

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

ADMINISTRATIVE PROCEEDINGS RULINGS
Release No. 1652/July 25, 2014

ADMINISTRATIVE PROCEEDING
File No. 3-15873

In the Matter of

THOMAS R. DELANEY II and
CHARLES W. YANCEY

ORDER ON MOTIONS

The Securities and Exchange Commission (Commission) issued an Order Instituting Administrative and Cease-and-Desist Proceedings (OIP) on May 19, 2014, pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934 (Exchange Act) and Section 9(b) of the Investment Company Act of 1940 (Investment Company Act). The OIP alleges that Penson Financial Services, Inc. (Penson), violated Rule 204T(a)/204(a) of Regulation SHO, pertaining to the regulation of short sales, and that Thomas R. Delaney II (Delaney) and Penson's Senior Vice President of Securities Lending (Vice President)¹ willfully aided and abetted and caused Penson's violations, and that Charles W. Yancey (Yancey) failed reasonably to supervise Delaney and the Vice President with a view to preventing and detecting their violations.

Yancey and Delaney filed Answers and motions for a more definite statement on June 12, 2014, and June 13, 2014, respectively. A prehearing conference was held on June 23, 2014. I denied Respondents' motions for a more definite statement on June 25, 2014. Thomas R. Delaney II, Admin. Proc. Rulings Release No. 1557, 2014 SEC LEXIS 2223. A hearing will begin on October 27, 2014.

¹ Michael H. Johnson (Johnson) was Senior Vice President of Penson Worldwide, Inc.'s Securities Lending Department. Michael H. Johnson, Exchange Act Release No. 72186, 2014 SEC LEXIS 1711 (May 19, 2014). The Commission accepted Johnson's Offer of Settlement and on May 19, 2014, he was (1) ordered to cease and desist from committing or causing any violation or any future violations of Rule 204 of Regulation SHO, (2) subjected to an industry-wide bar pursuant to Section 15(b)(6) of the Exchange Act and Section 9(b) of the Investment Company Act, with the right to reapply for reentry after five years, and (3) ordered to pay a civil money penalty of \$125,000, which may be distributed pursuant to Section 308(a) of the Sarbanes-Oxley Act of 2002, as amended (Fair Fund distribution).

Pending Issues

On July 9, 2014, Delaney filed Motions to Compel Production of: (1) Statements by Division Witnesses Under Rule 231(a) and Supporting Brief (Motion 1); (2) Withheld Document List Under Rule 230(c) and Supporting Brief (Motion 2); and (3) Material Exculpatory and Impeachment Evidence Under Rule 230(b)(2) and Supporting Brief (Motion 3). On July 10, 2014, Delaney and Yancey filed a Joint Motion for Issuance of Deposition of Johnson Under Rule 233 and Supporting Brief (Joint Motion).

On July 15, 2014, the Division filed its Consolidated Response to Motions 1, 2, and 3 (Consolidated Response), and filed its Response to Respondents' Joint Motion.

On July 17, 2014, Respondents filed a letter (Respondents' Letter) objecting to the Division's posture on the deposition testimony of Johnson. Respondents argue that if their request to depose Johnson is granted, the Division should not be allowed to call him as a witness and Respondents should begin and end the deposition examination. Respondents' Letter at 1-2. According to Respondents, Johnson's counsel is willing to make Johnson available for the deposition only if it is in lieu of testimony at the hearing. Id. at 1. As a compromise, if the Division agrees not to call Johnson as a witness, Respondents will not dispute the Division opening the deposition, however, they insist that it is their right to close the examination. Id. at 2.

On July 18, 2014, Randall J. Fons, counsel for Johnson, filed a letter (Fons Letter). Johnson's preferred position is that the testimony he provided to the Division in May 2012 and January 2013 be used at the hearing as his testimony. Fons Letter at 1 n.1. Johnson argues that subjecting him to both a deposition and live testimony would be unnecessary and inhumane, due to Johnson's medical condition. Id. at 2. If a deposition is deemed necessary, Johnson wants to be deposed at Fons's Denver office and with a one-hour limit on questions by each party. Id. Finally, any deposition would have to be scheduled after September 15, 2014, because Johnson has travel plans and business obligations in August and early September. Id.

On July 18, 2014, the Division filed a Motion for Leave to File Additional Briefing in Response to Respondents' Joint Motion. The Division requests leave to make an additional filing on the subject of Johnson's deposition by July 25, 2014.

On July 21, 2014, Delaney filed his Consolidated Reply Brief in Support of Various Motions to Compel (Consolidated Reply). In the Consolidated Reply, Delaney reiterates his position that contrary to applicable due process, the Division is gaining an unwarranted prosecutorial advantage by withholding information needed for Delaney's defense. Delaney contends that the Division has the burden of showing that every element of the claimed privilege exists for every document withheld and that each withheld document does not contain Brady or Jencks material. Consolidated Reply at 3.

Disposition of Pending Issues

Motion to Compel Production of Statements by Division Witnesses Under Rule 231(a) of the Commission's Rules of Practice

Rule 231(a) of the Commission's Rules of Practice, 17 CFR § 201.231(a), provides that:

Any respondent in an enforcement or disciplinary proceeding may move that the Division of Enforcement produce for inspection and copying any statement of any person called or to be called as a witness by the Division of Enforcement that pertains, or is expected to pertain, to his or her direct testimony and that would be required to be produced pursuant to the Jencks Act, 18 U.S.C. 3500. For purposes of this rule, *statement* shall have the same meaning set forth in 18 U.S.C. 3500(e). Such production shall be made at a time and place fixed by the hearing officer and shall be available to any party, provided, however, that the production shall be made under conditions intended to preserve the items to be inspected or copied.

Delaney wants the Division to produce for my review any and all prior statements by Division witnesses, including the notes of any interviews of witnesses who will or may be called to testify, to determine whether the notes comprise a full or partial substantially verbatim recording of the witnesses' statements. Motion 1 at 4.

The Division responds that the Jencks Act only requires production of, in essence, verbatim witness statements. Before the OIP was issued, the Division provided Respondents with all investigative testimony transcripts and later it provided Respondents with the declarations of potential witnesses. Consolidated Response at 6-7, 14. The Division takes issue with Delaney's position that an attorney's interview notes are Jencks Act statements and that Jencks Act material is required to be produced over two months before the hearing is scheduled to begin. *Id.* at 14. Division counsel confirms that none of the withheld interview notes were shown to, or ratified by, a witness. *Id.* at 17, n.8.

There is nothing that indicates the Division has not acted in accord with Delaney's description of the Division's obligation under the Jencks Act, which includes the description of a statement that has to be produced as: (1) a written statement made by a witness and signed or otherwise adopted or approved by him/her; (2) a stenographic, mechanical, electrical, or other recording, or a transcription thereof, which is a substantially verbatim recital of an oral statement made by a witness and recorded contemporaneously with the making of such oral statement; or (3) a statement, however taken or recorded, or a transcription thereof, if any, made by a witness to a grand jury. Motion 1 at 2 (citing 18 U.S.C. § 3500(e)). However, given Delaney's vehement position that the Division has failed to carry out its obligations, I ORDER the Division to provide my Office by August 29, 2014, for in camera review, all interview notes in the investigative file for any individual to be called as a witness that the Division has withheld from Delaney as non-Jencks Act material. The Division shall provide Respondents with Jencks Act material when it provides Respondents with its list of witnesses.

Motion to Compel Production of Withheld Document List Under Rule 230(c) of the Commission's Rules of Practice

Rule 230(c) of the Commission's Rules of Practice, 17 CFR § 201.230(c), provides that:

The hearing officer may require the Division of Enforcement to submit for review a list of documents or categories of documents withheld pursuant to paragraphs (b)(1)(i) through (b)(1)(iv) of this rule or to submit any document withheld, and may determine whether any such document should be made available for inspection and copying.

Delaney wants a list of documents that the Division has withheld from production pursuant to Rule 230(c) and the basis for withholding each document. Motion 2 at 1, 4. The Division responds that it is willing to provide its withheld document list for review by the hearing officer, which it states is the process provided for in Rule 230(c). Consolidated Response at 7. Attached to Motion 2 are Exhibits A-C, letters between Delaney and the Division. The Division's letter dated June 30, 2014, lists five categories of withheld documents. Motion 2, Ex. C. Delaney is not satisfied with this production. He argues that: (1) it was not made pursuant to Rule 230(c); (2) no basis exists for withholding some of the categories of documents withheld such as witness statements and third-party communications; and (3) the list is too generalized and vague. *Id.* at 2-4.

The person asserting a privilege has the burden of establishing its essential elements. United States v. BDO Seidman, 337 F.3d 802, 811 (7th Cir. 2003). The Division's letter of June 30, 2014, consisting of five two-sentence paragraphs stating that "Notes of interviews," "Internal memoranda, notes, and writings authored by Commission staff," "Written communications among Commission staff," "Written communications among Division staff and experts," and "Some e-mail communications with third-parties" are being withheld based on the attorney work product privilege, is not sufficient to meet this burden.

Following the directive of Rule 230(c), I ORDER the Division to submit for my review by August 29, 2014, a privilege log that includes for each withheld document the date of the document, the author and recipient, the type of document, and the privileged claimed. See Dole v. Milonas, 889 F.2d 885, 890 (9th Cir. 1989), see also Michael Sassano, Securities Act Release No. 8865, 2007 WL 4699012, at *3 (Nov. 30, 2007).

Motion to Compel Production of Material Exculpatory and Impeachment Evidence Under Rule 230(b)(2)

Rule 230(b)(2) of the Commission's Rules of Practice, 17 CFR § 201.230(b)(2), provides that nothing in the paragraph permitting the Division to withhold certain documents "authorizes the Division of Enforcement in connection with an enforcement or disciplinary proceeding to withhold, contrary to the doctrine of Brady v. Maryland, 373 U.S. 83, 87 (1963), documents that contain material exculpatory evidence."

Delaney argues that even though the Division represented in a letter that no Brady material has been withheld, it must do more. Motion 3 at 2. Delaney believes that several categories of material that the Division has withheld relate to communications with potential witnesses and these communications are likely to disclose information that may lead to a basis for impeachment. Id. Delaney wants to make clear that any privileged material that contains exculpatory evidence must be produced. Id. at 3-4. Delaney asserts that the Division's withholding of privileged documents violates Rule 230(b)(2) and Brady. Id. at 5-9. Delaney insists that there is Brady material in the interview notes and written communications among Commission staff and its experts because any communication that is adverse to the Division's position is fruitful impeachment evidence or may lead to the discovery of impeachment evidence and must be disclosed under the Brady doctrine. Id. at 7. Finally, Delaney maintains that the Division has failed to establish that it has conducted a proper Brady review. Id. at 8-9.

The Division contends that Delaney's Brady position is an attempt to obtain material protected from disclosure: i.e., staff interview notes and communications between the Division and its experts. Consolidated Response at 9. The Division reaffirms that no Brady material has been withheld from production and it will notify Delaney if it discovers any. Id. The Division disagrees that "anything in the notes that is not inculpatory must necessarily be exculpatory," and that it must produce anything that "might generate a lead for Delaney to pursue." Id. at 11. The Division also argues that if it locates Brady material in a document protected from disclosure, it must only produce the material itself and not the protected document. Id. at 10 (citing optionsXpress, Inc. Exchange Act Release No. 70698, 2013 WL 5635987, at *4 n.19 (Oct. 16, 2013)).

I DENY Motion 3, except that I ORDER the Division to file for the record by August 29, 2014, a statement summarizing the measures the Division has taken to comply with Brady and an affirmation by Division counsel that to the best of her knowledge and belief those measures are sufficient to uncover any Brady materials in the investigative file.

Respondents' Joint Motion to Take Johnson's Deposition

Rule 233(a) of the Commission's Rules of Practice, 17 CFR § 201.233(a), permits depositions upon oral examination by motion "setting forth the reasons why such deposition should be taken including the specific reasons why the party believes the witness will be unable to attend or testify at the hearing." Rule 233(b) requires a finding that it is likely the prospective witness,

will be unable to attend or testify at the hearing because of age, sickness, infirmity, imprisonment, other disability, or absence from the United States, unless it appears that the absence of the witness was procured by the party requesting the deposition; and that the taking of the deposition will serve the interests of justice. 17 CFR § 201.233(b).

Respondents maintain that Johnson is a critical witness and that a wide range of his cognitive abilities have been negatively impacted by Parkinson's disease, his condition will likely decline, and he could become unavailable at the last moment. Joint Motion at 2-4.

The Fons Letter states that Johnson disagrees with Respondents' description of the effect of Parkinson's syndrome on Johnson's ability to testify at the hearing, but notes that the stress of testifying does aggravate Johnson's medical condition. Fons Letter at 1-2.

I DENY the Joint Motion because there is nothing that indicates that Johnson is unwilling or unfit to testify at the hearing subject to a subpoena. According to the Fons Letter, Johnson is actively traveling and conducting business. If Johnson is subpoenaed, I will make every effort to accommodate his medical condition. The Division's motion for leave to file additional briefing is also denied.

Brenda P. Murray
Chief Administrative Law Judge