

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

COPY

In the Matter of:)
) File No. OIG-509
OIG-509)

WITNESS: Number 73

PAGES: 1 through 45

PLACE: Securities and Exchange Commission

100 F Street, N.E., Room 6465

Washington, D.C. 20549

DATE: Wednesday, August 5, 2009

The above-entitled matter came on for hearing, pursuant to notice, at 2:55 p.m.

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1 APPEARANCES:

2

3 On behalf of the Securities and Exchange Commission:

4 H. DAVID KOTZ, ESQ., Inspector General

5 HEIDI STEIBER, ESQ., Investigator

6 Office of Inspector General

7 Securities and Exchange Commission

8 100 F Street, N.E.

9 Washington, D.C. 20549

10 202-551-6037

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12 On behalf of the Witness:

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P R O C E E D I N G S

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2 MR. KOTZ: We are on the record at 2:55 p.m. on
3 August 5th, 2009, at the United States Securities and
4 Exchange Commission Office of Inspector General. I'm going
5 to swear you in. Would you please raise your right hand?
6 Whereupon,

7 [REDACTED]
8 was called as a witness and, having been duly sworn, was
9 examined and testified as follows:

EXAMINATION

10
11 BY MR. KOTZ:

12 Q Could you state and spell your full name for the
13 record.

14 A [REDACTED]. [REDACTED] is
15 [REDACTED].

16 Q [REDACTED], my name is David Kotz. I'm the
17 Inspector General of the United States Securities and
18 Exchange Commission. I have with me Heidi Steiber, also with
19 the Office of Inspector General. This is an investigation by
20 the Office of Inspector General, Case Number OIG-509. I'm
21 going to ask you certain questions. You have to provide
22 answers under oath. The court reporter will record and later
23 transcribe everything that is said. Please therefore provide
24 verbal answer to the questions as a nod of the head or
25 another nonverbal response won't be able to be picked up by

1 the court reporter.

2 Also so the record will be clear, please let me
3 finish my question before you provide your response. In
4 addition, it is important that you understand the questions
5 and give accurate answers. So if there's anything you don't
6 understand or anything you do not know or are not sure about,
7 please let me know. Otherwise, I will assume that you heard
8 and understood the question. Do you understand those
9 instructions?

10 A Yes.

11 Q I'll give you the standard perjury warning. As you
12 can see, your responsive statements given today are provided
13 after you've sworn an oath and will be taken down verbatim by
14 the court reporter. This is an official U.S. government law
15 enforcement investigation. The claims asserted in this case
16 are serious ones. It is very important that you tell me
17 everything you know about the matter at hand and are
18 completely forthcoming and truthful with me. I'm formally
19 advising you your testimony today is subject to the laws of
20 perjury. Providing false or misleading testimony under oath
21 is a very serious offense. If the evidence shows the
22 testimony you have given is false will be referred as
23 appropriate. Do you understand those instructions?

24 A Yes I do.

25 Q Great. Okay. Could you tell me first your current

1 Q So you believe that Salazzo declined your proposal
2 of having a front running exam relating to specialist firms
3 because he didn't generally want to look at those type of
4 fraud-related matters that would have to then be referred to
5 Enforcement?

6 A Well, yes, for those two reasons. One, he didn't
7 want to look into fraud-related matters. And two, I don't
8 think he enjoyed helping out the Enforcement people. You'd
9 have to get into his head to find out why he didn't want to
10 do these things, but it appeared to me that he just wanted to
11 do what he was good at. And he was a very good accountant.
12 I mean, he loved accounting. He still loves accounting as
13 far as I know. I remember, this is the type of guy who when
14 the new GAAP or GASP book came out, the tedious rules, the --
15 he would run out and get it. So that's what we're talking
16 about here. He would -- you know, he was very fastidious
17 about that. And he was a very good accountant. From all
18 accounts from the accountants that I thought were good, and I
19 have a financial background. I have an Personal Privacy, and he
20 was a superb accountant. I mean, he loved the stuff. But
21 when it came to fraud, he just didn't want to get involved in
22 it for whatever reason.

23 BY MS. STEIBER:

24 Q Did you feel like there was a competition in some
25 ways between OC and Enforcement that was coming from OC?

1 Like you said they didn't want to help them out.

2 A Well, that's an interesting question. Above Bob
3 Salazzo was a person who I was -- I sat pretty well with, and
4 his name is Marty Kuperberg. And Marty knew the importance
5 of enforcement cases. So for the time that I was there,
6 there was that tension.

7 Bob and Marty got along very well, but I remember
8 one time Marty said this is the least enforcement-oriented
9 associate director in the Commission. I remember him saying
10 that in front of -- saying it jokingly, but it was true, as
11 far as I could see. And there was -- but Marty knew that
12 there was an importance of bringing those cases, and Marty
13 knew that he needed to have a bunch of specialized lawyers
14 who could handle broker-dealer cases. So he formed that
15 group within the OC, and so he had this -- he formed that
16 group within OC in New York, and he had a group of attorneys
17 who were dedicated to bringing cases that came out of the
18 examination staff.

19 But Bob tried to keep us from doing that sort of
20 work. It got to the point where the attorneys -- to me, the
21 attorneys would come to me. **personal privacy**. They
22 would come to me for help. And more and more I kind of
23 prevailed and I got to work on those cases. But the
24 competition did exist between the OC attorneys and the
25 traditional enforcement attorneys in the New York Office.

1 Q Right.

2 A But from what I understand, it was an exam that was
3 targeting whether or not a ^{Examination Material} had
4 mismarked their fixed-income securities.

5 Q Do you think that was a cause exam?

6 A I would say yes, but I'm not sure. And, you know,
7 the only reason that gives me pause in thinking, I just can't
8 imagine someone being so silly as to write we're looking at
9 ^{Examination Material} because we want to see if they're
10 mismarking, you know, like what is it, an ethnic trend? You
11 know, it's just too absurd to write down on a form. So it
12 might have been just the wise thing to do. Let's go out to
13 all these ^{Examination Material} so that if Washington comes
14 down and says something, we can say we covered our bases. I
15 don't know.

16 BY MS. STEIBER:

17 Q Just to summarize, we've had some testimony that
18 the examination program misses the forest from the trees, and
19 it sounds like what you've been saying is it chooses to miss
20 the forest for the trees.

21 A I would say in certain cases they choose to miss
22 the forest for the trees. I used the term I think with him,
23 "blind eye." So --

24 Q It's a willful blindness?

25 A Well, a willful blindness has got the criminal

1 connotation. I don't want to go there. But I will say that
2 they turned a blind -- they did not want to see it, because
3 if they saw it, they would have to do something about it.
4 And they didn't want to. It's my take that they just didn't
5 want to get involved.

6 BY MR. KOTZ:

7 Q So you believe when Salazzo would do these
8 examinations, he would not want to look for or find fraud
9 because then he would have to deal with those issues?

10 A Yes. But the ^{Examination Material} case is taking it a step
11 above.

12 Q Right.

13 A I the ^{Examination Material} case, you know, I don't think you
14 could miss this. This was --

15 Q You couldn't miss it unless you wanted to miss it?

16 A Yeah. Well, I --

17 Q And you think Salazzo wanted to miss it?

18 A Yeah. I mean, because the person -- and we can get
19 it -- I wish the documents were around -- the people who were
20 supposed to be monitoring ^{Personal Privacy} trading were ^{Personal Privacy}
21 ^{Personal Privacy} and ^{Personal Privacy}. And they were both very close
22 friends of Bob Salazzo, very close friends. When ^{Personal Privacy}
23 ^{Personal Privacy}, Bob spent hours on the phone, from
24 what I understand during my stay here, he spent hours on the
25 phone trying to ^{Personal Privacy}. They are

1 extremely close, and [Personal Privacy], too. And [Personal Privacy] a good guy. I
2 don't know that much about [Personal Privacy] because he left before I got
3 there.

4 But those two people were going to take the fall
5 for this mismarking, and I think that -- you know, I don't
6 have any direct evidence of that, but you can't tell me that
7 an accountant who's that good, going into a firm, looking for
8 mismarking of fixed-income securities, can miss that. I
9 mean, that's -- it's not being hid.

10 BY MS. STEIBER:

11 Q Are you aware of any other instances in which
12 Salazzo made decisions whether to go forward with the case or
13 how hard to examine a firm based on personal relationships or
14 the prominence of individuals?

15 A No. That was the only one. And that was actually
16 something that stuck with me. You know, I was outside the
17 office and I was working for the law firm and I couldn't say
18 anything about it because, you know, I'm representing my
19 client, and he got a really good settlement out of it. You
20 know, if you want to you know what happened on that case, it
21 wasn't a mismarking. All the traders on the [Personal Privacy] trading desk
22 were dumping their securities into this one person's account.
23 He was going to get fired the year before, but they let him
24 stay on a year so that they can dump all the securities in
25 his account, so that they can get a bonus.