

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

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

 **COPY**

WITNESS: Number 33
PAGES: 1 through 47
PLACE: Securities and Exchange Commission
100 F Street, N.E.
3rd Floor Conference Room
Washington, D.C. 20549
DATE: Tuesday, April 28, 2009

The above-entitled matter came on for hearing, pursuant to notice, at 2:43 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 DAVID WITHERSPOON, ESQ., Investigator

6 HEIDI STEIBER, ESQ. Investigator

7 Office of the Inspector General

8 Securities and Exchange Commission

9 100 F Street, N.E.

10 Washington, D.C. 20549

11 (202) 551-6037

12

13 DAVID FIELDER, ESQ.

14 Office of the Inspector General

15 Securities and Exchange Commission

16 100 "F" Street, N.E.

17 Washington, D.C. 20549

18 (202) 551-5401

19

20 On behalf of the Witness:

21 THEODORE SONDE, ESQ.

22 Patton Boggs LLP

23 2550 "M" Street, N.W.

24 Washington, D.C. 20037

25 (202) 457-6334

P R O C E E D I N G S

1
2 MR. KOTZ: Okay. We are on the record at 2:43 on
3 April 28, 2009, at the United States Securities and Exchange
4 Commission, Office of Inspector General.

5 I'm going to swear you in now, if that's all right?

6 MR. DALE: Sure.

7 MR. KOTZ: Could you please raise your right hand?
8 Whereupon,

9 WILLIAM C. DALE

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

12 MR. KOTZ: Okay. Could you state and spell your
13 full name for the record?

14 THE WITNESS: William Charles Dale, Dale is
15 D-a-l-e.

16 MR. KOTZ: Okay. Mr. Dale, my name is David Kotz
17 and I'm the Inspector General of the United States Securities
18 and Exchange Commission. And I have here with me my
19 colleagues David Witherspoon, Heidi Steiber and David
20 Fielder. And I understand you have counsel, Theodore Sonde,
21 here. This is an investigation by the Office of Inspector
22 General, case number OIG-509.

23 I'm going to ask you certain questions; you'll
24 provide answers under oath. The court reporter will record
25 and later transcribe everything that is said. Please provide

1 management-type questions. I know that his -- a lot of his
2 academic background, he's a PhD and he's published in the
3 journal of finance on options.

4 Q So he has expertise in options trading, Mr. Mayhew?

5 A In options.

6 Q In options, okay. And you worked with him from
7 time to time?

8 A He was a couple of offices away from me, so yes,
9 I'd ask him question or --

10 Q And was your impression --

11 A -- he'd ask me questions.

12 Q -- of his background or his abilities?

13 A Very high.

14 Q Okay. I'm going to ask -- you sent an e-mail to
15 our offices in February of 2009. I'm going to show it to
16 you. We can put it into evidence, it's -- mark it as Exhibit
17 1. It's an e-mail from Terry and Bill Dale, Friday, February
18 20, 2009, 7:57, to our offices, just to refresh your
19 recollection.

20 And you state in there that you knew we were
21 looking into the Madoff investigation and NYRO staffers
22 contacted OAA concerning Madoff. You say, "Given the
23 discussion we had with NYRO, I'm -- I was surprised that the
24 case was closed." And we're going to get into, you know,
25 some specific questions, but, you know, can you just kind of

1 elaborate generally as to what you were trying to say in this
2 e-mail?

3 (SEC Exhibit No. 1 was marked for
4 identification.)

5 A Right. Given that the staff seemed to have
6 suspicions about the trading that was going on at the firm
7 and they said there might be a problem getting records, I
8 thought it was the kind of thing they would stick with. And
9 since it -- and if there was something going on they'd find
10 it. And when I learned that the thing blew up in December,
11 surprised that it hadn't been found out earlier.

12 Q And so you say you thought they would stick with
13 it, but they didn't stick with it?

14 A According to press and things I saw later, the case
15 was closed.

16 Q Okay. And so you were aware of the suspicions that
17 the enforcement staff attorneys had?

18 A Yes.

19 Q And what were those?

20 A They communicated it to us.

21 Q All right. Well, why don't we get into some
22 documents, in terms of those specific communications, and
23 that will hopefully help. All right, let me show you -- this
24 document we're going to mark as Exhibit 2. This is an e-mail
25 from you to Vance Anthony, 2/7/2006, 9:45 a.m.

1 And you see there was an e-mail here from Simona
2 Suh to Vance Anthony. You want to take a minute to look at
3 this?

4 (SEC Exhibit No. 2 was marked for
5 identification.)

6 (The witness examined the document.)

7 A Okay.

8 Q Okay. So, do you remember generally --

9 MR. SONDE: Have you finished reviewing that?

10 THE WITNESS: I've read it.

11 MR. SONDE: Okay.

12 BY MR. KOTZ:

13 Q Do you remember generally receiving some
14 information from Simona Suh about Madoff in this time period,
15 February 2006? Our records show there were two
16 conversations, one in February and then one later in May. Do
17 you remember this initial call or initial e-mail?

18 MR. SONDE: You've asked two questions, do you
19 remember the initial e-mail and then second question is do
20 you remember the initial telephone call.

21 THE WITNESS: Right. I don't think I remember this
22 as this.

23 MR. SONDE: "This" being the e-mail?

24 THE WITNESS: I don't remember this -- I do not
25 recall -- I don't remember -- this e-mail doesn't look

1 familiar to me.

2 MR. KOTZ: Okay. All right. Well, why don't I
3 show you a couple of additional documents. And this is --
4 we're going to mark as Exhibit 3. This is an e-mail from you
5 to Simona Suh, 2/7/2006, 10:16 a.m. There you go.

6 And then I'm going to show you another document,
7 which are some notes dated 2/8/2006, which we're going to
8 mark as Exhibit 4.

9 (SEC Exhibit Nos. 3 and 4 were
10 marked for identification.)

11 MR. SONDE: This is 4.

12 MR. WITHERSPOON: Mm-hmm, that's 4. 3 and 4.

13 MR. KOTZ: It seems as though from this e-mail that
14 there was a phone call that was set up as a result of the
15 information Simona provided. And then Exhibit 4 is -- it
16 seems to be notes from that phone call.

17 THE WITNESS: I see. I see.

18 MR. SONDE: First question is do you -- have you
19 ever seen this document?

20 THE WITNESS: I don't think so.

21 BY MR. KOTZ:

22 Q Okay, well -- I just -- what do you remember about
23 the communications with enforcement in this time period?

24 A Right. I remember a phone call. I thought that Dan
25 got the initial call, maybe not, and they wanted to talk

1 about -- we set up a phone call with I think Dan and I at our
2 end and people from the New York office at the other end. I
3 think there was quite a -- there were several people I think
4 in the New York end.

5 Q Okay, what did you guys talk about on the phone
6 call?

7 A They told us that there was a possible problem with
8 the trading of individual or personal accounts being done by
9 a principal or a boss at a prominent New York firm. And they
10 said -- but I think they said -- I'm not sure if they said
11 that a whistleblower or a tipper or a complainant or what,
12 who thought there was something -- something wrong was going
13 on. And I don't know if we asked them or if they told us
14 that he was providing to investors or investors were getting
15 a rate of return with almost no downside or with no downside
16 over the interim.

17 Q Okay. And did they ask you to do anything? What
18 were they -- why were they telling you all of this?

19 A The question I remember in so many words was
20 something like, "Is it possible to test or to prove that such
21 results are impossible using the strategy that the portfolio
22 manager or broker says he's using."

23 Q So what did you say?

24 A Well, we asked questions about what does he say
25 he's doing.

1 Q Right.

2 A And at some point, not sure about the sequence of
3 these things, I said something like, "Well do you know what a
4 split-strike conversion is?" And I knew what a conversion
5 was, I know what a strike on an option was, I wasn't quite
6 sure what split-strike conversion was. I think at that point
7 I said, "Let me see if I can get Stuart Mayhew to come in,
8 who has a lot of academic background in option pricing and
9 option theory, and see if he can help."

10 And I don't remember the sequence but I started
11 asking questions about -- they said basically, he buys the
12 stocks, he sells the calls, the out money calls and buys the
13 out money puts. I said, "Well, what else does he do? Are
14 the strikes always a certain difference from the market?
15 Does he always buy and is trading enough to dollar-for-dollar
16 cover the dollar value of the stocks? Does he always buy the
17 same stocks? How often does he rebalance or restart the
18 process?"

19 And they also told me that at times he goes
20 entirely cash. And they didn't have the answers to some of
21 the questions we asked before.

22 Q But do you remember any questions --

23 MR. SONDE: I'm not sure he's finished answering.
24 Have you completed your answer?

25 THE WITNESS: Yeah.

1 MR. SONDE: I remember -- okay, go ahead.

2 BY MR. KOTZ:

3 Q You said they didn't have some answers to the
4 questions, do you remember anything specific?

5 A Right, I don't think they knew the relationship or
6 if there was a consistent relationship between the strike
7 prices on the options and the market price.

8 They also told us that the stocks were not always
9 the same. They thought they were generally drawn or were
10 drawn from the S&P 100 universe. That wouldn't be all of
11 them. And over time they wouldn't always be the same ones.

12 I don't know if they volunteered or I asked, but I
13 think I said, "What's the rate of return?" And the number I
14 remember was -- is 8 1/2 percent. 8 1/2 percent annual rate
15 with little -- I think they said assume no down side, no
16 losses, something like that.

17 Q And so were they asking you to do something
18 specific?

19 A Well I think they asked the question, "Could you or
20 could somebody prove that these results were unattainable
21 using the strategy?" And that's how I -- we got -- I suppose
22 at that time I started asking more specific questions about
23 the strategy.

24 Q So did you give them an answer on the call as to
25 whether somebody could do it?

1 A There were a couple of things. Hearing that one
2 element of the strategy was going to cash and it might be, at
3 least in my mind, discretionary when he went to cash, that
4 takes the whole structure out of the strategy and introduces
5 an element -- a very, very -- a potentially, very important
6 element of market-timing.

7 For whatever the return is, one that could be
8 expected over time or simulated or observed for the
9 split-strike conversion part of the investment strategy,
10 there was an opportunity for a time-out. It just took it
11 completely out of stocks and out of options and put them into
12 treasury bills or something.

13 MR. SONDE: Come back to Mr. Coates' question --

14 MR. KOTZ: Kotz.

15 MR. SONDE: Kotz, I'm sorry. And answer whether
16 there was an answer given in this phone call as to their
17 question. Did you give them an answer?

18 THE WITNESS: No, I didn't tell them it was
19 impossible or it wasn't impossible. I said, "One, to do
20 something just to simulate or test the strategy we'd have to
21 know the -- we'd have to know -- we should know the details
22 of the strategy well." I think I said for other -- they --
23 in fact, there is this big discretionary element of going --
24 being able to go cash with nothing to observe that makes one
25 going -- an -- about going to cash, that in fact, it reduces

1 to a discretionary system in it's market-timing. And that's
2 a completely different situation than a structured portfolio
3 strategy that one can test or mathematically calculate the
4 probabilities.

5 BY MR. KOTZ:

6 Q So was there something that your office was
7 supposed to do after the call?

8 A I don't recall. I don't think so.

9 Q Okay. All right, let me show you another document
10 if I could. This is an e-mail we're going to mark as Exhibit
11 5. This is an e-mail 2/27/2008 (sic), so a few weeks after
12 the call from you to Vance Anthony.

13 (SEC Exhibit No. 5 was marked for
14 identification.)

15 A Right.

16 Q Do you know what that means, "Nonchu forget
17 Madoff?"

18 A That would be slang for don't forget Madoff.

19 Q And so, do you have any idea what you were saying
20 to Vance about not forgetting Madoff?

21 A I don't know.

22 Q But do you think that Vance was supposed to do
23 something? If you notice that the first document that I
24 showed you --

25 A Yeah.