individuals. In addition, DOJ has reported that there are numerous open investigations.<sup>11</sup> As Associate Director of the SEC’s Division of Enforcement, Scott Friestad, recently indicated, there are many insider trading cases already in the pipeline.<sup>12</sup>

Insider trading cases in 2009 were primarily remarkable in their size. As a result of long-running investigations, the government brought big cases with multiple defendants and outsized alleged profits. More than one-third of the SEC’s 2009 cases – 13 of 35 – involved three or more defendants. And 9 of the SEC’s cases alleged illegal profits or losses avoided of \$4 million or more. Moreover, Wall Street dominated last year’s insider trading enforcement cases: 8 of the large SEC cases involved an investment professional in some way and more than half of these 8 cases involved hedge funds.

Insider trading cases in 2009 also continued to reflect existing enforcement trends. With the increasingly globalized economy, securities fraud and enforcement expanded overseas: 6 enforcement

matters involved international aspects. Similarly, “gatekeepers” continue to play a prominent role in corporate compliance – and government enforcement cases. For example, 7 of the insider trading cases in 2009 involved attorneys.

### Highlights of Government Enforcement Efforts

By all accounts, 2009 was a blockbuster year for insider trading enforcement actions and criminal prosecutions. Many of the individuals charged and companies implicated were high-profile members of the financial and business communities.

#### A. High-Profile Cases With High-Dollar Values

No case exemplifies this trend more than *U.S. v. Rajaratnam, et al.*<sup>13</sup> and the parallel SEC enforcement action, *SEC v. Galleon Management, LP, et al.*<sup>14</sup> The *Galleon* case involves allegations of widespread insider

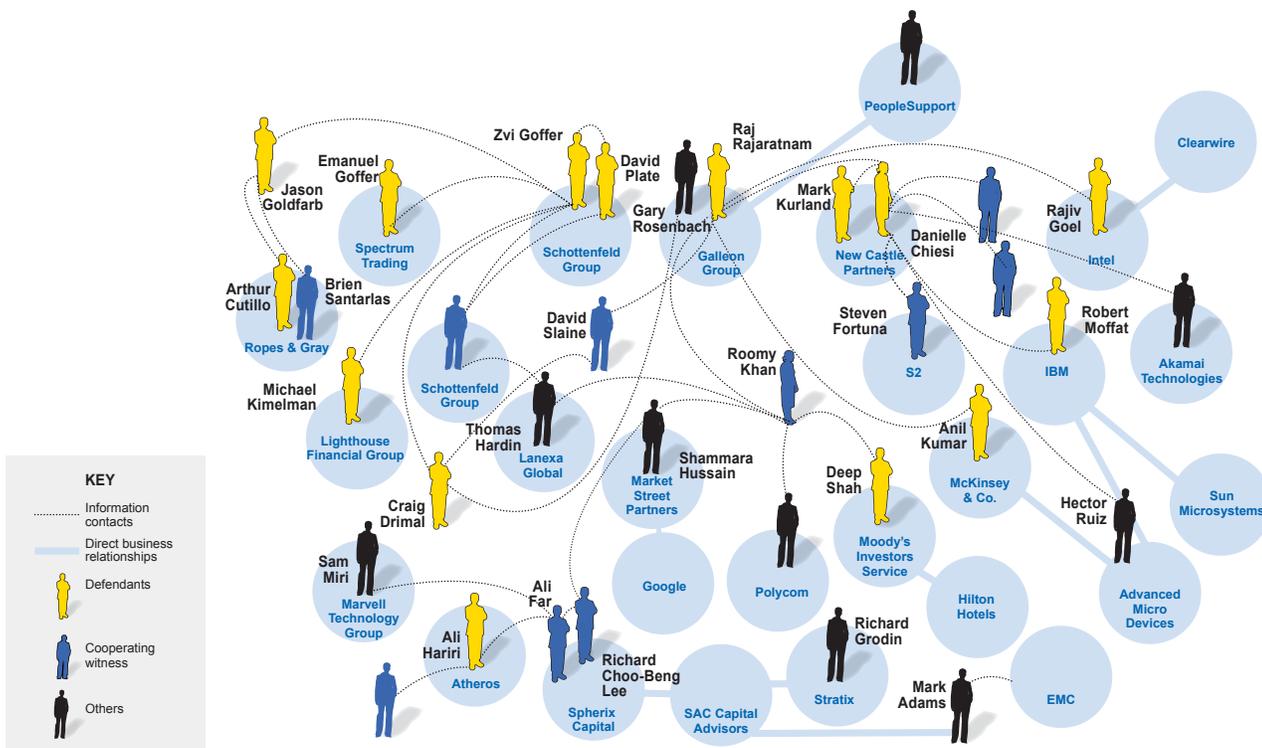
trading at several hedge funds including Galleon Management, LP – a formerly multi-billion dollar hedge fund founded and controlled by Raj Rajaratnam – New Castle Funds LLC, Spherix Capital LLC and S2 Capital Management, LP. The alleged sources of inside information include Rajiv Goel, a managing director at Intel Corporation; Anil Kumar, a former director at McKinsey & Co.; Robert Moffat, a former senior executive at IBM; as well as executives and consultants at other well known companies.

Public reports of the trading network show a complicated web of overlapping relationships and information sharing. See graph below.

The DOJ's most recent court filings allege that the scheme generated more than \$49 million in illicit profits or losses avoided. Thus far, the DOJ has charged more than 20 individuals, 9 of whom have pleaded

guilty. The SEC charged more than 26 defendants. Thus far, two entities have ceased doing business and were dismissed from the SEC action, and two other defendants have agreed with the SEC to the entry of an order (1) enjoining further securities law violations, (2) ordering them, jointly and severally, to pay more than \$1.4 million in disgorgement, and (3) ordering them, jointly and severally, to pay a civil penalty of more than \$667,000. Mr. Rajaratnam and Danielle Chiesi, a former consultant at New Castle Partners accused of providing inside information to Mr. Rajaratnam, both entered pleas of not guilty in the criminal case. The DOJ and SEC cases are ongoing.

Each week brings news of a new cooperating witness for the DOJ including: key information conduit Roomy Khan; Ali Far and Richard Choo Beng Lee of Spherix Capital; former McKinsey director Anil Kumar;



Gautham Shankar of the Schottenfeld Group; Rajiv Goel, formerly of Intel Capital; and many more. Mark Kurland, a principal of New Castle Partners, also entered a plea of guilty in the criminal case, but according to published reports has not agreed to cooperate with prosecutors.<sup>16</sup>

David Slaine, a former hedge fund portfolio manager at Chelsey Capital, is also reportedly cooperating in the *Galleon* criminal probe.<sup>17</sup> While Mr. Slaine has not been charged with insider trading relating to *Galleon*, he pleaded guilty in December 2009 to charges relating to an insider trading scheme with Erik Franklin, a former analyst at Chelsey Capital, to trade on inside information about upcoming investment bank analyst upgrades or downgrades that Franklin allegedly received from Mitchel S. Guttenberg, a former institutional client manager at a large investment bank. Mr. Slaine's plea was unsealed in February 2010.

In a separate but allegedly related case, a grand jury has indicted Zvi Goffer, Emanuel Goffer, Jason Goldfarb, Arthur Cutillo, Craig Drimal, David Plate, and Michael Kimelman; and all seven defendants have entered pleas of not guilty.<sup>18</sup> Brien Santarlas, who was also charged, has entered a plea of guilty and is awaiting sentencing.<sup>19</sup> In parallel proceedings, the SEC also brought an enforcement action against Mr. Santarlas and a separate enforcement action against the Goffers and Messrs. Goldfarb, Cutillo, Drimal, Plate, and Kimelman, as well as Gautham Shankar and Schottenfeld Group, LLC.<sup>20</sup> Mr. Shankar, who had been previously charged by the DOJ and connection with the *Galleon* case, entered a plea of guilty in November 2009 and is cooperating with the

authorities.<sup>21</sup> The SEC alleges that Zvi Goffer—known within the ring as “Octopussy” due to his reputation for having multiple sources of inside information—and attorney Jason Goldfarb paid tens of thousands of dollars for tips from attorneys Arthur Cutillo and Brien Santarlas. The SEC also alleges a separate scheme involving insider trading by Mr. Drimal, who worked at Galleon's office but was not employed by Galleon, Zvi Goffer and Mr. Shankar of the Schottenfeld Group, Emanuel Goffer and Mr. Plate of Spectrum Trading, and Mr. Kimelman of Lighthouse Financial.

In addition to the *Galleon* case, the DOJ and the SEC have also brought several other significant insider trading cases in 2009. For example, *SEC v. Tang* involved \$8 million in alleged profits or avoided losses and seven defendants who were executives at a private equity fund and a venture capital fund.<sup>22</sup> *SEC v. Stephanou, et al.* involved allegations of more than \$11 million in illegal profits and losses avoided as a result of alleged insider trading by seven defendants, including M&A professionals and a hedge fund portfolio manager.<sup>23</sup> The DOJ separately brought a criminal case against two of the defendants in this case. *SEC v. Saleh* involved allegations of illicit profits in excess of \$8 million as a result of alleged insider trading with call option contracts of Perot Systems Corp.<sup>24</sup>

And while the high-dollar cases grabbed the most attention, 2009 showed that the government still continues to pursue low-dollar insider trading cases as well—especially if they involve alleged insider trading by attorneys or a company's executives. For example, in *SEC v. Mahler*, the SEC brought

an enforcement action against a corporate attorney at a prominent law firm, who allegedly used information that she had misappropriated from her firm's client to gain \$5,800 in illicit trading profits.<sup>25</sup> In the related criminal case, Ms. Mahler has since entered a guilty plea to making false statements and is awaiting sentencing.<sup>26</sup>

## B. Focus on Previously Unregulated Activities

Another significant development in 2009 was the SEC's and DOJ's focus on previously unregulated industries and financial activities. As noted, many of the 2009 insider trading actions involved hedge funds, including most of the high-profile cases like *Galleon*. After years of high returns for many hedge funds and little to no regulatory oversight of hedge funds, the government seems to be taking a hard look at whether smart investing, or illegal advantage, drove that growth. Indeed, the government's increasing attention to hedge funds was highlighted in public comments by George Canellos, the SEC's recently appointed New York Regional Director, who cautioned, “[i]nvestment management, and especially hedge funds, is a big area of emphasis.”<sup>27</sup> Reports indicate that in the last two months of 2009 alone, the SEC issued more than three dozen subpoenas to various hedge funds.<sup>28</sup>

In *SEC v. Rorech, et al.*, the SEC filed its first-ever insider trading case involving credit default swaps (“CDS”).<sup>29</sup> The SEC's case surprised—and to some extent alarmed—the financial industry as this type of investment instrument was considered to be outside the purview of insider trading laws. A credit default

swap is a type of credit derivative contract where the buyer receives credit protection, and the seller of the swap guarantees the creditworthiness of the referenced instrument, such as a bond. The seller of a CDS agrees to pay the buyer a specific sum of money if a credit event occurs (e.g., default of the underlying instrument or the referenced company's bankruptcy or restructuring). In exchange, the buyer agrees to make premium payments to the seller during the course of the contract. As discussed above, Section 10(b) applies to swap agreements, such as CDS, when a material term of the swap agreement is based on the price, yield, value, or volatility of any security or any group or index of securities, or any interest therein.

The SEC alleged that Jon-Paul Rorech, a bond and CDS salesperson, tipped Renato Negrin, a portfolio manager for Millennium Partners, L.P., a hedge fund investment advisor, about a change in a company's bond offering, which Negrin used to buy CDS that were referenced to that company's bonds. The defendants moved for judgment on the pleadings, arguing that the CDS at issue were not "security-based" because the material terms of the CDS were not based on the price, yield, value, or volatility of the referenced bonds. The SEC alleged that the CDS's price term was indeed based on such factors, and the court held that the defendants failed to show that the SEC's allegation that the CDS were security-based swap agreements was implausible. The court held that whether the price, or any other material term, of the CDS were actually based on the referenced bonds raises questions of fact that are not properly addressed on a motion for judgment on the pleadings.<sup>30</sup>

Enforcement officials stated that "CDS may still be obscure to the

average individual investor, but there is nothing obscure about fraudulently trading with an unfair advantage." In 2010 and beyond, according to Kay Lackey, Associate Regional Director of the SEC's New York Office, the SEC will continue to look "at a broad array of financial products associated with the financial crisis, including credit default swaps."<sup>31</sup> Indeed, as discussed below, the SEC Enforcement Division recently created a New Products Unit that will focus on CDS, as well as other complex off-market financial products.

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The *Rorech* case made clear that insider trading is not just for stocks. While this is not a new concept,<sup>32</sup> *Rorech* serves to teach a lesson that seemed to have been forgotten. Insider trading enforcement extends across the wide spectrum of financial products from common instruments, like exchange-traded options, to over-the-counter derivatives, like credit default swaps. Firms and individuals, thus, cannot assume they can escape detection by trading away from exchanges. Compliance efforts within hedge funds and institutional investors should likewise include the "off-market investment groups."

### C. Aggressive Enforcement

What 2009 made very clear was that DOJ and SEC intended to pursue insider trading cases

aggressively. In 2009, the government brought multiple parallel criminal and civil cases. And contrary to prior practice, 2009 saw fewer SEC civil cases being stayed awaiting resolution of the criminal case, leaving defendants to proceed on parallel tracks. (Of course, despite the Fifth Amendment waiver dilemma, many criminal defendants prefer having the parallel SEC enforcement action as a means to obtain broader and earlier discovery of the government's evidence in the criminal case.) Both agencies also sought to impose harsh sanctions on insider trading defendants. Furthermore, the SEC sought to cast a wider net by expanding the scope of insider trading law, albeit with mixed success.

#### 1. Parallel proceedings

In 2009, the DOJ and SEC filed parallel criminal and civil insider trading cases in seven matters, against 30 defendants. These matters involved particularly large dollar amounts and/or complex trading schemes. For example, *SEC v. Cutillo, et al.* and *SEC v. Santarlas*, discussed above, allegedly involved a serial insider trading ring which made more than \$20 million in profits, and the parallel criminal action has resulted in one guilty plea and the indictment of seven other individuals. Additionally, in *SEC v. Grmovsek*, the defendant faced not only U.S. civil and criminal charges, but also civil and criminal charges in Canada.<sup>33</sup> The *Grmovsek* investigation was conducted jointly by the FBI, SEC, the Ontario Securities Commission, the Royal Canadian Mounted Police, and the Ministry of the Attorney General (Ontario) Stock Fraud and Criminal Asset

Forfeiture Units. In connection with his guilty plea in the United States, Mr. Grmovsek was sentenced to time served, after having been sentenced to 39 months imprisonment by a Canadian court. International parallel proceedings likely will become more common as governmental agencies increasingly cooperate with their counterparts abroad.

Significant ramifications result from parallel civil and criminal proceedings. In an SEC civil case, unlike in a criminal case, defendants may obtain extensive pre-trial discovery, including deposing key government witnesses. This provides defendants with a valuable chance to preview, and limit, the government's criminal case. Yet in an SEC civil case, unlike in a criminal case, the Court may instruct jurors to draw an adverse inference from a defendant's exercise of his or her Fifth Amendment right to refuse to testify. A defendant invoking these rights in anticipation of the criminal case thus faces the likelihood of an adverse civil judgment. This risk is often obviated by having the criminal case proceed on a faster track, both due to the requirements of the Speedy Trial Act and the interests of judicial efficiency, given that a criminal conviction will have a preclusive effect on liability in the parallel civil case.

An additional wrinkle arose in early 2010 in the *Galleon* case. The DOJ largely built its case through the use of court-authorized wiretaps to record telephone conversations of the defendants. Under the rules of criminal discovery, the defendants are entitled to those recordings. Under the prohibitions in the federal wiretap statute, however, the SEC cannot obtain the recordings from the DOJ.

The SEC, therefore, sought the tapes from the defendants through civil discovery. Defendants opposed the request in the civil and criminal cases, which are assigned to different judges in the Southern District of New York.

Judge Rakoff, presiding over the SEC case, ordered defendants to turn over the tapes to the SEC. As Judge Rakoff explained, "the notion that only one party to a litigation should have access to some of the most important non-privileged evidence bearing directly on the case runs counter to basic principles of civil discovery," particularly in the case where the party "otherwise left in ignorance is a government agency charged with civilly enforcing the very same provisions that are subject of the parallel criminal case arising from the same transaction."<sup>34</sup> Mr. Rajaratnam and Ms. Chiesi have appealed the order. Moreover, despite Judge Rakoff's ruling, it still remains unclear which judge will ultimately decide defendants' motion to suppress the wiretap recordings on the basis they were obtained in violation of the federal wiretap statute.

Recent events also showed the risks to the government in using wiretap evidence in the midst of parallel criminal and civil proceedings. The court-authorized wiretaps were made as part of the criminal investigation. The federal wiretap statute sets out detailed procedures for the conduct of a wiretap and restrictions on the use of the recordings. The government recently admitted to the trial judge in one of the pending criminal cases that the DOJ had inadvertently given some wiretap evidence to the SEC in the course of giving the SEC recordings of consensually recorded conversations.<sup>35</sup> Defendants will likely

argue that the government's misstep should result in the suppression of the improperly disclosed recordings.

Defendants and the government may more often be forced to confront the legal and strategic issues that recur in parallel proceedings. Since becoming Director of the SEC's Division of Enforcement in February 2009, Robert Khuzami—formerly chief of the Securities and Commodities Fraud Task Force in the United States Attorney's Office for the Southern District of New York—has continually promised that the Division will aggressively litigate and try its enforcement cases. This pressure to bring, and win, "message cases" may prompt the Division's trial attorneys to press for an early trial date. Courts are also pushing cases along, disfavoring what had become accepted practice of having the civil case stayed until resolution of the criminal case. For example, in the SEC's case against *Galleon*, Judge Rakoff in the Southern District of New York ordered that the SEC must try its case by mid-2010, irrespective of the on-going parallel criminal case.

## 2. *Aggressive penalties*

Both the DOJ and SEC sought tough sanctions in 2009. The chart at Appendix A summarizes the civil and criminal sanctions imposed in insider trading cases in 2009.

The SEC continued routinely to seek disgorgement of the illegal profits (or losses avoided), plus prejudgment interest, to permanently enjoin the defendant from future violations, and to impose a civil penalty of up to three times the profit or avoided losses. From tippers, the SEC may seek to disgorge, or impose a civil penalty based on, all of the profits

made by downstream tippees. In *SEC v. Jones, et al.*, for example, one defendant consented to settle the SEC's charges by agreeing to disgorge \$20,000 of trading profits, although the defendant did not himself trade.

The SEC may also seek a Rule 102(e) bar against professionals such as lawyers and accountants. Under Rule 102(e), "the Commission may censure a person or deny, temporarily or permanently, the privilege of appearing or practicing before it in any way."<sup>36</sup> The SEC may seek such a bar against an "attorney . . . accountant, engineer or other professional or expert,"<sup>37</sup> as it did for example, in *In re Matter of Matthew J. Browne*, a case involving insider trading by an attorney.<sup>38</sup> The SEC may also seek to bar a defendant from serving as an officer or director of any issuer of securities registered pursuant to Section 12 of the Exchange Act or that is required to file reports pursuant to Section 15(d) of the Exchange Act, as in *SEC v. Tajyar, et al.*, a case involving trading by an investor relations professional, among others.<sup>39</sup>

Prison sentences usually follow convictions, except for those individuals who provided substantial cooperation in the investigation and prosecution of others. The DOJ has also aggressively sought forfeiture in insider trading cases. For example, in *U.S. v. Naseem, et al.*, Hafiz Naseem, an investment banker in the Global Energy Group at Credit Suisse, was convicted at trial of providing tips about nine pending mergers and acquisitions, and sentenced to 10 years imprisonment. The government also secured a \$9 million criminal forfeiture against Naseem.<sup>40</sup> In its

case against David Tavdy—who was charged in 2007 as part of a ring of 13 individuals who traded on nonpublic information tipped from insiders at two prominent investment banks—the court imposed not only a 63-month prison term but a \$10.3 million criminal forfeiture.<sup>41</sup>

Despite its successes, the government's attempt to aggressively pursue insider trading was not without setbacks in 2009.

The DOJ's insistence on securing prison sentences following convictions in insider trading cases is also exemplified by the case of Michael Tom, who entered into a plea agreement with the government, under which the Court sentenced Mr. Tom to three years probation with six months community service.<sup>42</sup> The government successfully appealed the sentence as unreasonably lenient, and Mr. Tom was resentenced to one year and one day imprisonment and 3 months of supervised relief.<sup>43</sup>

### 3. Expanding the scope of the law

In 2009, the SEC sought to expand the theories under which it may pursue insider trading, with apparent success. In *SEC v. Dorozhko*, the Second Circuit held that insider trading liability may be imposed on a defendant who hacks into a third party's computer system, if he "affirmatively misrepresented himself in order to gain access to material, nonpublic information, which he then used to trade."<sup>44</sup> The Second Circuit

rejected counter-arguments that a duty must exist between the hacker and the source of the information. This ruling provides the SEC with a third way to prove insider trading: the classical theory, the misappropriation theory, and now any other conduct among strangers that involves a misrepresentation or other deceptive conduct. This new "misrepresentation theory" may be particularly prominent in insider trading cases involving electronically stored information.

### 4. Enforcement setbacks

Despite its successes, the government's attempt to aggressively pursue insider trading was not without setbacks in 2009. Three high-profile government losses illustrate some of the limits on the government's aggressive enforcement program.

First, in the well-publicized *SEC v. Cuban*, the federal district court in the Northern District of Texas limited the SEC's ability to prove insider trading under the misappropriation theory in a case that presented an unusual set of facts.<sup>45</sup> The Court dismissed for failure to state a claim the SEC's complaint, which alleged that Mr. Cuban had traded in violation of an agreement to keep confidential information about an upcoming private investment in public equity ("PIPE") deal. The Court held that liability under the misappropriation theory requires more: trading in violation of an agreement not to trade. The district court found in effect that an agreement to keep information confidential did not connote an agreement not to trade on the information. The SEC appealed to the Fifth Circuit, which has yet to rule.<sup>46</sup> The eventual

ruling by the Fifth Circuit (or perhaps ultimately the United States Supreme Court) could have a real impact on the drafting of non-disclosure agreements in many business contexts involving public companies.

Second, in the insider trading case against former Qwest Communications CEO Joseph Nacchio, an appeals court cut back on the government's expansive theory of loss under the federal sentencing guidelines. While the Nacchio prosecution resulted in an appellate affirmation of his underlying conviction, the Tenth Circuit handed a setback to the government when it remanded the case to the district court for resentencing.<sup>47</sup> Mr. Nacchio had been found guilty of 19 counts of insider trading and received a sentence including 72 months imprisonment, a \$19 million fine and forfeiture of \$52 million. The Court of Appeals, however, determined that in calculating the "gains" for purposes of sentencing, the district court ignored that some of Mr. Nacchio's profits from the sales could have been due to appreciation in the price of Qwest stock long after the public disclosure of the information that Mr. Nacchio possessed when he traded. The Court of Appeals held that sentencing for insider trading must take into account normal market forces, and the court must determine proceeds related to the insider information, rather than calculating total net profits through the simple arithmetic of subtracting actual total costs from actual total proceeds. In so ruling, the Tenth Circuit rejected the analysis of the Eighth Circuit in *U.S. v. Mooney*,<sup>48</sup> and it remains to be seen whether the *Nacchio* case will become the

standard for calculating gains for sentencing purposes.

Finally, while conventional wisdom would counsel that the populist outrage over the worldwide financial crisis and government bailouts of financial institutions would make trial treacherous for a market professional charged with insider trading or other securities crimes, the Brooklyn federal jury in the Bear Stearns hedge fund trial acquitted on all counts. In November 2009, after a three-week trial in the Eastern District of New York, and only six hours of deliberation, a jury found former Bear Stearns hedge fund manager Ralph Cioffi not guilty of insider trading, among other charges. The DOJ had accused Mr. Cioffi of insider trading, based on the fact that he had moved approximately \$2 million of his own investment from one of the funds he managed in advance of the fund's failure. (The core of the case against Mr. Cioffi and his deputy Matthew Tannin related to alleged misrepresentations to investors, not insider trading.) Many commentators observed that the swift verdict showed that the government cannot necessarily rely on emails plus the anti-Wall Street zeitgeist to ensure convictions. The acquittal across the board leaves open the legal question of whether it constitutes insider trading for a person to redeem shares from a hedge fund when the fund—the party on the other side of the trade—knows all of the same information as the redeemer.

#### D. Investigative Techniques

The government relied on established law enforcement techniques to investigate and enforce insider trading in 2009, but applied them in innovative ways.

The government also relied on new investigative techniques, including advancements in technology, and internal agency initiatives to make 2009 a banner year for advancements in insider trading enforcement techniques.

##### 1. *Old law enforcement methods – wiretapping – in an almost new context*

In the last year, the enforcement agencies turned to tried-and-true law enforcement techniques to crack down on insider trading. In two recent cases, *Galleon* and *Cuttillo*, the FBI and the U.S. Attorney's Office for the Southern District of New York obtained court-authorized wiretaps to investigate and bring insider trading charges. While wiretaps have long been used by law enforcement agencies in battling members of organized crime or narcotics traffickers, it is rare that wiretaps are used in an insider trading investigation. As a result, the government collected contemporaneous evidence of the exchange of inside information, rather than relying solely on traditional after-the-fact evidence. In the age of ubiquitous email, it is almost quaint to harken back to wiretaps in order to obtain the play-by-play of a conspiracy. Prosecutors and SEC enforcement lawyers have come to rely on emails for the contemporaneous account of an insider trader's every move. While some reporters stated that the *Galleon* and *Cuttillo* cases marked the first time ever that court-ordered wiretaps had been used in an insider trading case, in fact the Southern District of New York had used wiretaps in its so-called "Mob on Wall Street" case more than a decade ago that had resulted in the arrest and prosecution of dozens of insider traders.<sup>49</sup>

SEC Enforcement Director Khuzami noted that “the use of these tools underscores the view that large scale insider trading by industry professionals is as serious as organized crime, extortion and similar misconduct where wiretaps commonly are used.” He warned that “persons involved in illegal insider trading schemes now must rightly consider whether their conversations are under surveillance.” Benton Campbell, the U.S. Attorney for the Eastern District of New York, stated in December 2009 that his office has several pending wiretaps in white collar cases.<sup>50</sup>

## 2. *Going high-tech – market surveillance tools*

In 2009, regulatory and enforcement agencies put a greater focus on leveraging technology and other market surveillance tools to help identify insider trading and other financial fraud. The FBI, for instance, established the Financial Intelligence Center, and the SEC established an Office of Market Intelligence. According to federal officials, these offices will use technological tools and screening programs to analyze trading and other activity across markets, including equities, debt securities and derivatives, and cross-reference corporate press releases, announcements and regulatory disclosures. The goal for these agencies is to spot insider trading and other types of financial fraud by identifying patterns, connections and relationships. The electronic analysis will have to be exceedingly sophisticated in order to be effective in sifting through the huge amounts of potentially relevant data. The offices will also continue to collect, analyze, and act on the numerous

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tips, complaints, and referrals that these agencies receive each year.

## 3. *SEC organizational changes*

Consistent with Chairman Mary Schapiro’s promise to reclaim the image of the SEC as “an unrelenting law enforcement agency,” Enforcement Director Khuzami streamlined the internal processes of the Enforcement Division to enable it “to be as swift as possible.” Khuzami also has created new specialized units within the Enforcement Division, and has ushered in the use of tools more commonly associated with criminal investigations.

### a) Rapid subpoenas

Instead of having to obtain advance Commission approval, the SEC has now given regional office heads the authority to issue the formal orders of investigation that members of the SEC Enforcement staff need in order to issue subpoenas. Director Khuzami also has recommended that specific enforcement actions be shorter, subject to fewer reviews, and require quicker turn-around times for Wells submissions by defendants.<sup>51</sup>

Nowhere is the speed and nimbleness of the SEC more apparent than in the area of insider trading. For example, in *SEC v. Saleh*, just two days after Dell, Inc.

announced plans to acquire Perot Systems, the SEC filed an insider trading suit against Reza Saleh, alleging that he had illegally traded in Perot call options after learning about the merger before the public announcement.<sup>52</sup> Similarly, in *SEC v. Condroyer*, the SEC charged Nicolas Patrick Benoit Condroyer and Gilles Robert Roger with insider trading and obtained an emergency asset freeze *the day after* they tried to illegally profit from a Paris-based manufacturer’s acquisition of another health care products company located in Tennessee.<sup>53</sup>

### b) Cooperation agreements

For decades, it has been well known that cooperating with the DOJ in criminal cases—insider trading or otherwise—generally yields real benefits. For just as long, the SEC did not have a clear policy on cooperation. The Enforcement staff would state that cooperation would be taken into account, but was not authorized to make specific promises or enter into written cooperation agreements. And more often than not, a cooperating defendant realized meager benefit in the course of negotiating a resolution with the Commission. This all changed on January 13, 2010, when the SEC announced its new policy on cooperation, which looks a lot like the DOJ policy.

The SEC may now use “cooperation agreements,” “deferred prosecution agreements,” and “non-prosecution agreements.” While each agreement provides different benefits—and carries different risks—as a whole they are designed to provide tangible benefits for cooperation, particularly when the cooperator is “first in the door.” Director Khuzami

warns that “when you engage in misconduct, you now have to think even harder about the possibility of others coming forward to report to the SEC your secret conversations, your hushed plans, your schemes and deceptions.” He encourages those considering cooperating to contact the SEC “quickly” because “the benefits of cooperation will be reserved for those whose assistance is both timely and necessary.”

Furthermore, under Section 21A(e) of the Exchange Act, the SEC has long had a “bounty program” for individuals who help catch insider trading.<sup>54</sup> The SEC can make a bounty award from the civil penalties that are recovered from violators to any person (with a few exceptions) who provided information that led to the imposition of a civil penalty. The SEC’s total bounty awards per case cannot exceed 10% of the penalty. The Commission also has advocated for Congressional authority to expand this program to other areas as well.

#### c) New specialized units

Director Khuzami has also introduced several specialized units within the Enforcement Division.<sup>55</sup> One of the new units is the Asset Management Unit, which will focus on investigations involving investment advisors, investment companies, hedge funds, and private equity funds. The creation of this unit is yet another indication that the SEC is taking a hard look at previously unregulated hedge funds. Another new unit is the Structured and New Products Unit, which will focus on complex derivatives and financial products, including credit default swaps, collateralized debt obligations, and securitized products.

The Market Abuse Unit will focus on large-scale and complex market abuses, such as insider trading and market manipulation schemes, by institutional traders, market professionals, and the like.

#### 4. *Multi-agency and international coordination*

Over the last year, enforcement agencies enhanced their ability to identify and prosecute insider trading through increased coordination with each other, private organizations, trading boards, and international authorities. For instance, the SEC recently partnered with the U.S. Attorney’s Office for the Northern District of California, the FBI, and the Chicago Board Options Exchange to bring insider trading charges against Vinayak S. Gowrish and Adnan S. Zaman. The SEC claims that the defendants stole confidential information from their employers (private equity and financial advisory firms) about five upcoming deals and tipped friends in exchange for kickbacks. This past year the SEC also worked with U.K.’s Financial Services Authority to bring insider trading charges against Renato Negrin and Jon-Paul Rorech in the case involving credit default swaps. The SEC also regularly works with FINRA, the NYSE, and NASDAQ, and other exchanges to identify suspicious trading as it occurs.

On November 17, 2009, President Obama established an interagency Financial Fraud Enforcement Task Force to “enhance coordination and cooperation among federal, state, local, tribal, and territorial authorities responsible for investigating and prosecuting significant financial crimes and violations.” The DOJ leads the Task Force, which also

is composed of more than 20 agencies, including the SEC, the Department of the Treasury, FDIC, and HUD. Attorney General Eric Holder described the Task Force as “an aggressive, coordinated, and proactive effort to investigate and prosecute financial crimes.”

In addition, the FBI and DOJ together established the Securities and Commodities Fraud Working Group to provide a forum for exchanging information, discussing violation trends, legal developments, law enforcement issues, and investigative techniques. It remains to be seen whether the creation of a new task force will have a material impact on detection and prosecution of insider trading. History shows that it is easier to create such a multi-agency task force than it is to make many large government agencies work efficiently together.

#### **Private Litigation**

In addition to government enforcement, companies and individuals should be aware of the potential risks of private litigation as well. According to Cornerstone Research’s *Securities Class Action Filings – 2009: A Year In Review*, 12% of all private securities cases filed in 2009 contained allegations of insider trading.<sup>56</sup> Of the 26 federal securities class actions filed in 2009 that contained insider trading allegations, only 2 cases alleged substantive claims for insider trading.<sup>57</sup> The other 24 actions included trading allegations as circumstantial evidence of the defendants’ scienter. All 26 actions remain in the initial pleading stages, with the exception of *In re Heartland Payment Sys. Sec. Litig.*, No. 09-1043 (D.N.J. filed March 6, 2009),

which was dismissed with prejudice in December 2009 because the plaintiffs had failed to adequately allege a material misrepresentation or omission or allege scienter.

Based on the filings and pleadings of private securities cases in 2009, below are some practical takeaways for companies and individuals.

#### **A. Demonstrating Scienter Through Insider Stock Sales Remains a Challenge for the Plaintiffs' Bar in 2009**

Since the Supreme Court's decision in *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308 (2007), it has been more difficult for plaintiffs to demonstrate a defendant's scienter through his or her stock sales, and 2009 was no exception.

While *Tellabs* raised the bar for pleading securities fraud, the standard for pleading scienter still varies among the Circuits. For example, in the Ninth Circuit, a corporate insider's stock transactions may support an inference of scienter in securities fraud cases only if the transactions are "unusual or suspicious." A transaction is said to be suspicious only when it is "dramatically out of line with prior trading practices at times calculated to maximize the personal benefit from undisclosed inside information."<sup>58</sup> In the Second Circuit, an insider's stock transactions may support an inference of scienter through the insider's "motive and opportunity" to commit fraud. But, for the inference of scienter to be sufficiently "strong," the Second Circuit recognizes that the inference must survive consideration of other nonculpable

explanations.<sup>59</sup> Although with varying degrees of persuasion depending on the Circuit, among the factors that a court can consider in determining whether stock sales raise a strong inference of scienter under *Tellabs* are: (1) the amount and percentage of shares sold by insiders, (2) the timing of the sales, and (3) whether the sales were consistent with the insider's prior trading history.<sup>60</sup> Regardless, under any of the Circuits' standards, the fact that insiders sold stocks during the class period may increase the likelihood of the company attracting a class action in the first place. Plaintiffs will see such sales as easing Plaintiffs' burden of showing scienter, regardless of the circumstances of the sales.

Thus, at a minimum, a plaintiff must allege a "meaningful" trading history of each defendant. In a significant number of opinions issued in 2009, courts declined to infer the existence of scienter where the plaintiff failed to plead meaningful trading histories of each defendant.<sup>61</sup>

Consideration of a defendant's trading history is not all that *Tellabs* requires. Lower courts must also "take into account plausible opposing inferences." Thus, if a defendant can demonstrate a nonculpable explanation for his or her trades during the class period, it is possible to negate any inference of scienter.

Practitioners should carefully analyze the circumstances of any trading by corporate insiders during the class period, including reviewing public disclosures about the trades, such as information provided on Form 4s.

Among the types of questions you should ask are:

- Were the stock sales made under a Rule 10b5-1 plan?<sup>62</sup>
- Did the corporate insider's total holdings increase during the class period?<sup>63</sup>
- Did the corporate insider sell stock in anticipation of his or her departure from the company?<sup>64</sup>
- Did the corporate insider sell stock for tax reasons?<sup>65</sup>
- Did the corporate insider sell stock contemporaneously with exercising stock options?<sup>66</sup>
- Did the corporate insider suffer the same loss in stock value as the plaintiff?<sup>67</sup>
- Did the corporate insider sell restricted stock that was part of his overall compensation package?<sup>68</sup>
- Did the corporation repurchase shares under a share repurchase program during the class period?<sup>69</sup>
- Did other corporate insiders who would have been privy to the same material, nonpublic information as the defendant not sell stock during the class period?<sup>70</sup>
- Did the corporate insider sell stock at a price lower than the class period high?<sup>71</sup>
- Did the corporate insider sell stock well before the alleged misrepresentation or corrective disclosure?<sup>72</sup>
- Did the corporate insider sell stock following the company's earnings announcement?<sup>73</sup>

As the opinions issued in 2009 demonstrate, a simple explanation in a Form 4 of why the sales were made can be an effective way to rebut an inference of scienter. Failing to include these nonculpable explanations in judicially noticeable documents may make it more difficult at the motion to dismiss phase to rebut plaintiffs' scienter allegations and, as a result, increase the cost of litigation.

**B. 10b5-1 Plans May Provide an Effective Defense Against Private Insider Trading Claims and Negate An Inference of Scienter**

Since the SEC's adoption of Rule 10b5-1 in October 2000, it is best practice for executives to enter into pre-arranged trading plans under Rule 10b5-1(c) because these plans create a built-in protection against insider trading allegations. Rule 10b5-1(c) says that, so long as the plan is adopted at a time when the seller has no material nonpublic information, the seller is protected from insider trading liability even if the seller comes into possession of material nonpublic information by the time sales actually occur. In private securities class actions, courts can take judicial notice of publicly filed documents showing that a defendant's trades were made under a 10b5-1 plan. Thus, even at the motion to dismiss phase, a seller may effectively defend an insider trading claim or negate an inference of scienter by showing his or her stock sales were made under a 10b5-1 plan.

Once a 10b5-1 plan is in place, it is best for executives to refrain from modifying or canceling plans. Rule 10b5-1 has a general "good faith" requirement—that is, a plan must be entered into "in good faith and not as

part of a plan or scheme to evade" the prohibitions of Rule 10b5-1(c). In securities class actions (as well as in SEC and DOJ proceedings), a modification or cancellation of a plan can create the appearance of abuse and provide a basis to attack the affirmative defense at the motion to dismiss stage or later stages of the case. Indeed, the SEC adopted new interpretive guidance in 2009 that, among other things, flags as suspicious the cancellation of a trading plan and entering into a new plan with different terms in quick succession.<sup>74</sup>

The following 2009 opinions in securities class actions illustrate the benefits of entering into a 10b5-1 plan and the potential perils of modifying or canceling a plan once it is in place.

For example, *In re Countrywide Financial Corp. Sec. Litig.*,<sup>75</sup> the court granted three of the defendants' motion to dismiss the Section 20A claim as they demonstrated that their stock sales were made under 10b5-1 plans. As to the former CEO of Countrywide, however, the court denied his motion to dismiss the insider trading claim for sales made after he began modifying his plans. In parallel derivative litigation, the court concluded that Countrywide's CEO's amendments of his plans "appear[ed] to defeat the very purpose of the 10b5-1 plans."<sup>76</sup>

In *In re Gildan Activewear, Inc. Sec. Litig.*<sup>77</sup> and *In re PMI Group, Inc. Sec. Litig.*,<sup>78</sup> the courts held that the defendants' stock trades, made under 10b5-1 plans, rebutted any inference of scienter. By contrast, in *Backe v. Novatel Wireless, Inc.*, the court held that the defendants' stock sales supported an inference of scienter, where plaintiffs showed that the

As the opinions issued in 2009 demonstrate, a simple explanation in a Form 4 of why the sales were made can be an effective way to rebut an inference of scienter.

defendants had modified their 10b5-1 plans to allow them to sell more shares of stock and demonstrated an unusual and suspicious pattern of trading.<sup>79</sup>

There are significant benefits to having 10b5-1 plans in place. Likewise, public disclosure of at least the existence of these plans by the company in the public filings can go a long way in private litigation. Modifying a plan can be a red flag for both private litigants and the government, so expert advice should be sought before taking these steps.

## Economic Analysis

Since trading strategies and financial products have gotten more complex, expert testimony takes on greater importance than ever before in insider trading cases of all sorts: criminal, SEC enforcement, and private civil. An expert could look at a defendant's trading records for a particular period of time and might be able to explain to a jury whether the trading patterns are consistent with the possession of material nonpublic information about the stock being traded. In private civil litigation, an expert economist could do the familiar event study that could show that a particular increase or decrease in a company's stock price was due not to the release of the previously nonpublic information, but rather to exogenous factors such as changes in the worldwide economy, the local economy, the relevant industry,

other parts of the company, and the like. Finally, at sentencing an expert could provide the court with the kind of calculations that the Tenth Circuit now mandates under *Nacchio*.

## Compliance

In this regulatory environment, it is clear that companies need to assure themselves that they have a robust and up-to-date insider trading compliance program. Given the many public allegations in 2009 of insider tips flowing from companies and their advisors (and the public relations hits suffered by those companies when charges are filed), companies are now on notice that they need to minimize the risk that insider trading will emanate from the company.

As with compliance programs in general, an effective insider trading compliance program has to start with a compliance-oriented “tone at the top.” Senior executives need to publicly support the company’s policies and adopt their own trading habits to match. Top management also needs to be supportive of training efforts and encourage broad, frequent, and mandatory training of employees. Employees are more likely to appreciate and adopt a culture of compliance if the culture is one that is fostered and practiced by the company’s top management.

Each company needs to understand its business and corresponding business practices. For financial companies, for example, the company needs to evaluate its trading strategies and understand how its employees gather information. By contrast, an industrial conglomerate faces entirely different insider trading exposure. It is more likely to have

to ensure that personnel in its mergers and acquisitions operation understand the importance of safeguarding takeover plans. Having a real understanding of how the business operates will enable the company to create tailored policies and provide applicable training that has real life application for its employees. There is no ready-made one-size-fits-all insider trading compliance program that would be effective in practice and would be deemed effective in hindsight if something goes awry.

Companies also need to recognize that, in the age of instant messaging, Facebook and Twitter, its employees are able to communicate with a wide range of people instantaneously.

Companies also need to recognize that, in the age of instant messaging, Facebook and Twitter, its employees are able to communicate with a wide range of people instantaneously. The ubiquity of email communication is beginning to erode in favor of use of social networking sites. The march of technology will soon bring other forms of communications and new headlines (not necessarily in newsprint) when insider traders are caught using some as-yet unheard of means of electronic communication. Through these informal communications, information spreads rapidly. In this modern era of communication, companies need to have compliance policies and programs that are able to regulate and control any improper dissemination of information. To do so, the compliance function within an organization has to remain current on how the employees communicate with each other and with the outside world.

Companies also need to recognize that insider trading is not limited to traditional common stocks. Because what constitutes a “security” is not always clear, especially in the context of novel financial products, compliance programs and policies need to cover any such novel products.

Companies should also assume that every email, IM, and Tweet will be read, and in the wake of *Galleon*, that the phones (including cell phones) may be bugged. To that end, companies need to have policies and procedures in place that eliminate—or at the very least reduce—the risk of giving the authorities a reason to be suspicious.

## Conclusion

A clear takeaway from last year’s insider trading activities is that 2010 is likely to bring more investigations, indictments, and convictions. The government has sent a loud message that investigation and prosecution of insider trading will continue to be a top priority for both the Justice Department in criminal prosecutions and the SEC in its civil enforcement cases. ■

<sup>1</sup> See *Chiarella v. United States*, 445 U.S. 222 (1980).

<sup>2</sup> See *United States v. O’Hagan*, 521 U.S. 642 (1997).

<sup>3</sup> 17 C.F.R. § 240.10b5-2.

<sup>4</sup> 17 C.F.R. § 240.10b5-2(b).

<sup>5</sup> *Id.*

<sup>6</sup> 17 C.F.R. § 240.10b5-2(b)(3) (“[T]he person receiving or obtaining the information may demonstrate that no duty of trust or confidence existed with respect to the information, by establishing that he or she neither knew nor reasonably should have known that the person who was the source of the information expected that the person would keep the information confidential, because of the parties’ history, pattern, or practice of sharing and maintaining confidences, and because there was no agreement or understanding to maintain the confidentiality of the information.”).

<sup>7</sup> 17 C.F.R. § 240.14e-3.

<sup>8</sup> Commodity Futures Modernization Act of 2000, Pub. L. No. 106-554, § 1(a)(5), 114 Stat. 2763 (Dec. 21, 2000) (codified at 15

- U.S.C. § 78j(b)).
- <sup>9</sup> Gramm-Leach-Bliley Act, Pub. L. No. 106-102, § 206B, 113 Stat. 1138 (Nov. 12, 1999) (set out as a note under 15 U.S.C. § 78c).
- <sup>10</sup> 15 U.S.C. § 78u-1.
- <sup>11</sup> <http://www.fbi.gov/congress/congress09/perkins120909.htm>.
- <sup>12</sup> *SEC Speaks Annual Conference* (Feb. 5, 2010, Washington, D.C.).
- <sup>13</sup> *U.S. v. Rajaratnam et al.*, 09-Cr-1184 (RJH) (S.D.N.Y.).
- <sup>14</sup> *SEC v. Galleon Mgmt, LP et al.*, 09 Civ. 8811 (JSR) (S.D.N.Y.).
- <sup>15</sup> See *Galleon's Web*, The Wall Street Journal, February 16, 2010, <http://s.wsj.net/public/resources/documents/Galleon-Web-0911.html>. Reprinted with permission of The Wall Street Journal, Copyright © 2010 Dow Jones & Company, Inc. All Rights Reserved Worldwide.
- <sup>16</sup> Zachery Kouwe, *Kurland Pleads Guilty in Galleon Insider Case*, The New York Times DealBook, January 27, 2010, <http://dealbook.blogs.nytimes.com/2010/01/27/kurland-pleads-guilty-in-galleon-insider-case/>.
- <sup>17</sup> See Chad Bray, *Slaine Pleads Guilty to Insider-Trading Charges*, The Wall Street Journal, February 2, 2010, <http://online.wsj.com/article/SB10001424052748704022804575041412242162460.html>.
- <sup>18</sup> *U.S. v. Goffer, et al.*, 10-Cr-00056 (RJS) (S.D.N.Y.).
- <sup>19</sup> *U.S. v. Santarlas*, 09-Cr-1170 (PKC) (S.D.N.Y.).
- <sup>20</sup> *SEC v. Santarlas*, 09-CV-10100 (LAK) (S.D.N.Y.) and *SEC v. Cutillo et al.*, 09-CV-9208 (LAK) (S.D.N.Y.).
- <sup>21</sup> *U.S. v. Shankar*, 09-996 (VM) (S.D.N.Y.).
- <sup>22</sup> *SEC v. Tang, et al.*, 09-CV-05146 (JCS) (N.D.Cal.).
- <sup>23</sup> *SEC v. Stephanou, et al.*, 09-CV-01043 (S.D.N.Y.).
- <sup>24</sup> *SEC v. Saleh, et al.*, 09-CV-01778-M (N.D.Tex.).
- <sup>25</sup> *SEC v. Mahler*, 09-CV-01767 (PLF) (D.D.C.).
- <sup>26</sup> *U.S. v. Mahler*, 09-Cr-00266 (HHK) (D.D.C.).
- <sup>27</sup> See Andrew Ross Sorkin, *S.E.C. Plans Hedge Fund Sweeps*, The New York Times DealBook, January 5, 2010, <http://dealbook.blogs.nytimes.com/2010/01/05/sec-plans-hedge-fund-sweeps/>.
- <sup>28</sup> See Kara Scannell and Jenny Strasburg, *SEC Steps Up Insider-Trading Probes*, The Wall Street Journal, December 2, 2009, <http://online.wsj.com/article/SB10001424052748704107104574570183527937954.html>.
- <sup>29</sup> *SEC v. Rorech, et al.*, No. 09 Civ. 4329 (JGK), 2009 WL 4729921 (S.D.N.Y. Dec. 10, 2009).
- <sup>30</sup> *SEC v. Rorech, et al.*, 09 Civ. 4329 (JGK), 2009 U.S. Dist. LEXIS 115305 (S.D.N.Y. Dec. 10, 2009).
- <sup>31</sup> See Liz Rappaport, *Case Opens New Front on Insider Trading*, The Wall Street Journal, May 6, 2009, <http://online.wsj.com/article/SB124153448113387615.html>.
- <sup>32</sup> See *SEC v. Davis, et al.*, 03-CV-06672 (NRB) (S.D.N.Y. 2003) (charging insider trading ring in connection with nonpublic information concerning Treasury bonds).
- <sup>33</sup> *SEC v. Grmovsek*, 09-CV-9029 (CM) (S.D.N.Y.); *U.S. v. Grmovsek*, 09-Cr-01044 (NRB) (S.D.N.Y.).
- <sup>34</sup> *SEC v. Galleon Mgmt, LP et al.*, No. 09 Civ. 8811 (JSR), Order (S.D.N.Y. Feb. 9, 2010).
- <sup>35</sup> See Chad Bray and David Benoit, *Update: DOJ Inadvertently Gave SEC Wiretaps In Galleon Case*, The Wall Street Journal, February 2, 2010, <http://online.wsj.com/article/BT-CO-20100202-709779.html>.
- <sup>36</sup> 17 C.F.R. § 201.102(e).
- <sup>37</sup> *Id.*
- <sup>38</sup> *In re Matthew J. Browne, Attorney*, Exchange Act Rel. No. 59960 (May 21, 2009).
- <sup>39</sup> *SEC v. Tajyar, et al.*, 09-CV-03988 (DMG) (PJW) (C.D. Cal.).
- <sup>40</sup> *U.S. v. Naseem, et al.*, 07-Cr-00610 (RPP) (S.D.N.Y.).
- <sup>41</sup> *U.S. v. Guttenberg, et al.*, 07-Cr-00141 (DAB) (S.D.N.Y.).
- <sup>42</sup> *U.S. v. Tom*, 05-Cr-10361 (NMG) (D. Mass.).
- <sup>43</sup> *U.S. v. Tom*, 275 Fed. Appx. 23, 25 (1st Cir. 2008).
- <sup>44</sup> 574 F. 3d 42, 49 (2d Cir. 2009) (remanding case to determine whether defendant's hacking involved a misrepresentation).
- <sup>45</sup> *SEC v. Cuban*, 634 F. Supp. 2d 713 (N.D. Tex. 2009).
- <sup>46</sup> *SEC v. Cuban*, No. 09-10996 (5th Cir.).
- <sup>47</sup> *U.S. v. Nacchio*, 573 F.3d 1062 (10th Cir. 2009).
- <sup>48</sup> See *U.S. v. Mooney*, 401 F.3d. 940 (8th Cir. 2005).
- <sup>49</sup> *Organized Crime on Wall Street, Hearing Before the Subcomm. on Finance and Hazardous Materials of the H. Comm. on Commerce*, 106th Cong. 118, 262-63 (2000) (statement of Thomas V. Fuentes, Chief, Organized Crime Section, Criminal Investigative Division, Federal Bureau of Investigation).
- <sup>50</sup> *Securities Litigation During the Financial Crisis*, New York City Bar Association (Dec. 8, 2009).
- <sup>51</sup> See Robert Khuzami, *Speech by SEC Staff: Remarks Before the New York City Bar: My First 100 Days as Director of Enforcement*, U.S. Securities and Exchange Commission, August 5, 2009, <http://www.sec.gov/news/speech/2009/spch080509rk.htm>.
- <sup>52</sup> *SEC v. Saleh, et al.*, 09-CV-01778-M (N.D. Tex.).
- <sup>53</sup> *SEC v. Condroyer*, 09-CV-3600 (N.D. Ga.).
- <sup>54</sup> See 15 U.S.C. § 78u-1(e).
- <sup>55</sup> See *SEC Names New Specialized Unit Chiefs and Head of New Office of Market Intelligence*, U.S. Securities and Exchange Commission, Jan. 13, 2010, <http://www.sec.gov/news/press/2010/2010-5.htm>.
- <sup>56</sup> See Cornerstone Research, *Securities Class Action Filings, 2009: A Year in Review*, [http://securities.cornerstone.com/pdfs/Cornerstone\\_Research\\_Filings\\_2009\\_YIR.pdf](http://securities.cornerstone.com/pdfs/Cornerstone_Research_Filings_2009_YIR.pdf).
- <sup>57</sup> See *City of Brockton Retirement Sys. v. Acucray, Inc.*, No. 09-03362-CW (N.D. Cal. filed Dec. 30, 2009) (insider trading claim brought under Section 10(b) and Rule 10b-5); and *In re Bare Escentuals, Inc. Sec. Litig.*, No. 09-03268 (N.D. Cal. filed Dec. 23, 2009) (insider trading claim brought under Section 20(A)).
- <sup>58</sup> *Zucco Partners, LLC v. Digimarc Corp.*, 552 F.3d 981, 1005 (9th Cir. 2009).
- <sup>59</sup> See *ATSI Commc'ns, Inc. v. Shaar Fund, Ltd.*, 493 F.3d 87 (2d Cir. 2007).
- <sup>60</sup> *Zucco Partners, LLC*, 552 F.3d 1005.
- <sup>61</sup> See, e.g., *id.*; *Konkol v. Diebold, Inc.*, No. 08-4572, 2009 U.S. App. LEXIS 28194 (6th Cir. 2009); *Isham v. Perini Corp.*, No. 08-11449-NMG, 2009 U.S. Dist. LEXIS 98853 (D. Mass. Oct. 7, 2009); *Edward J. Goodman Life Income Trust v. Jabil Circuit, Inc.*, 595 F. Supp. 2d 1253 (M.D. Fla. Jan. 26, 2009); *In re Zumiez Inc. Sec. Litig.*, No. C07-1980-JCC, 2009 U.S. Dist. LEXIS 26153 (W.D. Wa. March 30, 2009).
- <sup>62</sup> *In re Gildan Activewear, Inc. Sec. Litig.*, 636 F. Supp. 2d 261 (S.D.N.Y. 2009); *In re PMI Group, Inc. Sec. Litig.*, No. C 08-1405, 2009 U.S. Dist. LEXIS 56709 (N.D. Cal. July 1, 2009); *In re Smith & Wesson Holding Corp. Sec. Litig.*, 604 F. Supp. 2d 332 (D. Mass. 2009); *In re First Marblehead Corp. Sec. Litig.*, 639 F. Supp. 2d 145 (D. Mass. 2009); *In re Countrywide Fin. Corp. Sec. Litig.*, No. 07-05295-MRP, 2009 U.S. Dist. LEXIS 32951 (C.D. Cal. April 6, 2009); *City of Roseville Employees' Retirement Sys. v. Horizon Lines, Inc.*, No. 08-969, 2009 U.S. Dist. LEXIS 106186 (D. Del. Nov. 13, 2009).
- <sup>63</sup> See *Avon Pension Fund v. GlaxoSmithKline PLC*, No. 08-04363, 2009 U.S. Dist. LEXIS 18969 (2d Cir. Aug. 24, 2009); *In re Radian Sec. Litig.*, 612 F. Supp. 2d 594 (E.D. Pa. 2009).
- <sup>64</sup> *Beaver County Retirement Bd. v. LCA-Vision*, No. 07-750, 2009 U.S. Dist. LEXIS 31375 (S.D. Ohio March 25, 2009); *Radian*, 612 F. Supp. 2d at 612.
- <sup>65</sup> *Radian*, 612 F. Supp. 2d at 611; *In re Medtronic Inc. Sec. Litig.*, 618 F. Supp. 2d 1016 (D. Minn. 2009).
- <sup>66</sup> *Medtronic*, 618 F. Supp. 2d at 1037-38.
- <sup>67</sup> *New York State Teachers' Retirement Sys. v. Fremont General Corp.*, No. 07-5756, 2009 U.S. Dist. LEXIS 94241 (C.D. Cal. Sept. 25, 2009).
- <sup>68</sup> *Radian*, 612 F. Supp. at 611.
- <sup>69</sup> *Beaver County Retirement Bd.*, 2009 U.S. Dist. LEXIS 31375, at \*72-73.
- <sup>70</sup> *Gildan Activewear*, 636 F. Supp. 2d at 271-72; *Beaver County Retirement Bd.*, 2009 U.S. Dist. LEXIS 31375, at \*72-73.
- <sup>71</sup> *Beaver County Retirement Bd.*, 2009 U.S. Dist. LEXIS 31375, at \*72-73.
- <sup>72</sup> *Gildan Activewear*, 636 F. Supp. 2d at 271; *Marblehead Corp.*, 639 F. Supp. 2d at 163-64; *In re Dot Hill Sys. Corp. Sec. Litig.*, No. 06-228-JLS, 2009 U.S. Dist. LEXIS 220022 (S.D. Cal. March 18, 2009).
- <sup>73</sup> *Brodsky v. Yahoo!*, No. 08-02150-CW, 2009 U.S. Dist. LEXIS 51281 (N.D. Cal. June 18, 2009).
- <sup>74</sup> See *Exchange Act Rules*, U.S. Securities and Exchange Commission, May 29, 2009, <http://www.sec.gov/divisions/corpfin/guidance/exchangeactrules-interps.htm> (Question 120, 18 and 120, 19); see also Alan D. Jagolinzer, *SEC Rule 10b5-1 and Insiders' Strategic Trade*, MANAGEMENT SCIENCE, Vol. 55, No. 2, February 2009, pp. 224-239.
- <sup>75</sup> *In re Countrywide Financial Corp. Sec. Litig.*, No. 07-05295-RMP, 2009 U.S. Dist. LEXIS 32951 (C.D. Cal. April 6, 2009).
- <sup>76</sup> *In re Countrywide Fin. Corp. Sec. Litig.*, 588 F. Supp. 2d 1132 (C.D. Cal. 2008).
- <sup>77</sup> *In re Gildan Activewear, Inc. Sec. Litig.*, 636 F. Supp. 2d 261 (S.D.N.Y. 2009).
- <sup>78</sup> *In re PMI Group, Inc. Sec. Litig.*, No. 08-1405-SI, 2009 U.S. Dist. LEXIS 56709 (N.D. Cal. July 1, 2009).
- <sup>79</sup> *Backe v. Novatel Wireless, Inc.*, 642 F. Supp. 2d 1169, 1184-85 (S.D. Cal. 2009).

Appendix  
A**2009: Results of Insider Trading Prosecutions and SEC Enforcement Actions****Criminal Cases**

<b>Date</b>	<b>Defendant</b>	<b>Role</b>	<b>Trial or Plea</b>	<b>Sentence</b>
3/3/09	David Tavdy <i>(U.S. v. Guttenberg, et al., S.D.N.Y. 2007)</i>	Tippee	Plea	<ul style="list-style-type: none"> <li>• 63 months imprisonment</li> <li>• Guideline Calculations: Offense level 26 (63-78 months): +8 base level +20 gain enhancement -2 for acceptance of responsibility</li> <li>• 3 years supervised release</li> <li>• \$300 special assessment;</li> <li>• \$10.3 million criminal forfeiture</li> </ul>
3/6/09	Robert Babcock <i>(U.S. v. Guttenberg, et al., S.D.N.Y., 2007)</i>	Tippee	Plea	<ul style="list-style-type: none"> <li>• 2 years probation</li> <li>• \$10,000 fine</li> <li>• \$200 special assessment</li> <li>• \$104,619 criminal forfeiture</li> </ul>
7/23/09	Michael Tom <i>(U.S. v. Tom, et al., D. Mass., 2005)</i>	Tippee	Plea	<ul style="list-style-type: none"> <li>• 1 year and 1 day imprisonment, plus 3 months of supervised relief</li> <li>• Guideline Calculations: Offense level 21 (37-46 months): +8 base offense level +14 gain enhancement +2 obstruction of justice -3 acceptance of responsibility</li> <li>• \$500 special assessment</li> </ul>
7/29/09	Alan Tucker <i>(U.S. v. Marshall, et al., S.D.N.Y., 2008)</i>	Tippee	Plea	<ul style="list-style-type: none"> <li>• 3 years probation, including 6 months home confinement</li> <li>• \$10,000 fine</li> <li>• \$1,054,979 criminal forfeiture</li> <li>• \$100 special assessment</li> <li>• Community service of 25 hours per quarter</li> <li>• Work at Pace University for first semester at salary of \$1</li> </ul>
8/7/09	George Paparrizos <i>(U.S. v. Stephanou, et al., S.D.N.Y., 2009)</i>	Tippee	Plea	<ul style="list-style-type: none"> <li>• 3 years probation</li> <li>• Guideline Calculations: Offense level 10 (6-12 months): 8 base offense level +4 gain enhancement -2 acceptance of responsibility</li> <li>• \$22,000 criminal forfeiture</li> <li>• \$200 special assessment</li> <li>• \$10,000 criminal penalty</li> </ul>

Appendix  
A**Criminal Cases (cont'd)**

Date	Defendant	Role	Trial or Plea	Sentence
9/17/09	Frederick Bowers ( <i>U.S. v. Devlin, et al.</i> , S.D.N.Y., 2008)	Tippee	Plea	<ul style="list-style-type: none"> <li>• 3 years probation</li> <li>• Guideline Calculations: Offense level 13 (12-18 months)*</li> <li>• 2,000 hours community service</li> <li>• \$15,000 fine</li> <li>• \$12,000 forfeiture</li> </ul>
10/1/09	Eric Holzer ( <i>U.S. v. Devlin, et al.</i> , S.D.N.Y., 2008)	Tippee	Plea	<ul style="list-style-type: none"> <li>• 5 years probation that includes 270 days (on weekends) at residential reentry center</li> <li>• Guideline Calculations: Offense level 13 (12-18 months). +8 base level +8 gain (\$119,347) -3 acceptance of responsibility</li> <li>• \$15,000 fine.</li> </ul>
12/15/09	Erik Franklin ( <i>U.S. v. Franklin</i> , S.D.N.Y., 2007)	Tippee	Plea	<ul style="list-style-type: none"> <li>• 3 years probation that includes 12 months of home confinement</li> <li>• Guideline Calculations: Offense level 27 (70-87 months)</li> <li>• 200 hours of community service</li> <li>• \$400 special assessment</li> <li>• \$2.59 million criminal forfeiture</li> </ul>

**SEC Enforcement Cases**

Date	Defendant	Role	Resolution	Sanction
1/22/09	Aaron Cooksey ( <i>SEC v. Cooksey</i> , W.D. Tex.)	Trader	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$23,552 disgorgement</li> <li>• \$883.70 prejudgment interest</li> <li>• \$23,552 civil penalty</li> </ul>
2/10/09	Joseph A. Federico ( <i>SEC v. Queri, et al.</i> , W.D. Penn., 2008)	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$23,326 disgorgement</li> <li>• \$7,540.22 prejudgment interest</li> <li>• \$23,326 civil penalty</li> </ul>
2/10/09	Philip J. Simao ( <i>SEC v. Queri, et al.</i> , W.D. Penn., 2008)	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$13,390 disgorgement</li> <li>• \$4,328.37 prejudgment interest</li> <li>• \$13,390 civil penalty</li> </ul>

\* Precise calculation unknown. It was publicly reported that Bowers faced up to 18 months in prison.

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## SEC Enforcement Cases (cont'd)

Date	Defendant	Role	Resolution	Sanction
2/10/09	Mark J. Costello ( <i>SEC v. Queri, et al.</i> , W.D. Penn., 2008)	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$9,540 disgorgement</li> <li>• \$3,083.85 prejudgment interest</li> <li>• \$9,540 civil penalty</li> </ul>
2/10/09	Franco J. Marretti, III ( <i>SEC v. Queri, et al.</i> , W.D. Penn., 2008)	Tippee and Tipper	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$9,552 disgorgement</li> <li>• \$3,150.92 prejudgment interest</li> <li>• \$54,817 civil penalty</li> </ul>
2/26/09	James T. Anderson ( <i>SEC v. Zomax, Inc., et al.</i> , D. Minn., 2005)	Trader	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$6,701,400 disgorgement</li> <li>• \$1,340,280 prejudgment interest</li> <li>• Prior criminal penalties</li> <li>• Officer and director bar</li> </ul>
3/13/09	Michael Biello ( <i>SEC v. Biello</i> , S.D. Tex., 2009)	Tipper	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$6,036 disgorgement</li> <li>• \$596.34 prejudgment interest</li> <li>• \$6,036 civil penalty</li> </ul>
4/16/09	J. Thomas Talbot ( <i>SEC v. Talbot</i> , C.D. Cal., 2004)	Trader	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$67,881 disgorgement</li> <li>• \$26,916 prejudgment interest</li> <li>• \$135,762 civil penalty</li> </ul>
4/17/09	William M. Gallahair ( <i>SEC v. Gallahair</i> , N.D. Cal., 2008)	Trader	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$152,068.45 disgorgement and prejudgment interest</li> <li>• \$120,170.13 civil penalty</li> </ul>
4/28/09	Matthew J. Browne ( <i>SEC v. Browne</i> , N.D. Okla., 2009)	Trader	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$81,773 disgorgement</li> <li>• \$1,505.98 prejudgment interest</li> <li>• \$81,773 civil penalty</li> <li>• Rule 102(e) bar</li> </ul>
4/30/09	Nasser Mardini ( <i>SEC v. Mardini</i> , N.D. Cal., 2009)	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• Disgorgement</li> </ul>
4/30/09	Joseph Azar ( <i>SEC v. Azar</i> , N.D. Cal., 2009)	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• Disgorgement</li> <li>• Civil penalty</li> </ul>
5/27/09	Gerald L. Brodsky ( <i>SEC v. Gansman, et al.</i> , S.D.N.Y., 2008)	Tippee	Default judgment	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$63,400 disgorgement</li> <li>• \$12,324 prejudgment interest</li> <li>• \$190,200 civil penalty</li> </ul>

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## SEC Enforcement Cases (cont'd)

Date	Defendant	Role	Resolution	Sanction
6/10/09	Michael Goodman <i>(SEC v. Macdonald, et al., S.D.N.Y., 2009)</i>	Tipper	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$1,023,054 disgorgement</li> <li>• \$251,301.42 prejudgment interest</li> <li>• Payment of amounts, plus civil penalty, waived due to financial condition</li> </ul>
7/15/09	Math J. Hipp <i>(SEC v. Hipp, W.D. Wa., 2009)</i>	Trader	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$118,245 disgorgement</li> <li>• \$3,280 prejudgment interest</li> <li>• \$118,245 civil penalty</li> </ul>
7/15/09	Anthony Perez <i>(SEC v. Perez, et al., M.D. Fla., 2009)</i>	Tipper	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$152,231 disgorgement (joint and several liability with Ian Perez)</li> <li>• \$761 prejudgment interest (joint and several liability with Ian Perez)</li> <li>• \$25,000 civil penalty (higher penalty not imposed due to financial condition)</li> </ul>
7/15/09	Ian C. Perez <i>(SEC v. Perez, et al., M.D. Fla., 2009)</i>	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$152,231 disgorgement (joint and several liability with Anthony Perez)</li> <li>• \$761 prejudgment interest (joint and several liability with Anthony Perez)</li> <li>• No civil penalty due to financial condition</li> </ul>
8/10/09	Gary M. Gosson <i>(SEC v. Queri, et al., W.D. Penn., 2008)</i>	Tipper	Default judgment	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$47,127 disgorgement</li> <li>• \$17,174.26 prejudgment interest</li> <li>• \$274,613 civil penalty</li> </ul>
8/10/09	Gary L. Camp <i>(SEC v. Queri, et al., W.D. Penn., 2008)</i>	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$128,792 disgorgement</li> <li>• \$46,935 prejudgment interest</li> <li>• \$128,792 civil penalty</li> </ul>
8/12/09	Edwin "Bucky" Lyon, IV and Gryphon Advisors, LLC <i>(SEC v. Lyon, et al., S.D.N.Y., 2009)</i>	Traders	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$66,712 disgorgement</li> <li>• \$33,850 prejudgment interest</li> <li>• \$310,288 civil penalty</li> </ul>

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## SEC Enforcement Cases (cont'd)

Date	Defendant	Role	Resolution	Sanction
8/12/09	Gryphon Master Fund, L.P.; Gryphon Partners, L.P.; Gryphon Partners (QP), L.P.; Gryphon Offshore Fund, Ltd.; Gryphon Management Partners, L.P.; Gryphon Management Partners III, L.P. <i>(SEC v. Lyon, et al., S.D.N.Y., 2009)</i>	Traders	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$243,576 disgorgement</li> <li>• \$123,590 prejudgment interest</li> </ul>
8/24/09	Nancy Jewell <i>(SEC v. Jewell, et al., S.D.N.Y., 2009)</i>	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$8,888 disgorgement</li> <li>• \$943.56 prejudgment interest</li> <li>• \$8,888 civil penalty</li> </ul>
8/24/09	Kristin Mays <i>(SEC v. Jewell, et al., S.D.N.Y., 2009)</i>	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$7,960 disgorgement</li> <li>• \$845.03 prejudgment interest</li> <li>• \$7,960 civil penalty</li> </ul>
8/24/09	Matthew B. Murphy, III <i>(SEC v. Jewell, et al., S.D.N.Y., 2009)</i>	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$9,078 disgorgement</li> <li>• \$963.72 prejudgment interest</li> <li>• \$9,078 civil penalty</li> </ul>
8/27/09	Thomas Genzale <i>(SEC v. Marshall, et al., S.D.N.Y., 2008)</i>	Tippee	Settlement	<ul style="list-style-type: none"> <li>• \$826,118.84 disgorgement</li> <li>• \$105,977.61 prejudgment interest</li> <li>• \$826,118.74 penalty</li> </ul>
8/27/09	John Marshall <i>(SEC v. Marshall, et al., S.D.N.Y., 2008)</i>	Tipper	Settlement	<ul style="list-style-type: none"> <li>• \$31,452.73 disgorgement</li> <li>• \$4,034.88 prejudgment interest</li> <li>• Permanent officer and director bar</li> <li>• Prior criminal settlement</li> </ul>
8/27/09	Alan Tucker <i>(SEC v. Marshall, et al., S.D.N.Y., 2008)</i>	Tippee	Settlement	<ul style="list-style-type: none"> <li>• \$18,342.06 prejudgment interest</li> </ul>
8/31/09	Sarath B. Gangavarapu <i>(SEC v. Gangavarapu, E.D. Tenn., 2009)</i>	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$361,761.56 disgorgement</li> <li>• \$46,408.12 prejudgment interest</li> <li>• \$361,761.56 civil penalty</li> </ul>

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## SEC Enforcement Cases (cont'd)

Date	Defendant	Role	Resolution	Sanction
9/9/09	Jeff L. Soisson and Karen Kaye Walker ( <i>SEC v. Soisson, et al.</i> , N.D. Tex., 2009)	Tipper (Walker) and Tippee (Soisson)	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$163,224 disgorgement (joint and several)</li> <li>• \$3,973.89 prejudgment interest (joint and several)</li> <li>• \$163,224 civil penalty (joint and several)</li> </ul>
9/14/09	Allen W. Moss ( <i>SEC v. Moss</i> , W.D. La., 2009)	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$75,400 disgorgement</li> <li>• \$2,091 prejudgment interest</li> <li>• \$75,400 civil penalty</li> </ul>
10/5/09	Alan J. Johnston ( <i>SEC v. Queri, et al.</i> , W.D. Penn., 2008)	Tippee and Tipper	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$26,503.48 disgorgement</li> <li>• \$9,241.74 prejudgment interest</li> <li>• \$49,374.19 civil penalty</li> <li>• Additional civil penalty of \$22,870.70 waived due to financial condition</li> </ul>
10/5/09	James L. Jerome ( <i>SEC v. Queri, et al.</i> , W.D. Penn., 2008)	Tippee and Tipper	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$46,246 disgorgement</li> <li>• \$16,853.20 prejudgment interest</li> <li>• \$46,246 civil penalty</li> <li>• Additional civil penalty of \$51,158 waived due to financial condition</li> </ul>
10/5/09	Brandt A. England ( <i>SEC v. Queri, et al.</i> , W.D. Penn., 2008)	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$51,158 disgorgement</li> <li>• \$18,643.25 prejudgment interest</li> <li>• \$51,158 civil penalty</li> </ul>
10/7/09	Feng "Frank" Xie ( <i>SEC v. Xie</i> , S.D. Cal., 2009)	Trader	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$62,050.25 disgorgement</li> <li>• \$5,297.25 prejudgment interest</li> <li>• \$62,050.25 civil penalty</li> </ul>
10/8/09 (SEC)	David Tavdy ( <i>SEC v. Guttenberg, et al.</i> , S.D.N.Y., 2007)	Tippee	Settlement	<ul style="list-style-type: none"> <li>• \$10.3 disgorgement</li> <li>• Permanent bar from associating with broker dealer</li> </ul>
10/15/09	Benjamin P. Jones ( <i>SEC v. Jones, et al.</i> , N.D. Cal., 2009)	Tipper	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• Approx. \$20,000 disgorgement (profits made by downstream tippees. This defendant did not trade himself)</li> <li>• Prejudgment interest</li> <li>• Approx. \$80,000 civil penalty</li> </ul>

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## SEC Enforcement Cases (cont'd)

Date	Defendant	Role	Resolution	Sanction
10/15/09	William F. Jones, III ( <i>SEC v. Jones, et al.</i> , N.D. Cal., 2009)	Tipper and Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• Approx. \$34,000 disgorgement</li> <li>• Prejudgment interest</li> <li>• Approx. \$60,000 civil penalty</li> </ul>
10/15/09	William T. Dailey, III ( <i>SEC v. Jones, et al.</i> , N.D. Cal., 2009)	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• Approx. \$20,000 disgorgement</li> <li>• Prejudgment interest</li> <li>• Approx. \$81,000 civil penalty</li> <li>• Bar from associating with any broker or dealer and investment adviser, with right to reapply after five years</li> </ul>
10/15/09	Jeremiah E. Carroll ( <i>SEC v. Jones, et al.</i> , N.D. Cal., 2009)	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• Approx. \$5,100 disgorgement</li> <li>• Prejudgment interest</li> <li>• Approx. \$5,100 civil penalty</li> </ul>
10/21/09	Gautam Gupta ( <i>SEC v. Zeglis, et al.</i> , N.D. Ill., 2009)	Tipper and Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$689,401 disgorgement</li> <li>• \$188,096.17 prejudgment interest</li> <li>• \$689,40.1 civil penalty</li> <li>• Agreed to satisfy payment with monthly payment schedule over one year</li> </ul>
10/23/09	Don N. Spaugy ( <i>SEC v. Spaugy</i> , N.D. Okla., 2009)	Trader	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$67,424 disgorgement</li> <li>• \$3,378.13 prejudgment interest</li> <li>• \$67,424 civil penalty</li> </ul>
10/27/09	Stanko J. Grmovsek ( <i>SEC v. Grmovsek</i> , S.D.N.Y., 2009)	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$8.5 million disgorgement</li> <li>• Payment of all but “nearly \$1.5 million” of this amount waived due to financial condition</li> </ul>
10/29/09	J. Bennett Grocock ( <i>SEC v. Grocock</i> , M.D. Fla., 2009)	Trader	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• Payment of disgorgement and civil penalty waived due to financial condition</li> </ul>
11/6/09	Gregory Carl Gunn ( <i>SEC v. Tedder, et al.</i> , N.D. Tex., 2008)	Tippee	Jury verdict	<ul style="list-style-type: none"> <li>• After “less than an hour of deliberation,” found defendant liable for insider trading</li> <li>• Illicit profits = \$108,587.87</li> </ul>
11/6/09	Nicos Achilleas Stephanou ( <i>SEC v. Stephanou, et al.</i> , S.D.N.Y., 2009)	Tipper	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$461,893 disgorgement</li> <li>• \$77,175 prejudgment interest</li> </ul>

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## SEC Enforcement Cases (cont'd)

Date	Defendant	Role	Resolution	Sanction
11/6/09	George Paparrizos ( <i>SEC v. Stephanou, et al.</i> , S.D.N.Y., 2009)	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$24,617 disgorgement</li> <li>• \$3,900 prejudgment interest</li> <li>• \$24,617 civil penalty</li> </ul>
11/18/09	Francis Elias Axiaq ( <i>SEC v. Axiaq, et al.</i> , N.D. Cal., 2008)	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$881,102 disgorgement</li> <li>• \$59,000 prejudgment interest</li> <li>• \$250,000 civil penalty</li> </ul>
11/23/09	David K. Donovan, Jr. and David R. Hinkle ( <i>SEC v. Donovan, et al.</i> , D. Mass., 2008)	Tipper	Jury verdict	<ul style="list-style-type: none"> <li>• On day after hearing closing arguments, jury found Donovan liable for insider trading.</li> <li>• Jury did not find that Donovan tipped Hinkle and that Hinkle did not commit insider trading</li> </ul>
12/2/09	Sonja Anticevic ( <i>SEC v. Anticevic, et al.</i> , S.D.N.Y., 2005)	Relief defendant	Default judgment	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$2,056,055.15 disgorgement</li> <li>• \$578,223.25 prejudgment interest</li> <li>• \$3,084,082.73 civil penalty (one-and-a-half times profits)</li> </ul>
12/15/09	Erik Franklin ( <i>SEC v. Guttenberg, et al.</i> , S.D.N.Y., 2007)	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$5,400,000 disgorgement with all but \$290,000 waived for inability to pay</li> <li>• Permanent bar from associating with any broker or dealer</li> </ul>
12/16/09	Adnan S. Zaman ( <i>SEC v. Gowrish, et al.</i> , N.D. Cal., 2009)	Tipper	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$78,456 disgorgement and prejudgment interest</li> <li>• Permanent bar from associating with any broker or dealer</li> </ul>
12/16/09	Pascal S. Vaghar ( <i>SEC v. Gowrish, et al.</i> , N.D. Cal., 2009)	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$366,001 disgorgement and prejudgment interest</li> <li>• All but \$33,000 of that amount, and civil penalty, waived due to financial condition</li> </ul>
12/16/09	Sameer N. Khoury ( <i>SEC v. Gowrish, et al.</i> , N.D. Cal., 2009)	Tippee	Settlement	<ul style="list-style-type: none"> <li>• Permanent injunction</li> <li>• \$198,607 disgorgement and prejudgment interest</li> <li>• Payment and civil penalty waived due to financial condition</li> </ul>
12/16/09	Elias N. Khoury ( <i>SEC v. Gowrish, et al.</i> , N.D. Cal., 2009)	Relief defendant	Settlement	<ul style="list-style-type: none"> <li>• \$5,836 disgorgement</li> <li>• \$864 prejudgment interest</li> </ul>

## About Morrison & Foerster's Securities Litigation, Enforcement, and White-Collar Defense Practice Group

Morrison & Foerster is a recognized leader in all aspects of securities litigation, enforcement, and white-collar defense. With more than 150 attorneys in 16 offices worldwide, we can handle virtually any kind of case, anywhere. Our Group includes prominent attorneys with decades of experience, more than a dozen former prosecutors, former SEC enforcement attorneys, current Fellows of the American College of Trial Lawyers and American Board of Trial Advocates, and in-house forensic accounting experts. We have represented clients from all industry sectors, including financial services, life sciences, computer hardware and software, telecommunications, and consumer products.

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*For information about our upcoming seminars on insider trading and other timely topics relating to securities litigation, securities enforcement, and white-collar defense, please check our [list of events](#) at [www.mofo.com](http://www.mofo.com).*

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