



## SECURITIES LITIGATION ALERT

## Court Allows Use of Wiretap Evidence in Galleon Insider Trading Case

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On November 24, 2010, Judge Richard J. Holwell of the Southern District of New York denied defendant Raj Rajaratnam's motion to suppress the government's wiretaps in the highly publicized Galleon insider trading case, allowing the admissibility of volumes of wiretap recordings to be used as evidence for the first time in a criminal insider trading case.

[Judge Holwell's order](#) ended many months of argument over the legality and admissibility of wiretaps in criminal insider trading cases. The order follows multiple rounds of briefing and a *Franks* hearing.

### Impact of Ruling

Judge Holwell's ruling allowing wiretaps to be used to investigate insider trading is significant and comes at a critical time. The Galleon investigation was the first time wiretaps have been used to investigate and charge insider trading crimes, and the government has relied heavily on the wiretap recordings in this case. Judge Holwell's holding that Title III could authorize wiretaps in cases that result in insider trading charges will undoubtedly change the way the government investigates and prosecutes such crimes. Indeed, recent news reports suggest the government is already aggressively using wiretaps to investigate other insider trading schemes. The use of wiretaps in insider trading prosecutions will also make defending such cases more difficult than in the past.

### The Proceedings and Judge Holwell's Findings

In his motion to suppress, Rajaratnam advanced three primary arguments regarding the inadmissibility of the wiretaps,

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including the following: (1) the use of Title III wiretaps in an insider trading case was unconstitutional; (2) the government's wiretap application did not demonstrate the requisite probable cause needed for the issuance of a wiretap; and (3) the government failed to demonstrate the necessity of the wiretaps. The Court denied the motion on the papers on the unconstitutionality and probable cause grounds, but granted Rajaratnam's request for a *Franks* hearing in connection with the issue of whether the issuance of a wiretap was "necessary."

Where a defendant makes a preliminary showing that the affidavit offered by the government in support of its wiretap application misstated or omitted material information, a *Franks* hearing may be held to determine if those misstatements or omissions were made intentionally or with reckless disregard for the truth. If the court makes such findings, it must then determine whether the federal district courts that issued the wiretaps would still have issued them had the misstated or omitted information been included in the wiretap application.

In this case, Rajaratnam argued that the wiretap application and supporting affidavit failed to mention or sufficiently describe the then ongoing related SEC insider trading investigation. He alleged that at the time of the wiretap application, the U.S. Attorney's Office and FBI knew of the SEC's investigation and had access to millions of documents obtained by the SEC. He also argued that though the FBI agent knew that the SEC had conducted numerous witness interviews and taken the deposition of the defendant himself, this information was omitted from the agent's affidavit in support of the wiretap. Finally, Rajaratnam argued that had this information been revealed, the issuing court would not have found the wiretap was "necessary" and would have denied the application.

At the four-day *Franks* hearing held in October of this year, the Court heard testimony from four witnesses, including the FBI Special Agent whose affidavit was submitted in support of the government's wiretap application. Following the hearing, the Court requested post-hearing briefing on the issue of whether the wiretaps were necessary in light of the SEC investigation.

On November 24th, the Court issued an order which held that (1) because Title III authorizes the government to use wiretaps to investigate wire fraud, the government may also investigate insider trading making use of interstate wires; (2) even though the government's wiretap application omitted and misstated important information regarding a crucial informant's

credibility, the remainder of the affidavit constituted sufficient probable cause for a wiretap; and (3) the evidence presented at the *Franks* hearing demonstrated that while the government did not disclose the full nature and scope of the SEC investigation, had it done so, the wiretap would still have been necessary and appropriate.

### **Title III Wiretaps May Be Used to Investigate Insider Trading**

The Court's first holding was that Title III wiretaps may be used to investigate insider trading, even though insider trading is not one of the offenses enumerated in Section 2516 of the statute. See 18 U.S.C. § 2516. The Court reasoned that, so long as the government obtained the wiretap in connection with an offense for which Title III specifically permits wiretapping, any additional evidence it intercepts incidentally may be used to charge and prosecute other offenses. Here, the government's wiretap application described evidence establishing probable cause for wire fraud and money laundering—both crimes for which wiretapping is expressly authorized, and therefore, the application was appropriate. The fact that the government ultimately only charged the defendants with insider trading, and not wire fraud or money laundering, did not invalidate the wiretaps. The Court concluded that the government, in good faith, sought to investigate wire fraud through its wiretaps and that the incidental crime of securities fraud could therefore properly be investigated and charged using the wiretaps.

### **The Government's Wiretap Application and Supporting Affidavit Sufficiently Established Probable Cause**

The Court's evaluation of probable cause focused on information concerning one particular confidential informant. Specifically, the agent's affidavit omitted to disclose that this informant had previously pled guilty to felony wire fraud. Rajaratnam argued that such evidence of her credibility should have been disclosed in the warrant application and had it been, the wiretap would not have issued. Judge Holwell acknowledged that it was "particularly disturbing" that the "highly-relevant information regarding [the informant's] prior criminal record for fraud" had not been disclosed. However, after a careful review of the remaining evidence in the affidavit, including evidence corroborating the informant's information, Judge Holwell concluded that the affidavit contained sufficient evidence of probable cause to support the original wiretap application, rendering a *Franks* hearing on the subject

unnecessary.

### **The Wiretaps Were Necessary, Despite the Government's "Glaring Omission"**

Judge Holwell reserved his harshest criticism of the government for his evaluation of the evidence presented at the *Franks* hearing. Title III requires a wiretap application to contain a "full and complete statement as to whether or not other investigative procedures have been tried and failed or why they reasonably appear to be unlikely to succeed if tried or to be too dangerous." The Court noted that a review of the evidence presented at the *Franks* hearing demonstrated that the government had made a "glaring omission" in failing to disclose the SEC's extensive, multiyear investigation.

The government had failed to disclose not only the existence of the SEC investigation itself, but the millions of documents, witness interviews and deposition of Rajaratnam taken by the SEC, all of which the criminal authorities relied upon in pursuing their own investigation. Judge Holwell held that this "nearly full and complete *omission* of what investigative procedures in fact had been tried ... deprived [the issuing judge] of the opportunity to assess what a conventional investigation of Rajaratnam could achieve ..." (emphasis original). The Court further concluded that such a "glaring omission" evidenced the government's "reckless disregard for the truth."

Because the Court found that there had been a material omission, it examined whether the wiretap would have been necessary and appropriate had the fact and extent of the SEC investigation been disclosed in the initial wiretap application. The Court noted that the "failure" of other techniques, as defined in Title III, did not require that those other techniques uncover no evidence. Judge Holwell pointed to the SEC chronologies, which "strongly suggested that Rajaratnam had been careful to exchange nearly all of his inside information by telephone," stalling a traditional investigation. Therefore, the Court concluded that, even though the government had recklessly omitted key information from its wiretap application, the wiretaps were necessary to uncover the full extent of the insider trading.

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