

For Immediate Release

Wednesday, June 3, 2009

Grassley asks regulator how it handled allegations of insider trading

WASHINGTON --- Senator Chuck Grassley is asking the Financial Industry Regulatory Authority – the securities industry’s own regulator – to explain how it handled allegations made in April 2008 about insider trading and other violations of the rules and regulations that govern capital markets.

“The allegations in question, if validated, would be serious violations of the law,” Grassley said. “The public needs to know that watchdogs are on the job and aggressively policing the marketplace for the good of every investor and confidence in the system. I expect to get a full accounting of what the enforcement division of FINRA did with the information it got about possible wrongdoing.”

Earlier this year, Grassley asked the Securities and Exchange Commission for the status of its investigation into the same allegations. A copy of Grassley’s February 2009 inquiry is posted with this news release at <http://finance.senate.gov> and <http://grassley.senate.gov>.

FINRA is the largest independent regulator for all securities firms doing business in the United States. According to FINRA, it oversees nearly 5,000 brokerage firms, 173,000 branch offices and 653,000 registered securities representatives.

Here is the text of Grassley’s letter to FINRA.

June 2, 2009

Richard G. Ketchum  
Chairman and Executive Officer  
Financial Industry Regulatory Authority, Inc.  
1735 K Street, NW  
Washington, DC 20006-1506

Dear Mr. Ketchum:

Recently, Congress has focused its attention on the shortcomings of the Enforcement Division of the Securities and Exchange Commission (SEC). The Financial Industry Regulatory Authority (FINRA) is charged with similar responsibilities in overseeing the securities industry. Considering that FINRA is the front-line in regulating broker-dealers, it should be particularly concerned with following up on tips from a variety of sources.

In a February 19, 2009 letter to the SEC, I expressed concern about the Enforcement Division’s response to a whistleblower’s allegations that Lehman Brothers (Lehman) systematically and regularly engaged in insider trading by releasing the content of equity

research reports to select sales executives, traders, and clientele prior to the report's public release (see Exhibit 1). These same allegations were set forth in the complaint of an NASD arbitration proceeding for wrongful termination filed by Edward Parmigiani in May 2006, NASD Case No. 06-01903 (see Exhibit 2). These insider trading allegations demonstrate violations not only of federal securities laws and several rules within section 501 of the Sarbanes-Oxley Act, but also appear to demonstrate violations of FINRA rules and regulations, specifically IM-2110-4.<sup>1</sup> Page ten of the complaint described four specific examples of such violations by Lehman employees, including (1) a salesman stating that he had to "get back to the office and start calling clients since (Lehman) is going to be downgrading U.S. Commodity Chemicals sector on the 2:15 pm today;" (2) Mr. Parmigiani receiving a call from a client who asked if Dan Niles was downgrading Altera and Xilinx; (3) Mr. Parmigiani receiving calls from two hedge funds about MEMC while he was working on research about MEMC Electronic Materials; and (4) Amkor stock began trading actively within a thirty minute period between when Mr. Parmigiani submitted his research to Lehman personnel and the research was made public.

In addition to those issues outlined in the February 19<sup>th</sup> letter, there appear to be violations of other FINRA rules and regulations outlined in the arbitration complaint. In particular, there are facts that illustrate improper interactions between the Investment Banking Department and Research Department at Lehman that would violate numerous sections of FINRA Rule 2711. The various violations set forth in Mr. Parmigiani's complaint include: (1) on page three, an executive warning to Mr. Parmigiani not to downgrade ChipPac because Lehman was engaged in underwriting transactions with ChipPac; (2) on page four, Mr. Parmigiani being pressured to become the coverage analyst for ChipMOS, even though Mr. Parmigiani was the "source" of Lehman's underwriting business with ChipMOS; (3) on page six, an executive telling Mr. Parmigiani to be "very careful" with the way Mr. Parmigiani covered Micron Technology because of Lehman's business relationship with Micron and Lehman Chairman and CEO Richard S. Fuld's role as Senior Relationship Manager "SRM" with respect to Micron; and (5) on page nine, Mr. Parmigiani being pressured by Lehman's research management to prepare an initiation report and launch coverage on Vishay Intertechnology, despite the fact that at that time there was an existing advising transaction by Lehman's banking department.

Considering that the allegations set forth in Mr. Parmigiani's complaint are in direct violation of FINRA rules and regulations, I am curious as to whether these allegations were investigated by your Enforcement Division. I am aware that on March 5, 2009, FINRA created an "Office of the Whistleblower" to handle high-risk tips. However, I am unsure whether the Office of the Whistleblower would effectively uncover violations set forth in other FINRA proceedings, such as those allegations set forth in Mr. Parmigiani's arbitration proceedings.

Accordingly, please schedule a briefing for my staff to discuss the procedures FINRA has in place to refer potential violations uncovered in one division, such as the arbitration unit, to its

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<sup>1</sup> IM-2110-4 states that "Trading activity purposefully establishing, increasing, decreasing, or liquidating a position in an exchange-listed security traded otherwise than on an exchange or a derivative security based primarily upon a specific exchange-listed security, in anticipation of the issuance of a research report in that security, is inconsistent with just and equitable principles of trade and is a violation of Rule 2110."

Enforcement Division. If there is currently no procedure, please explain how FINRA plans to avoid overlooking potential violations set forth in other FINRA proceedings and divisions.

Thank you for your cooperation in this matter.

Sincerely,  
Charles E. Grassley  
Ranking Member