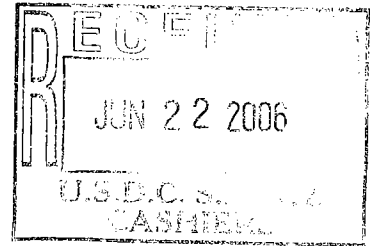


**UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK**



**UNITED STATES SECURITIES AND EXCHANGE
COMMISSION,**

PLAINTIFF,

v.

ALEXANDER J. YAROSHINSKY,

and

VICTOR E. ZAK

DEFENDANTS.

Case No. 06CV2401 (RCC)

AMENDED COMPLAINT

For its complaint against Alexander J. Yaroshinsky and Victor E. Zak, Plaintiff the United States Securities and Exchange Commission (“Commission”) alleges as follows:

SUMMARY

1. This is an insider trading case involving transactions in the securities of Connetics Corp. (“Connetics” or the “Company”) by Alexander J. Yaroshinsky (“Yaroshinsky”), the former Vice President of Biostatistics and Clinical Operations for Connetics, and Victor E. Zak (“Zak”). The Defendants’ trading was conducted in advance of a June 13, 2005 public announcement (the “Announcement”) by Connetics stating that it had received a “not approvable” letter from the Food and Drug Administration (“FDA”) concerning Velac Gel, a developmental stage acne medication that the Company was projecting would contribute significantly to its near-term and long-term financial

performance. After the announcement, Connetics' common stock fell 27% from the previous day's close on volume of more than 30 times its 30-day moving average.

2. On April 13, 2005, two months before the Announcement, Yaroshinsky, in his capacity as Connetics' Vice President of Biostatistics and Clinical Operations, participated on a telephone call with members of the FDA staff responsible for reviewing Velac Gel ("FDA staff"), during which he learned of the comments and conclusions by the FDA's Executive Carcinogenicity Assessment Committee ("ECAC") with respect to the results of a carcinogenicity study of Velac Gel. ECAC serves as the primary consulting body for the FDA on carcinogenicity issues. Its responsibilities include evaluating carcinogenicity study results, data generated from dose selection studies, and proposed carcinogenicity protocols.

3. Yaroshinsky subsequently positioned himself to benefit from a decline in the price of Connetics' securities. From April 26 through June 10, 2005, Yaroshinsky purchased 51 put contracts and sold 15,100 shares of Connetics common stock in his own account and purchased 2,025 Connetics put contracts in a nominee account he controlled.

4. Yaroshinsky communicated the information he learned on the April 13 telephone call with the FDA staff to Zak. Thereafter, from April 13 through June 10, 2006, Zak, who also positioned himself to benefit from a decline in the price of Connetics' securities, purchased 430 Connetics put contracts and sold short 75,000 Connetics shares. In addition, Zak sold a previously-acquired long position of 5,000 Connetics shares.

5. As a result of their unlawful conduct, the Defendants benefited financially by more than \$1.58 million. Specifically, Yaroshinsky benefited financially by more than \$680,000, and Zak benefited financially by more than \$900,000.

6. By virtue of their conduct, Yaroshinsky and Zak violated Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. § 78j(b)] and Rule 10b-5 [17 C.F.R. § 240.10b-5] promulgated thereunder, and, unless enjoined, will continue to engage in transactions, acts, practices, and courses of business similar to

Gel. In 2004, and early 2005, Connetics was projecting publicly that it expected Velac Gel to launch during the fourth quarter of 2005, and the Company and analysts who followed Connetics projected publicly that a launch of Velac Gel would contribute significantly to Connetics' 2005 and 2006 revenues.

16. Before Velac Gel could be sold in the U.S., however, Connetics was required to obtain approval from the FDA. As part of the approval process, the FDA required Connetics to perform a carcinogenicity study on Velac Gel to ascertain the incidence of the formation of skin tumors on mice. Consistent with his responsibilities at Connetics, Yaroshinsky played a role in the development and testing of Velac Gel.

17. From January 2004 through June 2004, Connetics performed the carcinogenicity study on mice. The carcinogenicity study results indicated that out of 160 mice treated with Velac Gel in varying formulations and dosages, 89 mice developed tumors.

18. On June 28, 2004, Connetics convened a panel of toxicology experts to provide feedback on the carcinogenicity study results. At the meeting, the panel convened by Connetics reported that it was unaware of any drug exhibiting a "positive dermal," similar to Velac Gel, that had been approved by the FDA. Yaroshinsky was present at this discussion.

19. On August 24, 2004, Connetics submitted the Velac Gel drug application to the FDA. The application included the results of the carcinogenicity study.

20. On April 13, 2005, at 2:15 p.m. EST, the FDA staff held a conference call with Connetics' staff to discuss the FDA staff's preliminary analysis of the carcinogenicity study results. During the call, the FDA told Connetics that ECAC had

concluded that the Velac Gel vehicle was positive and may be a “tumor promoter or a carcinogen.” The FDA staff further told Connetics that “this is a serious issue for a topical product for the treatment of acne... .” Yaroshinsky was present during this conference call with the FDA.

21. On the same day, at 3:13 p.m. EST, shortly after the teleconference with the FDA ended, Yaroshinsky, using a telephone at Connetics, called his friend and former neighbor Zak, at Zak’s office, and told Zak of the FDA staff’s comments and conclusions. After this call, Zak, who prior to April 13, 2005, maintained a bullish 5,000 share long position in Connetics securities, began executing bearish transactions in Connetics securities. Specifically, at 3:30 p.m. EST, Zak accessed his online brokerage account using his office computer, and sold short 5,000 shares of Connetics. Seventeen minutes later, Zak shorted an additional 2,000 shares and then eight minutes after this sale, Zak sold 3,000 shares from his previously held long position in Connetics securities.

22. Between April 14 and June 10, 2005, Zak sold short a further 68,000 shares of Connetics common stock, sold 2,000 more Connetics shares of his previously held long position, and purchased 430 Connetics put contracts. A put contract is a type of option in which the value of the purchaser’s investment increases in value as the price of the underlying security declines.

23. Zak’s short-selling of Connetics shares and buying of Connetics put options resulted in margin calls from his brokerage firm requiring additional funds to continue trading.

24. On April 14, 2005, the day after the call with the FDA staff, Connetics imposed a two- tier ban on trading in the Company’s securities. The first was to expire

on April 28, 2005, and covered all employees who were present on the FDA call the prior day, which included Yaroshinsky. Connetics also imposed a trading prohibition that extended to May 10, 2005 for employees who participated in preparing additional submissions to the FDA concerning the carcinogenicity study, which also included Yaroshinsky.

25. On the same day the trading ban was imposed, Yaroshinsky arranged for a nominee brokerage account to be opened in the name of his mother-in-law. Yaroshinsky controlled this account.


26. On April 21, while the trading ban was in place, Yaroshinsky purchased 5 put contracts in the nominee account.

27. On April 26, while the trading ban was in place, Yaroshinsky closed a short position consisting of 10 put contracts that he had written in February 2005. The effect of this transaction was to avoid losses that would predictably occur when the news of the non-approval of Velac Gel became public.

28. On April 26, 2005, after the close of the market, Connetics made its first public statement regarding the FDA's April 13 comments. The press release stated that the FDA is "interpreting some of the results of a pre-clinical study [the carcinogenicity study] for Velac Gel differently than the Company...there was a positive response to the product." The release, however, stopped short of disclosing the full extent of the FDA's concerns and the incidence of tumors in the mice tested. Most notably, missing from the release was ECAC's conclusion that the "vehicle was positive in this assay and may be a tumor promoter or a carcinogen." Even the partial disclosure, however, affected Connetics' share price. On April 27, 2005, the price of Connetics shares opened down

otherwise, and each of them, from future violations of Section 10(b) of the Exchange Act [15 U.S.C. §78j(b)] and Rule 10b-5 [17 C.F.R. §240.10b-5] thereunder; ordering Yaroshinsky and Zak to pay an amount equal to all moneys obtained through the illegal activities described above plus prejudgment interest thereon, and to pay civil penalties pursuant to Section 21A of the Exchange Act [15 U.S.C. §78u-1]; and

(b) grant such other relief as this Court deems just and proper.

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Washington, D. C.