UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

Division of Enforcement

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June 9, 2011

The Honorable Charles E. Grassley
Ranking Member
Committee on the Judiciary
United States Senate
152 Dirksen Senate Office Building
Washington, DC 20510

Dear Ranking Member Grassley:

As the Director of the Division of Enforcement, Chairman Schapiro asked that I respond to your May 24, 2011 letter concerning certain referrals from the Financial Industry Regulatory Authority ("FINRA") to the SEC related to SAC Capital. Your letter requested information concerning (1) the manner in which the Commission resolved each referral; (2) how the number of referrals concerning SAC Capital compared to referrals of "similarly situated firms"; and (3) whether Wells notices were "ever drafted with regard to SAC Capital related to any of these referrals or related to any other matter."

I am writing to provide you with information concerning actions taken by the SEC generally in response to SRO referrals (including potential insider trading-related referrals) and to highlight some of the SEC's continuing efforts to combat insider trading, particularly insider trading by hedge funds and hedge fund personnel. As SEC staff communicated to your staff on June 7, in order to protect confidential and nonpublic investigative information, we generally do not comment on the status of investigations or related referrals, and, in turn, are not providing information concerning the specific FINRA referrals you identified. As will be discussed in more detail below, we have filed numerous cases alleging insider trading involving hedge funds, hedge fund managers, financial professionals, corporate insiders, and attorneys who unlawfully traded on material nonpublic information. Our investigations often utilize confidential cooperators and sophisticated investigative and analytical techniques – frequently in coordination with criminal authorities – to develop significant investigative leads that, if compromised, could harm the government's ability to stop illegal conduct and hold wrongdoers accountable.

SEC staff would be happy to meet with your staff to discuss SRO referrals generally, our methods of analyzing and processing SRO referrals, and our insider trading enforcement initiatives and methods of investigation.

Actions Taken by the SEC in Response to SRO Referrals

All SRO referrals received by the Commission are handled by the Division of Enforcement's Office of Market Intelligence ("OMI"), which was established in January 2010. OMI has developed a coordinated intake, triage, and resolution process for handling all Tips, Complaints, and Referrals ("TCRs"), including SRO referrals, received by the Commission.[1]
In the last two fiscal years, the SEC received 721 SRO referrals related to potential insider trading violations, including 493 such referrals from FINRA.[2] In general, these referrals identify potentially suspicious trading by a number of individuals and entities, and provide background information on the security involved, the individuals or entities engaged in the trading, and any relevant corporate or other events that occurred at or around the time of the trading.

Once received by OMI, further analysis is necessary. A group of dedicated staff within OMI reviews all SRO referrals, including referrals that identify potentially suspicious trading. If OMI determines that an SRO referral is related to an existing investigation, that referral is directed to the relevant investigative group. SRO referrals not deemed related to an ongoing investigation are further analyzed by OMI to assess a variety of factors. After this review, OMI directs the SRO referrals to appropriate investigative staff across all of the SEC's offices, to other regulatory agencies, or to the SEC's Office of Compliance Inspections and Examinations. In certain instances, OMI closes some SRO referrals with no further action but maintains the information contained in them for future intelligence gathering.

Once potentially suspicious trading is identified – whether from an SRO referral or from other sources of investigative leads – and an investigation is commenced, Enforcement staff undertake the often painstaking work of collecting and analyzing trading data across equity and options markets, communications (email, telephone calls and instant messages, among others) and market-moving events (e.g., corporate earnings, product development, and acquisitions and mergers) to identify persons who may have engaged in insider trading. Next, Enforcement staff must establish a provable case by identifying, among other things, the source and materiality of the inside information and evidence that the trader knew or should have known the information was obtained by deception or in violation of a fiduciary or other duty.

Throughout our investigative process, Enforcement staff has available a range of investigative techniques. In addition to traditional investigative techniques such as testimony and document review and analysis, we have new tools. These include seeking assistance from cooperating witnesses – both through the SEC's new cooperation initiative established in January 2010 and the existing programs available to criminal authorities – that encourage key fact witnesses to provide valuable information. We also are hopeful that our new Whistleblower Program,

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[1] Prior to the creation of OMI, SRO referrals were accepted and reviewed by the Enforcement Division's Office of Market Surveillance.

[2] During that same timeframe, the SEC received a total of 1,666 SRO referrals. A number of these referrals relate to existing Enforcement investigations.

authorized under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 and which will be effective as of August 12, 2011, will prove helpful in the effort to combat insider trading.

The Division of Enforcement also is integrating SRO referrals into the TCR system to allow staff to search across all SRO referrals and identify traders that may be common to multiple referrals. In addition, we continue to develop our Automated Bluesheet Analysis Project ("ABAP"), spearheaded by the Division of Enforcement's new Market Abuse Unit. The ABAP seeks to more effectively utilize the "bluesheet" database of over 1 billion electronic equities and options trading records obtained by the Division in connection with investigations over the last 20 years.[3] At the beginning of virtually all investigations concerning possible market abuse, Enforcement staff submit bluesheet requests and load the resultant trading data into the bluesheet database. Prior to the development of the ABAP, investigative staff were limited to searching trading data supplied in response to particular bluesheet requests. We currently are developing templates that enable staff to search across this aggregated collection of trading data, conducting automated searches for suspicious trading patterns and identifying relationships and connections among multiple traders and across multiple securities. This project can generate significant enforcement leads and investigative entry points, including investigative leads that may relate back to prior investigations where such connections could not be established. While still in the process of being developed, Enforcement's new data analytic approaches already have led to significant insider trading enforcement actions that did not originate from an SRO referral, informant tip, investor complaint, media report, or other external source.[4]

In addition, Enforcement's new Asset Management Unit is responsible for an Aberrational Performance Inquiry project using risk-based analytics created by the SEC's Division of Risk, Strategy, and Financial Innovation to analyze performance data of thousands of hedge fund advisers and identify candidates appropriate for examination or investigation. As part of the evaluation process, staff from the Unit and the SEC's Office of Compliance Inspections and Examinations consider private funds and advisers that also have been subjects of SRO referrals. Every regional office of the SEC has worked on examinations and/or investigations arising from this initiative.

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[3] Each "record" within a bluesheet request represents a line of trading data: ticker symbol, date, purchaser or seller's name, address, the type of execution (buy or sell), account number, broker name, MPID number and related data.

[4] *See, e.g., SEC v. Nicos Achilleas Stephanou, Ramesh Chakrapani, Achilleas Stephanou, George Paparrizos a/k/a Georgios Paparrizos, Konstantinos Paparrizos, Michael G. Koulouroudis and Joseph Contorinis*, Civil Action No. 09 CV 1043 (S.D.N.Y. Feb. 5, 2009), http://www.sec.gov/litigation/litreleases/2009/lr20884.htm; *SEC v. James W. Self Jr. and Stephen R. Goldfield*, Civil Action No. 10-CV-4430-ER (E.D.P.A. Sept. 1, 2010), http://www.sec.gov/litigation/litreleases/2010/lr21638.htm; *SEC v. Jeffery J. Temple and Benedict M. Pastro*, Case No. 10-CV-1058 (D. Del., December 7, 2010), http://www.sec.gov/litigation/litreleases/2010/lr21765.htm; *SEC v. Jonathan Hollander*, Civil Action No. 11-CV-2885 (S.D.N.Y. April 28, 2011), http://www.sec.gov/litigation/litreleases/2011/lr21950.htm.

The SEC's Ongoing Efforts To Combat Insider Trading

While insider trading has always been a high priority for the Commission, we are in a period of historic insider trading enforcement at the SEC. In fiscal year 2010, the SEC brought 53 insider trading cases against 138 individuals and entities, a 43 percent increase in the number of filed cases from the prior fiscal year.

In particular, the SEC has filed numerous actions against financial professionals alleging insider trading involving hedge funds and their related feeder funds. Several recent actions against analysts and traders currently or formerly affiliated with hedge funds are indicative of our substantial efforts in this area.[5] Additional examples of some of our more significant recent insider trading cases include:

- The wide-ranging and complex *Galleon* line of cases where the SEC has charged 29 defendants, including Raj Rajaratnam and various employees of his hedge fund, for allegedly making approximately $90 million of illicit gains from insider trading in the securities of over a dozen publicly traded companies;
- The Expert Networks line of cases (which arose out of the Galleon investigation) in which the SEC has charged hedge funds, hedge fund employees and four technology company employees who, while moonlighting as consultants or "experts" without the knowledge of their employers, abused their access to inside information about technology companies such as AMD, Apple, Dell, Flextronics, and Marvell and passed it to the funds. The illicit gains alleged by the SEC in this investigation, which is continuing, exceed $30 million.
- The *Cutillo* line of cases where the SEC has charged nine defendants in a case involving serial insider trading by a ring of Wall Street traders and hedge funds who made over $20 million trading ahead of corporate acquisition announcements using inside information tipped by attorneys at the international law firm of Ropes & Gray LLP, in exchange for kickbacks;
- The *Nicos Stephanou* line of cases, in which the Commission alleged over $11.6 million in profits and charged eight individuals, including Jonathan Hollander, an analyst at CR

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[5] *See, e.g., SEC v. Jonathan Hollander*, Civil Action No. 11-CV-2885 (S.D.N.Y. April 28, 2011), Litigation Release No. 21950 (April 28, 2011), http://www.sec.gov/litigation/litreleases/2011/lr21950.htm; *In the Matter of Jonathan Hollander*, Administrative Proceeding File No. 3-14398 (May 19, 2011), http://www.sec.gov/litigation/admin/2011/ia-3208.pdf; *SEC v. Mark Anthony Longoria, Daniel L. DeVore, James Fleishman, Bob Nguyen, Winifred Jiau, Walter Shimoon, Samir Barai, Jason Pflaum, Barai Capital Management, Noah Freeman, and Donald Longueuil*, Civil Action No. 11-CV- 0753 (S.D.N.Y. February 8, 2011), Litigation Release No. 21844 (February 8, 2011), http://www.sec.gov/litigation/litreleases/2011/lr21844.htm; *SEC v. Robert Feinblatt, Jeffrey Yokuty, Trivium Capital Management LLC, Sunil Bhalla, and Shammara Hussain,* Civil Action No. 11-CV-0170 (S.D.N.Y. January 10, 2011), Litigation Release No. 21802 (January 10, 2011), http://www.sec.gov/litigation/litreleases/2011/lr21802.htm; *SEC v. Galleon Management, LP, Raj Rajaratnam, Rajiv Goel, Anil Kumar, Danielle Chiesi, Mark Kurland, Robert Moffat, New Castle Funds LLC, Roomy Khan, Deep Shah, Ali T. Far, Choo-Beng Lee, Far & Lee LLC, Spherix Capital LLC, Ali Hariri, Zvi Goffer, David Plate, Gautham Shankar, Schottenfeld Group LLC, Steven Fortuna, and S2 Capital Management, LP*, Civil Action No. 09-CV-8811 (S.D.N.Y. November 5, 2009), Litigation Release No. 21284 (November 5, 2009), http://www.sec.gov/litigation/litreleases/2009/lr21284.htm; *In the Matter of Ali T. Far and Choo-Beng Lee,* Administrative Proceeding File No. 3-13891(May 12, 2010), http://www.sec.gov/litigation/admin/2010/ia-3027.pdf.

Intrinsic, and which resulted in the guilty pleas of Nicos Stephanou, George Paparrizos and Michael Koulouroudis and a guilty verdict against Joseph Contorinis, a portfolio manager for the Jeffries Paragon Fund;

- The *Garret Bauer* case, a $37 million insider trading case, in which the Commission charged trader Garrett Bauer and Matthew Kluger, a mergers and acquisitions ("M&A") attorney who worked at the law firm Wilson Sonsini and tipped Bauer on eight M&A transactions in which the law firm was counsel; and
- The *Cheng Yi Liang* case, a $3.6 million case, in which the Commission charged a Federal Drug Administration ("FDA") chemist for trading in advance of at least 27 public announcements about FDA drug approval decisions involving 19 publicly traded companies.

As noted above, subject to our obligations to protect confidential and nonpublic investigative information, we would welcome the opportunity to brief your staff further on our insider trading enforcement initiatives, including our cooperation initiative, the Automated Bluesheet Analysis Project, methods of analyzing referrals, and related information.

Please call me at (202) 551-4894 or have your staff call Eric Spitler, Director of the Office of Legislative and Intergovernmental Affairs, at (202) 551-2010 if you have any questions or comments.

Sincerely,

Robert Khuzami

Robert S Khuzami