

ACT

UNITED STATES OF AMERICA  
Before the  
SECURITIES AND EXCHANGE COMMISSION  
June 8, 2007

SECURITIES & EXCHANGE COMMISSION  
MAILED FOR SERVICE

JUN 11 2007

FIRST CLASS

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In the Matter of	:	ORDER CONCERNING THE DIVISION
	:	OF ENFORCEMENT'S DUTY TO
MICHAEL SASSANO,	:	PROVIDE ACCESS TO CERTAIN
DOGAN BARUH,	:	NON-PRIVILEGED INVESTIGATIVE
ROBERT OKIN, and	:	MATERIALS FROM NY-7220
R. SCOTT ABRY	:	

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Rule 230(a)(1) of the Rules of Practice of the Securities and Exchange Commission (Commission or SEC) requires the Division of Enforcement (Division) to make available for inspection and copying by Respondents "documents obtained by the Division prior to the institution of proceedings, in connection with the investigation leading to the Division's recommendation to institute proceedings." Rule 230(d) of the Commission's Rules of Practice provides that the Division shall commence making documents available to Respondents for inspection and copying no later than seven days after service of the Order Instituting Proceedings (OIP). Rule 230(c) of the Commission's Rules of Practice authorizes the presiding Administrative Law Judge (ALJ) to require the Division to prepare a privilege log, if the Division withholds any documents from inspection and copying.

#### Omnibus Formal Orders of Investigation

The Commission occasionally grants the Division authority to issue subpoenas and take testimony under an omnibus formal order of investigation. When the Commission issues such an omnibus order, it typically involves a particular type of misconduct that may have occurred in a variety of settings, not all of which are known to the Division's staff when the Commission authorizes the Division to investigate. As the enforcement staff learns of specific individuals and entities who might have engaged in the misconduct contemplated by the omnibus formal order of investigation, the Division's staff uses a procedural shortcut: it commences new sub-investigations without approaching the Commission to seek new formal orders of investigation. The issue for decision concerns the scope of the documents that the Division must make available to Respondents under Rule 230 in such circumstances.

#### Background

The Commission issued its OIP in this matter on January 31, 2007. By letter dated February 14, 2007, the Division informed me that it "anticipate[d] completing its obligations under Rule 230(a) by the end of next week." On February 15, 2007, I ordered the Division to provide evidence that it had complied with Rules 230(a)(1) and (d). In that same Order, I required the Division to prepare an itemized privilege log. By pleading dated February 16, 2007,

the Division stated that it “anticipate[d] completing its disclosures by February 23, 2007.” On March 7, 2007, the Division filed a 240-item privilege log.

At the first prehearing conference, the Division estimated that its case-in-chief would involve 10 to 15 witnesses or “maybe a few more,” plus hundreds of exhibits (Prehearing Conference of Mar. 6, 2007, at 27-29). The Division submitted its proposed witness and exhibit lists on May 11, 2007. The Division’s proposed witness list includes 45 individuals. The Division’s proposed exhibit list includes thousands of exhibits relating to 83 mutual fund families, 18 annuity fund families, 6 hedge funds, and 2 trading platforms.

### The Parties’ Pleadings

On May 29, 2007, Respondent Michael Sassano (Sassano) sought an order directing the Division to produce documents and transcripts relevant to this proceeding from the Division’s nationwide, omnibus investigation of market timing and late trading in the mutual fund industry (Motion). Sassano demonstrated that the Commission issued an Order Directing Private Investigation and Designating Officers to Take Testimony, In re Certain Mutual Fund Trading Practices, NY- 7220, on September 10, 2003. The exhibits to Sassano’s Motion showed that the Division’s proposed exhibit list includes many documents obtained under the authority of the Commission’s omnibus formal order of investigation in NY-7220. Sassano argues that NY-7220 is therefore the investigation that led to the institution of this proceeding, and that he is entitled to inspect and copy all documents gathered by the Division during the course of NY-7220.<sup>1</sup> Sassano contends that the Division’s refusal to provide access to these materials has substantially prejudiced his ability to prepare for the hearing. Respondent R. Scott Abry later joined in Sassano’s Motion.

On June 5, 2007, the Division argued that Sassano’s motion should be denied (Opposition). According to the Division, its Northeast Regional Office opened a “case number,” NY-7273, on January 29, 2004, for an “ongoing” investigation of market timing and late trading at Canadian Imperial Bank of Commerce. The Division acknowledges that the Commission never issued a formal order of investigation in NY-7273 and, in fact, that the Commission did not issue another formal order concerning market timing and late trading, other than NY-7220. The Division also acknowledges that it took testimony and subpoenaed documents relating to the present OIP under the authority of the Commission’s formal order of investigation in NY-7220. The Division has provided some (but not all) of these materials from NY-7220 to Respondents. Nonetheless, when the Division requested the Commission to issue the present OIP, its Action Memorandum identified NY-7273, not NY-7220, as the only relevant investigation.

On June 7, 2007, Sassano submitted his reply to the Division’s Opposition (Reply).

### Discussion

At issue is the meaning of Rule 230(a)(1)’s phrase “documents obtained . . . in connection with the investigation leading to the Division’s recommendation to institute

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<sup>1</sup> The Division took a contrary position during the Prehearing Conference of May 17, 2007, at 68-72. This was the first notice I had of the parties’ dispute about the relevant investigation numbers.

proceedings.” Sassano urges an expansive reading, while the Division favors a narrow interpretation. Sassano has the better of the argument.

When the Commission revised its Rules of Practice in 1995, it prepared a series of Comments on the new rules for the benefit of the public. The Comments are statements explaining the basis for a rule, describing the rule’s rationale, referencing related rules, or providing information concerning pertinent Commission practice. The Comments are not a part of the rules, and are not included in the Code of Federal Regulations. However, the Commission published its Comments in the Federal Register. The Commission believed that the information in the Comments would assist persons consulting the rules in a more thorough understanding of the Rules. See Rules of Practice, 60 Fed. Reg. 32738, 32739 (June 23, 1995) (preamble to final rules). The Commission continues to cite the Comments to various Rules of Practice in its opinions and orders. See, e.g., Navistar Int’l Corp., Securities Exchange Act of 1934 Release No. 55304, 2007 SEC LEXIS 319, at \*8 n.12 (Feb. 13, 2007) (Order Denying Stay) (citing Comment to Rule 401).

In relevant part, Comment (a) to Rule 230 provides:

The “investigation leading to the Division’s recommendation to institute proceedings” ordinarily is delineated by the investigation number or numbers under which requests for documents, testimony or other information were made. When an investigation is initiated by the Division . . . it is assigned a number, often referred to as the “case” or “investigation” number. Each request for documents, testimony or other information from persons not employed by the Commission specifies the investigation or preliminary investigation number to which it relates. In turn, each written recommendation by the Division . . . to institute proceedings identifies on its cover page, by investigation number, the source investigation or investigations to which it relates. Accordingly, the identity and content of the appropriate investigation file or files from which documents must be made available can be based on objective criteria.

Rules of Practice, 60 Fed. Reg. at 32762 (emphasis added). The Division maintains that Sassano’s Motion should be decided only by reference to the “plain language” of the text of Rule 230(a). This is a veiled request to ignore Comment (a) to Rule 230. Unlike the Division, I consider the text of Rule 230(a) to be somewhat ambiguous on the point in dispute. The Division also asserts that Rule 230(a) does not tie the Division’s production obligations to a formal order number (Opposition at 2, 6). Comment (a) to Rule 230 suggests otherwise. The Commission has never disavowed Comment (a) to Rule 230. I am aware of no reason why Comment (a) to Rule 230 should not be consulted when resolving the present dispute.

I reject the Division’s argument that NY-7273 is the only relevant investigation here. The exhibits to Sassano’s Motion show otherwise. I give limited weight to the fact that the Division’s Action Memorandum to the Commission identified NY-7273, but not NY-7220, as the source investigation. This is merely bootstrap evidence, designed to support the Division’s call for the narrowest possible interpretation of its Rule 230(a) production obligations. The question is not whether the caption of the Action Memorandum here was consistent with the captions of prior Action Memoranda arising from other omnibus formal orders of investigation. Rather, the question is whether the Division’s captioning practice is likely to survive scrutiny by a court of appeals.

I also reject Sassano's claim that Rule 230 entitles Respondents to inspect and copy all of the non-privileged documents obtained by the Division in connection with its nationwide, omnibus investigation in NY-7220 (Motion at 6; Reply at 4).<sup>2</sup> Finally, I reject Sassano's assertion that Rule 230 entitles Respondents to inspect and copy non-privileged documents obtained by the Division in connection with its investigation in NY-7220 relating to any entity that currently employs or formerly employed any person referenced in the OIP or the Division's list of proposed witnesses; and any other individual or entity from or about whom the Division intends to offer evidence at the hearing (Motion at 6-7 n.5).<sup>3</sup>

I accept Sassano's argument that Respondents are entitled to inspect and copy the non-privileged documents obtained by the Division in NY-7220 relating to any of the mutual funds, annuity funds, hedge funds, trading platforms, and individuals referenced in the OIP, as clarified by the letter dated May 18, 2007, from Mark D. Salzberg to Shawn P. Naunton, and the Division's proposed exhibit list (Motion at 6-7 n.5). Respondents are also entitled to inspect and copy the non-privileged documents obtained by the Division in any other investigations that were not part of the omnibus NY-7220 investigation, but yielded documents that may become Division exhibits in this proceeding, including C-3781, In re Ritchie Capital Management, and B-1229, In re Prudential Securities. This ruling applies to documents obtained by the Division's headquarters office and any Division Regional Office. It is not limited to documents previously reviewed by the Sassano prosecutorial team in the Division's Northeast Regional Office.

#### Remedy

The hearing in this matter is scheduled to begin on July 9, 2007. The Division opposes any delay of the hearing (Prehearing Conference of Apr. 10, 2007, at 8-15; Order of Apr. 10, 2007, at 2; Opposition at 2 (characterizing Sassano's Motion as "simply an eleventh-hour litigation tactic aiming to delay these proceedings")). Accordingly, the remedy I have chosen keeps the Division's concern in mind.

It is now apparent that the Division has not yet completed its Rule 230 production responsibilities. In particular, the Division's letter of February 14 and its pleading of February 16 are inaccurate, and that the Division's privilege log of March 7 is, in all likelihood,

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<sup>2</sup> Additional guidance is often available from considering the practice of other federal agencies. Rule 10.42 of the Rules of Practice of the Commodity Futures Trading Commission (CFTC), 17 C.F.R. § 10.42, is quite similar to the SEC's Rule 230. CFTC Rule 10.42(b)(3) provides in pertinent part:

When the investigation by the [CFTC's] Division of Enforcement that led to the pending proceeding encompasses transactions, conduct or persons other than those involved in the proceeding, the requirements of [CFTC Rule 10.42(b)(1)] shall apply only to the particular transaction, conduct and persons involved in the proceeding.

<sup>3</sup> Sassano's interest in obtaining exculpatory information pursuant to Rule 230(b)(2) plays no role in identifying "the investigation leading to the Division's recommendation to institute proceedings." This aspect of Sassano's Motion is plainly a fishing expedition.

substantially incomplete. See supra pp. 1-2. Because the hearing date is fast approaching, I will require the Division to cure these deficiencies by June 15, 2007. See Rule 180(b) of the Commission's Rules of Practice (providing that an ALJ may direct a party to cure a deficient filing and resubmit it within a fixed period of time).

If the Division is unable or unwilling to produce all relevant, non-privileged evidence gathered pursuant to the nationwide, omnibus formal order of investigation in NY-7220, and to cure its deficient filings within the time specified, I will impose an appropriate sanction. See Rule 180(c) of the Commission's Rules of Practice (authorizing an ALJ, among other things, to prohibit the introduction of evidence or exclude testimony if a person fails to cure a deficient filing within the time specified pursuant to Rule 180(b)).

The Division identifies several practical problems that might result if it is compelled to make available its investigative file in NY-7220. It represents that the documents gathered pursuant to the authority of NY-7220 are not maintained in a single location, but rather, are housed in the Division's headquarters office and in several Regional Offices. The Division further asserts that, if it is given a second chance to make proper production, it might take dozens of staff attorneys several months to identify and assemble the relevant documents, review them for privilege, amend its March 7 privilege log, and then make the non-privileged documents available to Respondents. These are matters the Division should have considered before it asked the Commission to issue the OIP.

The Division implicitly assumes that it should be granted an extended second chance to complete its Rule 230 production responsibilities. The assumption is unwarranted. Another ALJ has already ruled against the Division on a similar issue in a companion case, Administrative Proceeding No. 3-12386, Warren Lammert. Although the ALJ in Lammert ultimately required the Division to produce only the files from two sub-investigations, the ALJ's order was based on a determination that all the mutual fund investigations conducted under the authority of the omnibus formal order constituted one investigation for purposes of Rule 230. See Lammert Prehearing Conference of Feb. 9, 2007, at 8, 10, 27-31, 56-57 (official notice). The Division has been aware of the Lammert ruling since February 7-9, 2007, and its efforts to distinguish Lammert in its Opposition were unpersuasive. Moreover, the Commission imposed a decision-making deadline of 300 days in this proceeding. See OIP ¶ IV; Rule 360(a)(2) of the Commission's Rules of Practice. Absent extraordinary circumstances, the parties are not entitled to "mulligans" in cases subject to the decision-making deadlines.<sup>4</sup>

If the Division so chooses, it may circumscribe its duty to produce materials from NY-7220 by scaling back on the thousands of exhibits it intends to offer and/or the 45 witnesses it intends to call at the hearing. The choice of how to proceed is up to the Division, but it must make its choice known by June 15, 2007.

#### ORDER

Sassano's motion is granted in part and denied in part, as explained above. If the Division intends to introduce evidence at the July 9 hearing that it gathered pursuant to


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<sup>4</sup> A "mulligan" is a free shot sometimes given a golfer in informal play when the previous shot was poorly played. Merriam-Webster's Collegiate Dictionary 764 (10th ed. 1998).

subpoenas authorized by NY-7220, then it must provide Respondents with access to all the relevant, non-privileged evidence that it gathered pursuant to the nationwide, omnibus formal order of investigation in NY-7220. It must also supplement its March 7, 2007, privilege log to identify with particularity any additional documents from NY-7220 that it withholds from inspection and copying.<sup>5</sup> The Division must complete production and amend its privilege log by June 15, 2007.<sup>6</sup>

If the Division is unable or unwilling to provide Respondents with access to the relevant, non-privileged portions of its investigative file in NY-7220 by June 15, 2007, then it may not introduce at the July 9 hearing any evidence that it gathered pursuant to subpoenas authorized by NY-7220. See Rules 180(b) and (c) of the Commission's Rules of Practice.

SO ORDERED.

  
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James T. Kelly  
Administrative Law Judge

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<sup>5</sup> Consistent with my Order of February 15, 2007, any additional withheld documents must be identified with particularity: i.e., date, length, subject matter, author, addressee, and all claimed grounds for withholding. Identification of additional withheld materials by category will not be sufficient. Inasmuch as the Division's current privilege log ends with entry # 240, it is suggested that the Division commence any supplemental privilege log with entry # 241.

<sup>6</sup> If the Division intends to introduce evidence at the July 9 hearing that it gathered pursuant to subpoenas authorized by other formal orders of investigation, such as C-3781 or B-1229, the Division must provide Respondents with access to all non-privileged documents in those investigative files by June 15, 2007, as well.