

COMMONWEALTH OF MASSACHUSETTS  
OFFICE OF THE SECRETARY OF THE COMMONWEALTH  
SECURITIES DIVISION  
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BOSTON, MASSACHUSETTS 02108

SECRETARY OF THE  
COMMONWEALTH  
2013 OCT -2 PM 4:57  
SECURITIES DIVISION

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IN THE MATTER OF:

CITIGROUP GLOBAL MARKETS INC.

Docket No. 2013-0014

Respondent.

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**CONSENT ORDER**

This Consent Order (“Order”) is entered into by the Massachusetts Securities Division with respect to the ongoing investigation by the Massachusetts Securities Division (“Division”) of misconduct by a research analyst employed by CGMI’s Taiwanese affiliate in which large hedge fund and institutional clients received confidential nonpublic research information in the form of unpublished research views (*Docket No.* 2013-0014).

On October 2, 2013 CGMI submitted an Offer of Settlement (“Offer”) for the purpose of disposing the allegations set forth in the in the Offer of Settlement. Respondent CGMI admits to the Division’s Statement of Facts set forth in Section VI herein, neither admits nor denies the conclusions of law set forth in Section VII and violations of law set forth in Section VIII herein, and consents, for the purpose of these proceedings, to the entry to this Order by the Division, consistent with the language and terms of the Offer, settling the claims thereby with prejudice.

**I. JURISDICTION AND AUTHORITY**

1. The Massachusetts Securities Division is a division of the Office of the Secretary of the Commonwealth with jurisdiction over matters relating to securities as provided for by MASS. GEN. LAWS ch. 110A (the “Act”). The Act authorizes the Division to regulate: 1) the offers

and/or sales of securities; 2) those individuals offering and/or selling securities within the Commonwealth; and 3) those individuals transacting business as broker-dealer agents and investment advisors within the Commonwealth.

2. The Division brings this action pursuant to the enforcement authority conferred upon it by Section 407A of the Act and MASS. GEN. LAWS ch. 30A, wherein the Division has the authority to conduct adjudicatory proceedings to enforce the provisions of the Act and all regulations and rules promulgated thereunder.

3. This proceeding is brought in accordance with Sections 204 and 407A of the Act and its Regulations.

## **II. RELEVANT TIME PERIOD**

4. Except as otherwise expressly stated, the conduct described herein occurred between November 1, 2012, and December 31, 2012.

## **III. RESPONDENT**

5. CGMI is a Financial Industry Regulatory Authority (“FINRA”) registered broker-dealer with its principal address located at 390-388 Greenwich Street, New York, New York 10013-2396 and offices throughout the United States, including in Boston, Massachusetts. CGMI’s Central Registration Depository (“CRD”) identification number is 7059. CGMI has been registered to conduct business as a broker-dealer in Massachusetts since July 31, 1981. CGMI is a wholly-owned subsidiary of Citigroup Financial Products, Inc. and indirectly is a wholly-owned subsidiary of Citigroup Inc. Citigroup Research, formerly CIRA, is a part of Citigroup Inc.’s Institutional Clients Group and provides research for individual and institutional clients.

#### IV. RELATED PARTIES

6. Citigroup Research (“CIR”) is a globally integrated business unit of the Institutional Clients Group of Citigroup Inc., operating out of U.S. and non-U.S. affiliates located in different countries throughout the world. CIR research analysts in the U.S. are employed by CGMI.

7. Citi Equities (“Citi Equities”) is a globally integrated business unit of the Institutional Clients Group of Citigroup Inc., providing a broad range of products and services for equity and equity linked instruments. Citi Equities employees in the U.S. are employed by CGMI.

8. CGMI Research Analyst is a research analyst employed by CGMI located in the U.S. CGMI Research Analyst is responsible for the coverage of technology stocks, including Apple Inc.

9. Citigroup Global Markets Taiwan Securities Co. Limited (“Citi Taiwan”) is a non-U.S. affiliate of CGMI located in Taipei, Taiwan. CIR research analysts employed by Citi Taiwan cover Asian-based issuers, including Asian firms that produce and assemble upstream technology products in supporting technology companies.

10. Taiwan Equity Sales (“Taiwan Equity Sales”) is a business unit located in Taipei, Taiwan operating out of Citi Taiwan.

11. Kevin Chang (“Kevin Chang”) was a research analyst employed by Citi Taiwan during the relevant time period and was responsible for the coverage of technology companies and suppliers in the technology supply chain, including Hon Hai Precision Industry Co., Ltd. As of September 4, 2013, Kevin Chang was terminated from employment by Citi Taiwan.

12. Hon Hai Precision Industry Co., Ltd. (“Hon Hai”) (Ticker: 2317. TW) is a Taiwan-based company involved in the manufacture and sale of technology products. As of May 2012, Hon Hai was the largest supplier of Apple iPhones and iPads.

13. Apple, Inc. (“Apple”) (Ticker: AAPL on the NASDAQ), formerly Apple Computers, Inc., is a U.S.-based multi-national corporation headquartered in Cupertino, California that designs, develops, and sells consumer electronics such as the Apple iPhone and iPad.
14. SAC Capital (“SAC Capital”) is a U.S. hedge fund founded by Steven A. Cohen, comprised of the following management companies: (i) CR Intrinsic Investors, LLC (“CR Intrinsic”), a Delaware limited liability company; (ii) Sigma Capital Management, LLC (“Sigma”), a Delaware limited liability company; and (iii) S.A.C. Capital Advisors, L.P. (“SAC LP”) a Delaware limited partnership that actively managed investments beginning in approximately 2009.
15. Citadel, LLC (“Citadel”), formerly known as Citadel Investment Group, LLC, is a global financial institution based in Chicago, Illinois. Surveyor-Capital is a hedge fund division within Citadel.
16. GLG Partners (“GLG Partners”) is a wholly-owned subsidiary of British alternative investment manager, Man plc., based in London:
17. T. Rowe Price (“T. Rowe Price”) is a publicly owned investment firm headquartered in Baltimore that offers mutual funds, sub-advisory services, and separate account management for individuals and institutions.

## **V. RELEVANT DISCIPLINARY HISTORY**

### **A. 2003 Global Research Analyst Settlement**

18. On October 17, 2003, CGMI entered into an Administrative Consent Order (Docket No. 2003-046) with the Division (“2003 MSD Settlement”).
19. On October 31, 2003, CGMI settled civil and regulatory actions brought by the Division and other regulators, which alleged that CGMI violated federal and state securities laws as well

as NASD and NYSE rules arising out of CGMI's misconduct, including its research department, between 1999 and 2001 ("2003 Global Research Analyst Settlement").

20. These actions alleged, *inter alia*, that CGMI published fraudulent research reports, permitted inappropriate influence over research analysts, and failed to adequately supervise employees who engaged in those practices.

21. These actions also alleged that CGMI engaged in improper "spinning" of shares to executives of investment banking clients and failed to maintain policies and procedures reasonably designed to prevent the potential misuse of material, nonpublic information in certain circumstances.

**B. 2012 CGMI Consent Order**

22. On October 26, 2012, CGMI made a settlement offer that was acceptable to the Division that resulted in an Administrative Consent Order (Docket No. 2012-0090) ("2012 CGMI Consent Order").

23. The 2012 CGMI Consent Order related to the alleged failure by CGMI to prevent or detect the written disclosure of material, nonpublic research information in a restricted period prior to an IPO.

24. CGMI agreed to 1) permanently cease and desist from further violations of the Act, 2) to be censured, 3) to a fine of \$2,000,000, and 4) to review and/or implement certain internal policies and procedures relating to outgoing communications of its research analysts with parties external to CGMI.

25. Among other things, Respondent CGMI agreed to the following:

Respondent CGMI agrees within 90 days of the signed Order to review its written supervisory policies and procedures ... To the extent written supervisory policies and

procedures do not exist ... Respondent must establish such procedures. All written policies and procedures ... below must include methods for enforcement and compliance oversight:

1. **CIR<sup>1</sup> will review its electronic surveillance program for the incoming and outgoing communications of its research analysts with parties external to CGMI** for compliance with federal and state securities laws and regulations and compliance with the Global Research Analyst Settlement.
2. CGMI will enhance the training provided to CIR equity research analysts, CIR supervisors, and CIR compliance personnel. Such training will include but not be limited to the following topics:

(i) **CIR equity research analysts cannot preview in writing unpublished, or disavow in writing published research views to personnel outside of CIR** (other than is permitted under federal or states securities laws or regulations);

(ii) in connection with any IPO for which CGMI is acting as manager or co-manager, except as expressly permitted by the federal securities laws and FINRA Rule 2711(c)(2), CIR equity research analysts may not disseminate to parties external to CGMI written material discussing the subject company prior to CGMI's initiating research coverage on the subject company; and

(iii) other than in the form of, or to the extent embedded in published research or financial or other analysis or modeling prepared by a CIR equity research analyst, CIR equity research analysts may not disseminate to any person within CGMI confidential nonpublic information obtained from a covered company or a company with which CGMI has contracted to act as manager or co-manager without affixing to such material a legend clearly stating "CONFIDENTIAL: FOR INTERNAL USE ONLY":

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<sup>1</sup> For purposes of this paragraph 25, "CIR" was defined in the 2012 CGMI Consent order as a business unit of CGMI.

(Emphasis added).

No later than 180 days after the date of entry of the Order, Respondent's Director or Co-Director of Citigroup Research shall certify to the Division, in writing, that Respondent has fully complied in all material respects with the undertakings set forth [above].

## **VI. STATEMENT OF FACTS**

### **A. CGMI'S PRE-DECEMBER 13, 2012 HON HAI AND APPLE PUBLISHED RESEARCH REPORTS**

26. On November 13, 2012, Kevin Chang published a research report on Hon Hai ("November 13 Hon Hai Research Report").

27. In the November 13 Hon Hai Research Report, Kevin Chang issued a "*Buy*" rating for Hon Hai, stating that "HH [Hon Hai] is consolidating market share and is gaining bargaining power from Apple," and forecasting that Hon Hai's total Apple iPhone shipment *will go up* from 21 million units in the third quarter of 2012 to 50 million units in the fourth quarter of 2012.

28. On November 28, 2012, CGMI Research Analyst published a research report on Apple ("November 28 Apple Research Report").

29. In the November 28 Apple Research Report, CGMI Research Analyst issued a "*Buy*" rating for Apple, stating that "[o]ur primary take away is that improved availability of iPhone5 adds to our confidence in the quarter," and forecasting 47 million units of Apple iPhones in the last quarter of 2012 (which is Apple's first fiscal quarter of 2013 because Apple's fiscal year begins in September).

30. The November 28 Apple Research Report forecast was based on a model which included approximately 47 million Apple iPhone units in the last quarter of 2012 and 40 million Apple iPhone units for the first quarter of 2013.

31. The research views published by Kevin Chang and CGMI Research Analyst in the November 13 Hon Hai Research Report and the November 28 Apple Research Report were consistent with a Wall Street consensus of the coverage of Hon Hai and Apple up to this point in time.

32. On December 10, 2012, Kevin Chang published a subsequent research report on Hon Hai (“December 10 Hon Hai Research Report”).

33. In the December 10 Hon Hai Research Report, Kevin Chang maintained a “*Buy*” rating for Hon Hai, with the report’s sub-title as “Robust Nov Sales Driven by iPhone 5,” forecasting 47 million Apple iPhone units by the end of the last quarter of 2012 and *increasing* the first quarter Apple iPhone production forecast to 45 million units from 40 million units.

#### **B. MACQUARIE DECEMBER 13, 2012 HON HAI RESEARCH REPORT**

34. The Macquarie Group (“Macquarie”) is a global provider of banking, financial, advisory, investment and funds management services based in Australia. The Macquarie Group is a competitor to CGMI in its coverage of Hon Hai.

35. According to records submitted to the Division, on December 13, 2012, Macquarie published a research report out of its Taiwan branch on Hon Hai, first available at 3:44 A.M. EST. (“Macquarie December 13 Hon Hai Research Report”).

36. In the Macquarie December 13 Hon Hai Research Report, with the sub-title “Structural risks from Apple demand,” Macquarie *downgraded* Hon Hai from “*Outperform*” to “*Neutral*”, and *lowered* its Apple iPhone forecast in the first quarter of 2013 to 26-28 million units, which represented a 35-40% cut from its prior numbers, citing lowered customer demand for Apple iPhones.



### C. CGMI LOOKED TO KEVIN CHANG FOR HIS HON HAI PROJECTIONS

37. According to CGMI's approved travel records, CGMI Research Analyst conducted research on-site in Taipei, Taiwan between December 8, 2012 and December 15, 2012.

38. On December 13, 2012, CGMI employees responded to the Macquarie December 13 Hon Hai Research Report by requesting feedback from Kevin Chang regarding his analysis of the Apple supply chain.

39. Email communications from a CGMI employee of Citi Equities to various Citi Equities and CIR personnel asked "**45mm in Q4 and 25mm in Q1!!!! Kevin/[CGMI Research Analyst]...we are NOT seeing that, correct???**" (Emphasis added).

40. Over the course of the morning on December 13, 2012, a CGMI employee of Citi Equities continued to seek research views from Kevin Chang, asking via email "Pls call me as soon as you can...getting tons of questions on this Apple 1Q iPhone story..."

41. On December 13, 2012 the CGMI employee received an email from Taiwan Equity Sales with the title "Hon hai (iPhone) order cuts-likely true" and forwarded the email to Kevin Chang the following morning, December 14, 2012, stating that "**Taiwan sales ... are already going out with that the cuts are likely true**" prior to any CGMI approved publication or broad dissemination of this information (Emphasis added).

### D. CGMI'S LARGE HEDGE FUND AND INSTITUTIONAL CLIENTS SOUGHT KEVIN CHANG'S RESEARCH VIEWS ON HON HAI

42. CIR research analysts, including CGMI Research Analyst, had been performing on-site due diligence in Taiwan.

43. Because the information in the Macquarie December 13 Hon Hai Research Report was a

significant departure from the previous Wall Street consensus, it prompted clients of CGMI to seek CGMI's research views on Apple and its suppliers, namely Hon Hai.

44. On the morning of December 13, 2012, an employee of SAC Capital, a CGMI client holding Apple stock, began emailing Kevin Chang, asking "**Hey Kevin, Are you picking up any order cuts to iPhone?**"(Emphasis added).

45. Also on the morning of December 13, 2012, an employee of SAC Capital's CR Intrinsic division emailed Kevin Chang, asking "Hi Kevin, Macquarie just downgraded Hon Hai and cited very weak demand for the iPhone (down 35-40%) into the March qtr. **Have you picked up any checks that would suggest this is the case? I think when we exchanged emails a bit earlier you were still pretty bullish about March estimates?** Thanks! . . ." (Emphasis added).

46. Also on the morning of December 13, 2012, an employee of SAC Capital's LP division, emailed Kevin Chang, asking "Hello Kevin, do you have some time to speak? Not sure if you are in Taiwan?"

47. Also on the morning of December 13, 2012, an employee of SAC Capital's Sigma Capital division emailed Kevin Chang, asking "A competitor had a negi [negative] note on HH today. I was wondering if you had a few minutes tonight (ET), am for you, to catch up on your general thoughts."

48. On December 13, 2012, prior to the publication of Kevin Chang's December 14 Hon Hai Report, another employee of the hedge fund emailed Kevin Chang, copying a Citi Equities employee, with the subject of the email as "[Employee Name] at SAC request for conference call today URGENT."

49. In this email chain, the SAC employee asked, "Kevin are you available?" The Citi Equities employee replied to this chain, asking, "Kevin, Have been told this morning that you are

in Japan. Is there a possibility of you calling [the hedge fund employee] on his mobile number at [U.S. phone number] or in his office at [U.S. phone number]. Any help is greatly appreciated.”

Lastly, the employee of the hedge fund replied to both Kevin Chang and the Citi Equities employee, stating, “Thanks very much mobile is best at [U.S. phone number].”

50. Also on December 13, 2012, Kevin Chang received an email from another CIR research analyst, copying other CIR and Citi Equities personnel, stating “...**Citadel called-wanted your views on AAPL #s at Maq** [Macquarie]” (Emphasis added).

51. Also on December 13, 2012, a Citadel employee sent an email to Kevin Chang, copying two other Citadel employees, asking “Can we do a quick call tonight? Thx.”

52. Also on December 13, 2012, an employee of Citadel’s Surveyor-Capital division emailed an employee of Citi Equities and was forwarded to Kevin Chang, asking “**Was someone from CITI out talking about iPhone trends today?...You sure, someone told me Kevin Chang had something on Apple iPhone trends?**” (Emphasis added).

53. Also on December 13, 2012, GLG Partners called CGMI and Kevin Chang was sent an email from Taiwan Equity Sales, copying employees of GLG Partners, asking “Hey Kevin...a competitor is saying builds for iPhone5 ...coming down drastically in Q1 for shipment in the following quarters. Not sure if this is what you’ve heard...”

54. Also on December 13, 2012, a T. Rowe Price employee emailed Kevin Chang, asking “**Hi Kevin, What did your companies say about iphone shipment in 4Q and 1Q? Are you around for a chat?**” (Emphasis added).

55. Kevin Chang replied, in part, “I am traveling and will be back in the afternoon. Free for a chat around 5pm today.”

## INFORMATION ON DECEMBER 13, 2012

56. In response to client inquiries following the publication of the Macquarie December 13 Hon Hai Research Report, on December 13, 2012, Kevin Chang forwarded previews of his unpublished research views on Hon Hai to certain of CGMI's large hedge funds and institutional clients. Each of the emails described in this section containing unpublished previews of confidential research information was sent prior to the publication of Kevin Chang's December 14 Hon Hai Research Report.

### **a) Kevin Chang Disclosed Confidential Nonpublic Research Information to SAC Capital** *First Recipient of Unpublished Research*

57. A SAC Capital employee contacted a CGMI employee of Citi Equities, asking "can u **send me everything u have** on the entire iphone 4/4s/5 supply chain?" (Emphasis added.)

58. Within minutes, the Citi Equities employee forwarded the request to two CGMI employees in CIR, directing them to comply with SAC Capital's requests: "Not sure who's world this is in, but can you please send directly to [employee for SAC Capital]? . . . **He needs it asap – works directly for [SAC Capital].**" (Emphasis added).

59. CIR employees responded, supplying the SAC Capital employee with CGMI's Global Supply Chain Handbook and detailed supply chain teardown models on both the Apple iPhone and the Apple iPad.

60. On Thursday, December 13, 2012, at approximately 9:49 A.M. EST, Kevin Chang sent the SAC Capital employee unpublished research, including his own Hon Hai projection numbers, in what Kevin Chang terms as the "New Forecast" ("New Forecast").

61. The New Forecast sent from Kevin Chang to the SAC Capital employee contained Mr. Chang's unpublished research for Apple iPhone order forecasts:

Here is the new forecast

iPhone

4Q12 total 53M (45M iPhone 5 and the rest goes to iPhone 4/4S)

1Q13 total around 33M (25M iPhone 5 and the rest goes to iPhone 4/4S)

iPad

4Q12 total + 12M

1Q13 total around 9M

iPad mini

4Q12 total 7~10M (HH do +6M), . . .

1Q13 total + 10M

. . .

62. The New Forecast stated, among other things, that in the first quarter of 2013, the forecast of Apple orders for iPhones would be cut to 33 million units, consisting of 25 million Apple iPhone 5s, and the rest in 8 million Apple iPhone 4/4Ss.

63. These new figures represented a 26.7% cut from Kevin Chang's December 10, 2012 Hon Hai Research Report, in which his first quarter 2013 order estimates were 45 million Apple iPhones total, consisting of 38 million Apple iPhone5s and 7 million Apple iPhone4/4Ss.

64. The email containing the New Forecast previewed the unpublished research report published the following day by Kevin Chang on Hon Hai.

65. The Division alleges that the New Forecast's Apple iPhone unpublished research for the first quarter of 2013 were what formed the basis for Kevin Chang's reduction in Hon Hai target price and earnings published a day later in the December 14, 2012 ("December 14 Hon Hai Research Report").

66. The New Forecast sent from Kevin Chang also contained additional explanations and predictions concerning Apple products.

***Second Recipient of Unpublished Research***

67. Also on December 13, 2012, Kevin Chang replied via email to an employee of SAC Capital's CR Intrinsic delivering his New Forecast, unpublished research and detailed explanations regarding the new Apple iPhone production forecasts.

***Third Recipient of Unpublished Research***

68. Also on December 13, 2012, at approximately 9:49 A.M. EST, Kevin Chang replied via email to an employee of SAC LP delivering his New Forecast, unpublished research and detailed explanations regarding the new Apple iPhone production forecasts.

***Fourth Recipient of Unpublished Research***

69. Also on December 13, 2012, Kevin Chang replied via email to an employee of SAC Capital's Sigma Capital delivering his New Forecast, unpublished research and detailed explanations regarding the new Apple iPhone production forecasts.

**b) Kevin Chang Disclosed Confidential Nonpublic Research Information to Citadel**

70. In addition to the above, on December 13, 2012, Kevin Chang replied via email to two (2) Citadel employees delivering his New Forecast, unpublished research and detailed explanations regarding the new Apple iPhone production forecasts.

71. Moreover, the email chain between Kevin Chang and two (2) Citadel employees indicated that **the New Forecast is a result of Kevin Chang's own due diligence, not from Hon Hai, Apple, or Macquarie** (Emphasis added).

72. A Citadel employee replied to Kevin Chang shortly after receiving the New Forecast email asking, “**Kevin, just to confirm, these are your estimates?** Not from company?” Kevin Chang replied with two words, “**My estimate.**” (Emphasis added).

**c) Kevin Chang Disclosed Confidential Nonpublic Research Information to GLG Partners**

73. On December 13, 2012, Kevin Chang replied via email to two (2) employees at GLG Partners delivering his New Forecast, unpublished research and detailed explanations regarding the new Apple iPhone production forecasts.

74. After GLG received the New Forecast email, a GLG employee replied to Kevin Chang asking, “When you get a second could you please call me on +[foreign phone number] thanks.” Kevin Chang replied back, saying, “I am flying back to Taiwan this morning. Free to chat Friday afternoon (Friday morning London time).” The GLG employee responded back, asking again, “Just tried you...when you get a moment can you please call me on +[same foreign phone number] thanks.”

**d) Kevin Chang Disclosed Confidential Nonpublic Research Information to T. Rowe Price**

75. On December 13, 2012, Kevin Chang replied via email to a T. Rowe Price employee delivering his New Forecast, unpublished research and detailed explanations regarding the new Apple iPhone production forecasts.

76. In reply to the New Forecast email sent to T. Rowe Price, the T. Rowe Price employee shared with Kevin Chang that “**We still own lots of Apple, despite of [sic] profit-taking earlier.**” (Emphasis added).

**e) Kevin Chang Disclosed Confidential Nonpublic Research Information to Citi Equities and Taiwan Equity Sales**

77. On December 13, 2012, when Kevin Chang emailed his New Forecast to GLG Partners, the

Head of Taiwan Equity Sales was also cc'd on the communication.

78. On December 13, 2012, an employee of Taiwan Equity Sales sent an email to the Head of Taiwan Equity Sales, with an unknown number of bcc'ed individuals. The email states in part:

Sending on behalf of [Head of Taiwan Equity Sales]. Morning. **Key thing to share today is HON HAI which Kevin has been a super bull. Chatters of Apple iphone order cuts in Q1. TRUE. –According to our latest channel checks, chatters of Apple iphone 5 order true. We previously expected 45mn in iphone shipments in Q1 but now ~35mn ... Sales**

**Commentary: I don't have as much patience as Kevin. I'd trim hon hai...Else, SHORT Largan (pure iphone 5 play) to hedge your downside.**

(Emphasis added).

79. At least one recipient of the employee of Taiwan Equity Sales' email was a CGMI employee in Citi Equities.

80. On December 14, 2012, the Citi Equities employee forwarded the email to Kevin Chang (cc'ing another CGMI employee in Citi Equities and CGMI Research Analyst), writing "Received this from Taiwan sales [with employee of Taiwan Equity Sales' email below] ... **they are already going out with that the cuts are likely true.**" (Emphasis added).

81. Kevin Chang, in response to the Citi Equities employee, admitted that the Hon Hai numbers were not yet to be disclosed, stating, "**We apparently can't talk about the new numbers yet,**" even though, by this time, the New Forecast had already been disclosed to at least four (4) CGMI hedge fund and institutional clients (Emphasis added).

82. This preview of confidential unpublished research in the emails described above was sent prior to the public dissemination of Kevin Chang's December 14 Hon Hai Research Report containing virtually identical information at 10:20 A.M. EST on December 14, 2012.



**F. KEVIN CHANG PUBLISHED HON HAI RESEARCH REPORT ON DECEMBER 14, 2012.**

83. On Friday, December 14, 2012, at approximately 10:20 A.M. EST, Kevin Chang published the December 14 Hon Hai Research Report which included a “Buy” rating, but *reduced* prior Apple iPhone order forecasts for the first quarter of 2013 by 24.4% to 34 million Apple iPhones total, consisting of 26 million iPhone5s and 8 million Apple iPhone4/4S’s.

84. The Division’s table below summarizes Kevin Chang’s views on Apple iPhones order forecasts for the first quarter of 2013 during the period of December 10, 2012, through December 14, 2012:

<i>Kevin Chang's Forecasts</i>	Monday, December 10, 2012	Thursday, December 13, 2012	Friday, December 14, 2012
figures in millions of units	Positive Hon Hai Report	<b>New Forecast Email</b>	Negative Hon Hai Report
total iPhone forecast	45	33	34
<b>iPhone 5 forecast</b>	<b>38</b>	<b>25</b>	<b>26</b>
iPhone 4 forecast	7	8	8

85. The December 14 Hon Hai Research Report included virtually identical information to the New Forecast Kevin Chang had previously disseminated to CGMI hedge fund and institutional clients, Citi Equities, and Taiwan Equity Sales. The earlier dissemination of the New Forecast resulted in the communication of unpublished research views to CGMI and certain CGMI clients who had the opportunity to use the information for their own competitive advantage and later publication to other clients.

86. Prior to the publication of the December 14 Hon Hai Research Report, CGMI clients who did not receive the New Forecast did not have the benefit of Kevin Chang’s unpublished research and were left to rely on the prior December 10 Hon Hai Research Report.

**G. CGMI RESEARCH ANALYST DOWNGRADED APPLE ON DECEMBER 16, 2012 - TWO DAYS AFTER KEVIN CHANG'S HON HAI RESEARCH REPORT**

87. As of December 13, 2012, Kevin Chang and CGMI Research Analyst had committed via email to coordinate public dissemination of a Hon Hai research report and an Apple research report for simultaneous publication on Sunday, December 16, 2012.

88. On December 13, 2012, CGMI Research Analyst wrote to Kevin Chang, “**This is something we’re going to have to coordinate.** Can we aim for Monday aim your time?” Kevin Chang agreed, stating, “Yes, I will send u my note tonight taiwan time.” (Emphasis added).

89. CGMI Research Analyst replied again to Kevin Chang, reaffirming their intent for coordinated dissemination and finalizing the simultaneous publication of CGMI Research Analyst’s Apple report and Kevin Chang’s Hon Hai report to be Sunday, December 16, 2012: “I may take longer to write but will send you ahead of time. **We should have our SA’s coordinate the time so they are released at the same time.**” (Emphasis added).

90. The Division alleges that the Hon Hai research report, containing significant cuts in Apple iPhone production numbers, would have a detrimental impact on Apple.

91. The two research reports were published separately. As Kevin Chang described in an email to CGMI Research Analyst on Friday, December 14, 2012, “**I have an *issue* that forces me to publish my HH note on apple order cut note right away. It’s totally out of my control.** I figure that might cause u some inconvenience but there’s pretty much nothing I can do about it.” (Emphasis added).

92. Kevin Chang published his revised Hon Hai Research Report on Friday, December 14 at 10:20 A.M. EST.

93. At the time the December 14 Hon Hai Research Report was published, the Taiwanese Stock Exchange on which Hon Hai (2317.TW) is listed had already closed (10:20 A.M. EST on Friday, December 14, 2012 was 10:20 PM Taiwan time).

94. However, Apple stock had the remainder of Friday to trade on the NASDAQ.

95. On Sunday, December 16, 2012, CGMI Research Analysts authored a *downgrade* of Apple, from a “Buy” to a “Neutral”, citing demand weaknesses of the Apple iPhone 5 and hyperlinking Chang’s Friday revised December 14 Hon Hai Research Report (“the December 16 Apple Research Report”).

96. In the section of the December 16 Apple Research Report titled “Non-US Research Analyst Disclosures” Kevin Chang is included among a list of non-U.S. research analysts who “prepared this report.”

97. On Sunday, December 16, 2012, one CGMI client asked whether “this d/g [downgrade] have some teeth via your Taiwan analyst’s supply chain checks?” CGMI Research Analyst responded to confirm that the research report out Sunday was “**definitely leveraging work done by our Taiwan analyst.**” (Emphasis added).

98. A CGMI client inquired on Sunday, December 16, 2012, where Kevin Chang and CGMI Research Analyst sourced their information in their research reports: “Question-which companies did you meet with in Asia last week that indicated order cuts from Apple? And were these cuts officially confirmed by the companies’ IR/senior management or were they more mid-level managers via channel checks?”

99. CGMI Research Analyst replied, “I typically won’t name who we meet with, but can **confirm that we meet either with IR or senior management in all instances.**” (Emphasis added).

## **H. TRADING BY RECIPIENTS OF CONFIDENTIAL NONPUBLIC RESEARCH INFORMATION**

100. The Division alleges that SAC Capital, Citadel, and T.Rowe Price executed sales of Apple stock on December 13 and 14, 2012.

101. Between 9:00 AM EST December 13 and end of business (adjusted for dividends and splits) on December 14 the price of Apple stock dropped approximately 5.2%, from \$531.15 to \$503.50.

102. Because the December 16 Apple Research Report was published on a Sunday, customers could not act on the information contained therein until trading began on the following day, on Monday, December 17, 2012.

## **I. RELEVANT CGMI POLICIES AND PROCEDURES**

103. At all relevant times, written policies and procedures of CGMI proscribed certain conduct by research analysts in connection with the use of confidential, material nonpublic information, research analysts' communications with third parties, and simultaneous dissemination of research reports in connection with covered companies.

104. CGMI's policy concerning Restrictions on the Use of Material Non-Public Information (MNPI) states that:

Citi employees are prohibited from trading securities (including, but not limited to, equity securities, convertible securities, corporate debt, derivatives and single stock futures) while in possession of MNPI (defined in section 2.2). This prohibition applies to Citi securities as well as the securities of any other issuer while in possession of MNPI. It also applies to transactions for any Citi account, client account, employee account or other account over which the employee has investment discretion. Citi employees are also prohibited from disseminating MNPI to any other person, within Citi or externally, unless that person has a need to know the information.

Conveying to others, where it is reasonable to believe that the person will seek to act on that information improperly ("Tipping") is also strictly prohibited. Citi employees should not provide information to anyone who does not have a need to know, even if the employee doesn't believe that the person will act on the information. Both the person providing the

information and the recipient will be held liable for such misuse of MNPI, regardless of whether profits resulted from the information's misuse.

105. CGMI's policy concerning "Confidential and Material, Nonpublic Information" states that:

"Whether information is material depends on the facts and circumstances. Some examples of information likely to be considered material include:

- Earnings announcements or estimates, or changes to previously released earnings information;
- Significant dividend increases or decreases;
- Expansion or curtailment of operations . . .
- Changes in research recommendations (by the Firm or other Firms) or debt ratings. . ."

106. CGMI's policy on Confidential and Material, Nonpublic Information also includes

"Proprietary Information" which states in pertinent part:

**Proprietary information is Confidential Information owned or created by the Firm. It is presumed to be intrinsically valuable and may provide a competitive advantage to the Firm.** Information about the Firm's business, operations, financial condition, results, and prospect, as well as nonpublic information about the market, should be presumed to be confidential. This includes:

. . . .

- ***Information About the Marketplace*** – such as a major development regarding the earnings or business of a company regardless of whether it is a client or potential client of the Firm. Examples of major developments include a proposed or pending tender offer, privatization, divestiture, recapitalization, bankruptcy, or similar transactions.

107. CGMI's policy concerning "Client Communications and Simultaneous Distribution" states in pertinent part:

Confidential Information may be obviously "material" given that it may have an immediate impact on the stock price of the subject company. However, there are many grey scenarios where it will not be obvious as how the market will react to the non-public information. Accordingly, all CIR employees are encouraged to treat all non-public information as material in the initial instance to minimize the risk of any inadvertent breaches . . .

CIR policy requires that terminations/initiations of coverage and changes in ratings, EPS ratios<sup>2</sup> and target prices only be made available to clients in a published note/report and in no

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<sup>2</sup> Changes in EPS estimates up to 3% do not require a new report/note.

other form. Such information must be disseminated broadly (i.e. via GEO) and simultaneously. This is the requirement of “simultaneous distribution.”

For the purposes of this policy, a research view is defined as a written or oral communications that provides information reasonably sufficient upon which to base an investment decision in relation to one or more financial instruments including, but not limited to, a recommendation or suggestion of an investment strategy or an analysis or an opinion on the present or future value of a security, issuer of securities, commodity or any related derivative contract, or an analysis of the price or market for any derivative.

### **Interaction with Sales and Trading Personnel**

You should treat the Firm’s sales and trading personnel no differently than any external client and must ensure that any research view you communicate to such persons is your published research view.

You must not communicate a new research view (whether oral or written) firstly for internal use for Citi’s own advantage, and then for later publication to external clients.

108. CGMI’s policy concerning “Research Independence” states in pertinent part:  
The Firm provides a full range of investment and financial services to a wide range of clients. In the course of providing such services, perceived, potential and/or actual conflicts may arise between CIR, clients and other divisions of Citi, including Investment Banking, Corporate Broking and Sales & Trading. This Policy is intended to address and manage these conflicts and ensure the independence of Research . . .

- Draft Research – CIR employees are not permitted to communicate to a non-CIR employee (or a non-employee) any portions of a Research report prior to the Research report being publicly disseminated, with the exception of CIR Legal Compliance and EROC. Among other things, this restriction expressly prohibits a Research Analyst from making a “courtesy” call to a company before the Research report is made public; sending a subject company draft Research for fact checking; or giving Sales or Trading personnel or clients a “heads-up” regarding a Research report prior to publication.

## **VII. CONCLUSIONS OF LAW**

109. CGMI violated its own policies and procedures, federal and state securities laws, and the 2012 CGMI Consent Order.

## **FINRA RULES**

110. CGMI, as a FINRA member, was required by FINRA and NASD rules and regulations to reasonably design a supervisory system to prevent the improper disclosure of confidential nonpublic information.

## **FEDERAL SECURITIES LAWS**

111. CGMI, as a SEC registered broker-dealer, was required by the 1934 Exchange Act to establish, maintain and enforce reasonable policies and procedures to prevent the misuse of material, nonpublic information.

## **PRIOR CONSENT ORDER WITH THE DIVISION**

112. As a result of the 2012 CGMI Consent Order, CGMI, as a Massachusetts registered broker-dealer, is prohibited by the Act and the Consent Order from disseminating draft research relating to iPhone forecasts on December 13, 2012, prior to publication of new information.

## **VIII. VIOLATIONS OF MASSACHUSETTS UNIFORM SECURITIES ACT**

### **COUNT I: VIOLATIONS OF § 204(a)(2)(B)**

113. Section 204(a)(2)(B) provides that:

(a) The secretary may by order impose and administrative fine or censure or deny, suspend or revoke any registration or take any other appropriate action if he finds (1) that the order is in the public interest and (2) that the applicant or registrant or, in the case of a broker-dealer or investment adviser, any partner, officer, or director, any person occupying a similar status or performing similar functions, or any person directly or indirectly controlling the broker-dealer or investment adviser: --

(B) has willfully violated or willfully failed to comply with any provision of this chapter or a predecessor chapter or any rule or order under this chapter or a predecessor chapter;

114. The Division herein restates and re-alleges the facts set forth in Section VI above.

115. The conduct of Respondent, as described above in Section VI, in conjunction with the

prior 2012 CGMI Consent Order entered into with the Division as discussed in Section V, constitutes a violation of Mass. Gen. Laws ch. 110A, §204(a)(2)(B).

**COUNT II: VIOLATIONS OF § 204(a)(2)(G)**

116. Section 204(a)(2)(G) of the Act provides in pertinent part:

(a) The secretary may by order impose an administrative fine or censure or deny, suspend, or revoke any registration or take any other appropriate action if he finds (1) that the order is in the public interest and (2) that the applicant or registrant or, in the case of a broker-dealer or investment adviser, any partner, officer, or director, any person occupying a similar status or performing similar functions, or any person directly or indirectly controlling the broker-dealer or investment adviser:—

(G) has engaged in any unethical or dishonest conduct or practices in the securities, commodities or insurance business.

117. The corresponding regulation at 950 CMR § 12.204 (1)(a) provides in pertinent part:

(1) Dishonest and unethical practices in the securities business.

(a) Broker-Dealers. Each broker-dealer shall observe high standards of commercial honor and just and equitable principles of trade in the conduct of its business. Acts and practices, including, but not limited to the following, are considered contrary to such standards and constitute dishonest or unethical practices which are grounds for imposition of an administrative fine, censure, denial, suspension or revocation of a registration, or such other appropriate action:

(28) Failing to comply with any applicable provision of FINRA member conduct rules or any applicable fair practice or ethical standard promulgated by the SEC or by a self-regulatory organization approved by the SEC.

**1. FINRA Rule 2010**

118. FINRA Rule 2010 states that:

A member, in the conduct of its business, shall observe high standards of commercial honor and just and equitable principles of trade.

**2. NASD Rules 1050 and 3010**

119. With respect to the requirements for non-U.S. affiliate research analysts, NASD Rule



1050 states in pertinent part that:

- (f) The requirements of paragraph (a) shall not apply to an associated person who:
- (1) is an employee of a non-member foreign affiliate of a member ("foreign research analyst"),
  - (2) resides outside the United States, and
  - (3) contributes, partially or entirely, to the preparation of globally-branded or foreign affiliate research reports but does not contribute to the preparation of a member's research, including a mixed-team report, that is not globally-branded.

Provided that the following conditions are satisfied:

(A) A member that publishes or otherwise distributes globally-branded research reports partially or entirely prepared by a foreign research analyst must subject such research to pre-use review and approval by a registered principal in accordance with NASD Rule 1022(a)(5) or a supervisory analyst pursuant to NYSE Rule 344.11. In addition, the member must ensure that such research reports comply with NASD Rule 2711, as applicable.

(B) In publishing or otherwise distributing globally-branded research reports partially or entirely prepared by a foreign research analyst, a member must prominently disclose:

- (i) each affiliate contributing to the research report;
- (ii) the names of the foreign research analysts employed by each contributing affiliate;
- (iii) that such research analysts are not registered/qualified as research analysts with the NYSE and/or NASD; and
- (iv) that such research analysts may not be associated persons of the member and therefore may not be subject to Rule 2711 restrictions on communications with a subject company, public appearances and trading securities held by a research analyst account.

(C) The disclosures required by paragraph (f)(3)(B) of this Rule must be presented on the front page of the research report or the front page must refer to the page on which the disclosures can be found. In electronic research reports, a member may hyperlink to the disclosures. References and disclosures must be clear, comprehensive and prominent.

(D) Members must establish and maintain records that identify those individuals who have availed themselves of this exemption, the basis for such exemption, and evidence of compliance with the conditions of the exemption. Failure to establish and maintain such records shall create an inference of a violation of Rule 1050.

Members must also establish and maintain records that evidence compliance with the applicable content, disclosure and supervision provisions of Rule 2711. Members must maintain these records in accordance with the supervisory requirements of Rule 3010, and in addition to such requirement, the failure to establish and maintain such records shall create an inference of a violation of the applicable content, disclosure and supervision provisions of Rule 2711.

(E) Nothing in paragraph (f) of this Rule shall affect the obligation of any person or broker-dealer, including a foreign broker-dealer, to comply with the applicable provisions of the federal securities laws, rules and regulations and any self-regulatory organization rules.

(F) The fact that a foreign research analyst avails himself of the exemption in paragraph (f) shall not be probative of whether that individual is an associated person of the member for other purposes, including whether the foreign research analyst is subject to the Rule 2711 restrictions on communications with a subject company, public appearances and trading securities held by a research analyst account.

(G) A member that distributes non-member foreign affiliate research reports that are clearly and prominently labeled as such must comply with the third-party research report requirements in Rule 2711(h)(13).

(H) For the purposes of the exemption in paragraph (f), the terms "affiliate," "globally-branded research report" and "mixed-team research report" shall have the following meanings:

- (i) "Affiliate" shall mean a person that directly or indirectly controls, is controlled by, or is under common control with, a member.
- (ii) "Globally-branded research report" refers to the use of a single marketing identity that encompasses the member and one or more of its affiliates.
- (iii) "Mixed-team research report" refers to any member research report that is not globally-branded and includes a contribution by a research analyst who is not an associated person of the member.

3. **NASD Rule 3010(a)** states in relevant part: .

**(a) Supervisory System**

Each member shall establish and maintain a system to supervise the activities of each registered representative, registered principal, and other associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable NASD Rules. Final responsibility for proper supervision shall rest with the member.

120. The Division herein restates and re-alleges the facts set forth in Section VI above.

121. Respondent's conduct, as described in Section VI constitutes a violation of FINRA Rule 2010 and NASD Rules 1050 and 3010. In conjunction with the foregoing, CGMI violated 950 CMR § 12.204 (1)(a)(28), which constitutes a violation of Mass. Gen. Laws ch. 110A, §204(a)(2)(G).

**COUNT III: VIOLATIONS OF §204(a)(2)(J)**

122. Section 204(a)(2)(J) of the Act provides in pertinent part:

The secretary may by order, deny, suspend, or revoke any registration if he finds

(1) that the order is in the public interest and (2) that the applicant or registrant

...

(J) has failed to reasonably to supervise agents, investment adviser representatives, or other employees to assure compliance with this chapter;

123. The Division herein restates and re-alleges the facts set forth in Section VI above.

124. The conduct of Respondent, solely in its capacity as a Broker Dealer, as described above in Section VI, constitutes a violation of Mass. Gen. Laws ch. 110A, §204(a)(2)(J).

**IX. ORDER**

CGMI consents to the entry of this Order,

**IT IS HEREBY ORDERED:**

Respondent CGMI in full settlement of these matters admits the Division's Statement of Facts set forth in Section VI herein, neither admits nor denies the conclusions of law set forth in Section VII and violations of law set forth in Section VIII herein, and makes the following representations and agrees to the undertakings herein as part of the Order:

- A. Respondent CGMI agrees to permanently cease and desist from violations of the Act.
- B. Respondent CGMI agrees to be censured by the Division.
- C. Respondent CGMI shall pay a civil penalty in the amount of \$30,000,000.00 (thirty

million) within 30 (thirty) days after the entry of an Order pursuant to this Offer.

Payment shall be: (1) made by United States postal money order, certified check, bank cashier's check, bank money order, or wire; (2) made payable to The Commonwealth of Massachusetts; and (3) either hand-delivered, mailed to One Ashburton Place, Room 1701, Boston, Massachusetts 02108; or wired per Division instructions; and (4) submitted under cover letter or other documentation that identifies the Respondent making the payment and the docket number of the proceedings.

#### D. Internal Review

In light of the facts agreed to in Section VI above, Respondent CGMI agrees within one hundred and eighty (180) days of the signed Order pursuant to this Offer, and again annually for a period of three (3) years following the entry of the Order, to review its written policies and procedures to determine that they are reasonably designed to ensure compliance with all applicable federal and state securities laws with respect to the following:

- a. The review and surveillance of electronic communications by CGMI research employees, including but not limited to communications between CGMI research employees and employees of non-U.S. Affiliates of CGMI and/or employees of other unaffiliated entities such as institutional and retail clients;
- b. CGMI research department business standards, including but not limited to those that govern conflict management, internal and external communications, business ethics, and client relationships and responsibilities; and

c. Escalation procedures with regard to violations of the policies and procedures referenced in subsections (a) and (b) above, to determine whether these procedures are reasonably designed to achieve compliance with federal and state securities laws. If any changes are determined to be appropriate based on this review, such changes shall be promptly referred to CGMI research legal and compliance personnel to facilitate prompt resolution. Corrective action taken as part of the resolution process may include but is not limited to, providing additional education and training, revising and/or supplementing existing policies and procedures, and/or referral to federal and state regulators as required by law and regulations promulgated thereunder.

E. Education and Training:

Respondent CGMI agrees within one hundred and eighty (180) days of the signed Order pursuant to this Offer that all CGMI publishing equity research analysts shall participate in a training program that includes, among other things, instruction on the disclosure requirements of governing federal and state securities laws as well as the application of those requirements to the potential dissemination of confidential, nonpublic research information. In addition, within ninety (90) days following the hiring by, or transfer to CGMI of any new publishing equity research analysts, each such employee shall be required to participate in the same or similar training program. Attendance shall be mandatory for all CGMI publishing equity research analysts. CGMI shall provide for appropriate record keeping to track compliance with these requirements including, but not limited to, attendance records. Such

records shall be maintained for a period of no less than six (6) years and must be provided to the Division upon request.

F. Establish, Implement and Enforce Policies and Procedures:

- a. Director or Co-Director of Citigroup Research shall certify annually for a period of three (3) years following the entry of this signed order compliance with all material aspects of the review and training requirements of Sections D and E above; and
- b. Director or Co-Director of Citigroup Research shall report annually for a period of three (3) years following the entry of this signed order any changes determined to be necessary as part of the process described in Section D(c) above.

The certifications and any such additional materials shall be submitted to the Director of the Massachusetts Securities Division, with a copy to the Enforcement Section.

G. Reporting Requirements:


Any failure to comply with the requirements set forth in paragraphs D through F above shall be reported to the Division within ten (10) days of discovery. The report shall be submitted to the Director of Enforcement, Massachusetts Securities Division with a copy to the Enforcement Section. For good cause shown, and upon receipt of a timely request from CGMI, the Division may extend any of the procedural dates set forth above.

H. Nothing herein is intended to or shall be construed to replace, supersede or override, with respect to Respondent, federal securities laws, rules and regulations of the rules of any self-regulatory organization.

- I. Respondent CGMI agrees that it shall not seek or accept, directly or indirectly, reimbursement or indemnification, including, but not limited to any payments made pursuant to any insurance policy, with regard to all amounts that Respondent shall pay to the Division pursuant to the Division's Order.
- J. Respondent CGMI further agrees that it shall not claim, assert, or apply for a tax deduction or tax credit with regard to any state, federal or local tax for any amounts that Respondent shall pay to the Division pursuant to the Division's Order.
- K. Respondent CGMI agrees that, upon issuance of an Order by the Division that contains the terms as set forth above, if it fails to comply with any of the terms set forth in the Division's Order, the Enforcement Section may institute an action to have this agreement declared null and void. Upon issuance of an appropriate order, after a hearing, the Enforcement Section may re-institute the actions and investigations that it had brought against the Respondent.
- L. The Order as entered into by The Commonwealth hereby waives any disqualification contained in the laws of The Commonwealth, or rules or regulations thereunder, including any disqualifications from relying upon the registration exemptions or safe harbor provisions that CGMI or its affiliates may be subject to as a result of the findings contained in the Order. The Consent Order also is not intended to subject CGMI or its affiliates to any disqualifications contained in the federal securities laws, rules and regulations thereunder, the rules and regulations of self-regulatory organizations or various states' or U.S. Territories' securities laws, including, without limitation, any disqualifications from relying upon the registration exemptions or safe harbor provisions. In addition, the Consent Order is not intended to form the basis for any such

disqualifications.

**WILLIAM FRANCIS GALVIN  
SECRETARY OF THE COMMONWEALTH**



By. \_\_\_\_\_

Bryan J. Lantagne, Esq.  
~~First Deputy-Secretary of State~~  
Director-Massachusetts Securities Division  
Massachusetts Securities Division  
One Ashburton Place, Room 1701  
Boston, Massachusetts 02108-1552

Dated: October 2, 2013