

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

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

 ORIGINAL

WITNESS: Number 53

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Securities and Exchange Commission

100 F Street, N.E.

Washington, D.C. 20549

DATE: Thursday, May 21, 2009

The above-entitled matter came on for hearing, pursuant to notice, at 10:38 a.m.

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1 APPEARANCES:

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3 On behalf of the Securities and Exchange Commission:

4 H. DAVID KOTZ, ESQ. Inspector General

5 DAVID FIELDER, ESQ. Asst. Inspector General

6 HEIDI STEIBER, ESQ. Investigator

7 Office of Inspector General

8 Securities and Exchange Commission

9 100 F Street, N.E.

10 Washington, D.C. 20549

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12 On behalf of the Witness:

13 STEPHEN JOHNSON, PRO SE

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1 P R O C E E D I N G S

2 MR. KOTZ: All right, we are on the record at 10:38
3 a.m. on May 21, 2009, United States Securities and Exchange
4 Commission Office of Inspector General.

5 I'm going to swear you in now. Could you please
6 raise your right hand?

7 Whereupon,

8 STEPHEN JOHNSON

9 was called as a witness and, having been first duly sworn,
10 was examined and testified as follows:

11 EXAMINATION

12 BY MR. KOTZ:

13 Q Great. Could you state and spell your full name
14 for the record, please?

15 A Stephen Johnson, S-t-e-p-h-e-n, Johnson,
16 J-o-h-n-s-o-n.

17 Q Great. Mr. Johnson, my name is David Kotz. I'm
18 the Inspector General of the United States Securities and
19 Exchange Commission. I have with me my colleagues David
20 Fielder and Heidi Steiber, both with the office of Inspector
21 General.

22 This is an investigation by the Office of Inspector
23 General, case number OIG-509. I'm going to ask you certain
24 questions, and you will have to provide answers under oath.
25 The court reporter will record and later transcribe

1 A Accounting.

2 Q You were an accountant?

3 A An accountant in the accounting department, general
4 accounting.

5 Q For Con Ed? How long were an accountant for Con
6 Ed?

7 A Eight years.

8 Q So that was between what periods of time?

9 A That would have been '86 to '94.

10 Q Okay. And what did you do in '94?

11 A I went to Herzog, Heine, Geduld, it's a
12 broker-dealer, a NASDAQ market maker.

13 Q Could you spell -- Herzog, I guess, is H-e-r-z-o-g.

14 A R-z-o-g. H-e-i-n-e, and Geduld, G-e-d-u-l-d.

15 Q Okay. And that was a broker-dealer?

16 A Yes.

17 Q And how long did you work for them?

18 A I was there from '94 until early '99.

19 BY MR. FIELDER:

20 Q They are one -- or at least back then, they were
21 one of the largest clearing brokers, weren't they?

22 A I don't think they were one of the largest
23 clearing -- they were the largest market maker at the time.

24 Q Okay.

25 A They made market in 5000 stocks. It was basically

1 them and Knight.

2 Q Okay.

3 BY MR. KOTZ:

4 Q And what kind of duties did you have for them?

5 A When I went there, I was in the internal audit
6 department as a senior auditor.

7 Q So what kind of projects or -- would you work on?

8 A Internal audit. We would perform audits of the
9 various departments inside the company.

10 Q All right. What about -- what did you do in 1999?

11 A Well, before I left there, actually, I migrated to
12 the trading room.

13 Q Okay.

14 A And I worked as a market maker on the trading desk
15 in '98 and '99.

16 Q Okay. What about after that?

17 A In early '99, I left to trade as a day trader for
18 four years.

19 Q Okay. That was until about 2003?

20 A 2003. Then I went to Bear Stearns.

21 Q And what was your position at Bear Stearns?

22 A Internal audit, back to audit.

23 Q Okay.

24 A And then from there --

25 Q How did you do at day trading?

1 whatever types of cases they were working on.

2 Q What kind of assistance would you provide?

3 A Obtain trade data through the blue sheet system.

4 Q What would be the reason to obtain trade data?

5 A To see who was trading in certain stocks, like if
6 there were some insider trading cases, we would want to see
7 who bought the stock right before an announcement of earnings
8 or some kind of M&A announcement. A lot of my time was spent
9 on a case called the Squawk Box case, which was a
10 frontrunning case, and it was the -- I don't know if you've
11 heard of it, but --

12 Q Yeah, it's --

13 A -- recently, they got a guilty verdict, and brokers
14 at Merrill Lynch, Lehman, and Smith Barney were passing along
15 the internal squawk box of institutional orders to a group of
16 day traders at a company called AB Watley. That was the bulk
17 of my work from the time I came in here through 2007,
18 actually.

19 Q Okay, okay. And is that the position you have
20 today, staff accountant?

21 A No, I'm a branch chief.

22 Q Okay. So what was the first promotion you got?

23 A Branch chief.

24 Q Okay. And when was that, 2007?

25 A That was in August or September of 2007.

1 A And that was my -- I mean, up until today, that's
2 my take on it.

3 Q Okay. Now prior to assisting Simona and Meaghan on
4 the Madoff matter, had you any experience with Ponzi scheme
5 cases?

6 A I may have. You know what? Maybe not before that
7 time, because the bulk of my time -- basically, from August
8 2004 on, was the Squawk Box case.

9 Q Right, okay.

10 A So I didn't really get involved in a lot of cases
11 where I was the examiner assigned to a case. I did sit in on
12 interviews, you know, if people wanted me to sit there. If
13 there was a trader coming in --

14 Q Right.

15 A -- I would sit in on an interview and stuff like
16 that.

17 Q Right, okay. So you had significant frontrunning
18 experience --

19 A Yes.

20 Q -- but not --

21 A Correct.

22 Q -- experience with Ponzi schemes.

23 A Right. And the other thing, as I understood it,
24 was one of the items they wanted to question him about was
25 frontrunning his customer orders.

1 Q Right.

2 A So I think the combination of market maker and
3 frontrunning got me invited to that interview.

4 Q Right, okay. Did they indicate to you initially
5 what they were looking at Madoff for?

6 A I -- if I remember correctly, it was that he was --
7 they believed he was operating as an investment advisor and
8 he wasn't registered, and he had significant accounts. And I
9 remember, you know, someone discussing the possibility of
10 frontrunning customer orders.

11 Q Okay. Let me show you a document. We're going to
12 mark this document as Exhibit 1.

13 (SEC Exhibit No. 1 was marked for
14 identification.)

15 BY MR. KOTZ:

16 Q Okay. Have you ever seen this document before?

17 A I don't think I've seen this document, but I've
18 seen a spin on this after the fact.

19 Q Okay.

20 A I think I saw it in, like, a magazine article.

21 Q Okay. But at the time that you assisted the
22 enforcement investigators on the Madoff investigation, had
23 you ever seen Exhibit 1, Harry Markopolos' submission?

24 A No.

25 Q And so when they first approached you and told you

1 about the case, you indicated that they talked about the fact
2 that Madoff was -- potentially wasn't registered --

3 A Right.

4 Q -- as an investment advisor, there might be
5 frontrunning.

6 A Right.

7 Q Did at any point in time they say, "He might be
8 running a Ponzi scheme"?

9 A I don't remember anybody saying he was -- he might
10 be running a Ponzi scheme.

11 Q Okay. Okay. When you saw Exhibit 1 or some
12 version of Exhibit 1 on the computer, or, you know, in an
13 article, subsequent to December 2008, did you have any
14 impression of the information in there? Did you read it?

15 A I mean, I -- the article -- are you familiar with
16 the article of the same -- I think it's the same name, I
17 don't know. I read an article right after that, which would
18 have been probably in December of 2008, and I was shocked.

19 BY MR. FIELDER:

20 Q Was it the Journal article? I think there was a
21 Wall Street Journal article with that title.

22 A It may have been. But I remember the title.

23 Q Okay.

24 A That's why when you showed me this, I thought that
25 was the article, and then I saw the date on it.

1 A And also -- I mean, for me personally, it didn't --
2 I mean, we didn't see any -- nothing that was produced in
3 front of me showed anything that he was frontrunning a
4 customer order or the market making business. It -- you
5 know, it seemed to be totally, you know, two different
6 operations.

7 Q Okay. So you did not see --

8 A I mean, with the whole idea of trading options on
9 the London exchange, you know, it didn't seem logical that
10 he'd be frontrunning customer orders by trading S&P -- you
11 now, by buying the whole market.

12 Q Okay. So is it fair to say that from what you
13 understand, they were looking at this issue of frontrunning.
14 It seems as though he wasn't frontrunning. And what was left
15 was that he should register as an investment advisor.

16 A Yes.

17 Q Okay. And were they trying to prove that he should
18 register as an investment advisor, or did they kind of come
19 to that conclusion after the testimony?

20 A I think they came to that conclusion after the
21 testimony.

22 BY MR. FIELDER:

23 Q On that point, though, I think -- and correct me if
24 I'm wrong, you testified that when you first met with him,
25 when they first pulled you in, that that was -- you said that

1 your understanding was they were looking at him for two
2 things.

3 A Yeah, yeah.

4 Q One was whether or not he should be registered as
5 an IA, and that was before the testimony.

6 A Correct.

7 Q And then two was frontrunning.

8 A Yeah.

9 Q So they had that as kind of an operating hypothesis
10 before his testimony, correct?

11 A Yeah, yes. And then afterwards they said he's
12 clearly operating as an investment advisor and should be
13 registered.

14 BY MR. KOTZ:

15 Q And seemed to kind of rule out the frontrunning.

16 A Yeah.

17 Q Okay. All right. Let me show you another
18 document. We're going to mark this as Exhibit 10. This is
19 an e-mail from you to Simona Suh, 1/17/2007, 10:33 a.m.

20 (SEC Exhibit No. 10 was marked for
21 identification.)

22 BY MR. KOTZ:

23 Q And this is January of 2007. Simona says, "I'm
24 preparing the case for closing," and I guess she's just
25 asking if you have any documents.

1 A Yes.

2 Q So -- but you didn't -- you weren't aware of any
3 further developments in the case after the day or the day
4 after Madoff's testimony, and this e-mail.

5 A Yeah. I probably hadn't -- this is probably the
6 next e-mail I got from her after the June e-mail I was CC'd
7 on.

8 Q And were you ever made aware of why they closed the
9 case?

10 A No.

11 Q Did you know whether Madoff had registered as an
12 investment advisor at that time?

13 A I thought I heard that he did, and I don't know who
14 would have told me that.

15 Q Okay. Okay. Let me show you the next document.
16 We'll mark it as Exhibit 11. This is an e-mail from you to
17 Rob Deleonardis, 12/18/2008, at 10:03 a.m, and this is Rob
18 forwarding to you a Wall Street Journal article about Madoff.

19 A Yes.

20 (SEC Exhibit No. 11 was marked for
21 identification.)

22 BY MR. KOTZ:

23 Q So what was your reaction when you heard in
24 December of 2008 that Madoff had confessed to a Ponzi scheme?

25 A I was surprised. I mean, I --

1 Q Okay.

2 A -- I was shocked, I mean, of -- just for the sheer
3 magnitude of it.

4 Q And then I guess Rob sent you this article, and you
5 said, "I saw this one." Now were you surprised also to read
6 in these -- in this article or in other articles, that it
7 seems as though one of the issues that had been brought to
8 the SEC's attention in connection with the investigation that
9 you worked on was actually that he was running a Ponzi
10 scheme?

11 A Yes.

12 Q And so is it fair to say that you were surprised
13 that they were aware of an issue of a Ponzi scheme, because
14 you worked on the investigation and that issue didn't come
15 up?

16 A Yes.

17 Q Were there any conversation internally with Rob or
18 others about what happened? You know, any theories about
19 what happened, that the SEC didn't catch this Ponzi scheme?

20 A No. I mean, I didn't -- I was surprised to read
21 about this Markopolos. I -- this is the first time I heard
22 his name, was when I heard of this in December.

23 Q In December of 2008.

24 A Yeah.

25 Q And were you surprised that there was all these