

UNITED STATES OF AMERICA  
Before the  
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDINGS RULINGS

Release No. 659/August 3, 2010

ADMINISTRATIVE PROCEEDING

File No. 3-13847

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In the Matter of

MORGAN ASSET MANAGEMENT, INC.,  
MORGAN KEEGAN & COMPANY, INC.,  
JAMES C. KELSOE, JR., and  
JOSEPH THOMPSON WELLER, CPA

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: ORDER DENYING RECONSID-  
: ERATION, CERTIFICATION,  
: AND A STAY  
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The Securities and Exchange Commission (Commission or SEC) issued an Order Instituting Proceedings (OIP) in this matter on April 7, 2010. The schedule requires Respondents to identify their prospective witnesses and proposed exhibits and file the direct written testimony of their proposed experts by August 10, 2010. The hearing begins on September 13, 2010.

On June 1, 2010, Respondents served a subpoena *duces tecum* on the Commission's Office of Compliance Inspections and Examinations (OCIE). On June 16, 2010, OCIE moved to quash the subpoena. For reasons never explained, OCIE did not file an accompanying motion to delay its obligation to comply with the subpoena pending a ruling on the motion to quash. On July 20, 2010, after considering pleadings submitted by OCIE and Respondents, I granted the motion to quash in part and denied it in part (July 20 Order).

On July 27, 2010, OCIE moved for reconsideration of the July 20 Order. In the alternative, OCIE asked me to certify my ruling for interlocutory review by the Commission and to stay the July 20 Order pending the completion of interlocutory review. On July 30, 2010, Respondents opposed OCIE's motion. The Division of Enforcement (Division) also filed a "limited response" to OCIE's motion.

Motion for Reconsideration

OCIE invokes Section 929I of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), Pub. L. No. 111-203, 124 Stat. 1376 (2010), which was

signed by the President on July 21, 2010, and took effect on July 22, 2010.<sup>1</sup> According to OCIE, Section 929I protects from compulsory disclosure all the documents sought by Respondents' subpoena.<sup>2</sup>

OCIE's motion for reconsideration fails to address the threshold question of whether Section 929I should be construed to apply prospectively or retroactively. The Supreme Court has considered the retroactive application of statutes in several opinions. In Bradley v. Richmond Sch. Bd., 416 U.S. 696, 711 (1974), it held that "a court is to apply the law in effect at the time it renders its decision, unless doing so would result in manifest injustice or there is statutory direction or legislative history to the contrary." In Bowen v. Georgetown Univ. Hosp., 488 U.S. 204, 208 (1988), the Court ruled that "[r]etroactivity is not favored in the law. Thus, congressional enactments and administrative rules will not be construed to have retroactive effect unless their language requires this result." See also Landgraf v. USI Film Prods., 511 U.S. 244, 263-65 (1994) (recognizing the "apparent tension" between Bradley and Bowen); Kaiser Aluminum & Chem. Corp. v. Bonjorno, 494 U.S. 827, 837 (1990) (same).

Here, it is unnecessary to choose sides in the Bradley/Bowen debate, because prospective application of Section 929I is indicated even under Bradley: the delayed effective date of the Dodd-Frank Act constitutes "statutory direction" that Section 929I is to be applied prospectively only.<sup>3</sup> See Wright v. FEMA, 913 F.2d 1566, 1572 & n.13 (11th Cir. 1990); Criger v. Becton, 902 F.2d 1348, 1351 (8th Cir. 1990); Ragin v. Harry Macklowe Real Estate Co., 801 F. Supp. 1213, 1228 (S.D.N.Y. 1992) (collecting cases). Moreover, implementation of Section 929I may require revision to various Commission regulations. No such notice-and-comment rulemakings have yet commenced.

I hold that OCIE may not claim the protection of Section 929I of the Dodd-Frank Act to resist production of documents in response to an administrative subpoena issued before July 22, 2010.

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<sup>1</sup> OCIE erroneously asserts that the new legislation took effect on July 21, 2010. Section 4 of the Dodd-Frank Act states that, "[e]xcept as otherwise specifically provided," the Act "shall take effect [one] day after the date of enactment." Section 929I does not otherwise specifically provide.

<sup>2</sup> In its brief two-week life, Section 929I has already provoked much controversy. See, e.g., Kara Scannell, *SEC Gets FOIA Foil in Financial Law*, WALL ST. JOURNAL, July 31, 2010; *Darkness at the SEC*, NEW YORK POST, July 30, 2010; Oren Yaniv, *Financial Reform Bill Signed by President Obama Gives SEC "Free Pass,"* NEW YORK DAILY NEWS, July 29, 2010. Several members of Congress have expressed concern or called for its repeal. See, e.g., Statement of Senator Ted Kaufman of Delaware, dated July 29, 2010; SEC Freedom of Information Restoration Act, H.R. 5924, 111th Cong. (2010).

<sup>3</sup> OCIE cannot be heard to argue that a delay of one day is not much of a delay. The Dodd-Frank Act differs from innumerable other statutes which provide that they will take effect on the date of enactment.

## Motion for Certification

Rule 400(a) of the Commission's Rules of Practice provides that petitions by parties for interlocutory review are disfavored, and the Commission ordinarily will grant a petition to review a hearing officer's ruling prior to its consideration of an initial decision only in extraordinary circumstances. The Rule further provides that the Commission may decline to consider a ruling certified by a hearing officer pursuant to Rule 400(c) or the petition of a party who has been denied certification if it determines that interlocutory review is not warranted or appropriate under the circumstances.

OCIE is not a party to this proceeding. Rule 101(a)(8) of the Commission's Rules of Practice defines "party" to mean "the interested division," the Respondents, or "any person seeking Commission review of a decision." Rule 101(a)(6) defines "interested division" to mean "a division or an office assigned primary responsibility by the Commission to participate in a particular proceeding." In this proceeding, the Division of Enforcement is the only "interested division."<sup>4</sup> To the best of my knowledge, the Commission has never construed the clause of Rule 101(a)(8) affording party status to "any person seeking Commission review of a decision." I find that clause could not possibly be intended literally to include the proverbial man-on-the-street who has strong opinions, but no stake in the outcome of a proceeding. It can only have meaning by reference to Rule 210(a)(1) of the Commission's Rules of Practice, which provides that "[n]o person shall be granted leave to become a party . . . in an enforcement . . . proceeding . . . except as authorized by" Rule 210(c). OCIE has not sought leave to participate as a party pursuant to Rule 210(c).

Of course, under Rule of Practice 400(a), the Commission reserves the right, at any time, on its own motion, to direct that any matter be submitted to it for review. The Commission has, on one occasion, taken own-motion interlocutory review of a matter at the request of a non-party. Clarke T. Blizzard, 55 S.E.C. 754, 755-56 (2002). The question is: if petitions for interlocutory review are "disfavored" when presented by parties, should they not be "strongly disfavored" when presented by non-parties? Cf. Rule of Practice 161(b)(1) (describing one type of motion that is strongly disfavored).

Enactment of Section 929I of the Dodd-Frank Act does not provide a sound basis for the Commission to take interlocutory review of the July 20 Order on its own motion. The change in the law did not become effective until nearly six weeks after OCIE was required to comply with the subpoena in question. See pp. 5-6, infra. Moreover, it would be difficult to

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<sup>4</sup> In a proceeding to bar an accountant from appearing and practicing before the Commission, the Division of Enforcement and the Office of the Chief Accountant would be "the interested divisions." In a proceeding to bar an attorney from appearing and practicing before the Commission, the Office of General Counsel would be "the interested division." It is unclear whether OCIE could ever qualify as "the interested division."

limit interlocutory review of this issue to the impact of Section 929I on administrative subpoenas. The larger and more controversial question is whether Section 929I should be applied retroactively to block disclosure of information sought in pending requests under the Freedom of Information Act (FOIA). There is no sound basis for using this adjudicatory proceeding to issue a declaratory order under 5 U.S.C. § 554(e), interpreting the impact of Section 929I on pending FOIA appeals.<sup>5</sup> Just as OCIE is not a party to this proceeding, so too, no FOIA requestors are parties to this proceeding. Their rights should not be determined here.

Nor should the Commission take interlocutory review on its own motion to review those aspects of the July 20 Order partially denying OCIE's motion to quash.

OCIE cannot prevail on interlocutory review by arguing that the subpoena is burdensome. In Michael Sassano, 92 SEC Docket 111, 114 & nn.8-10 (Nov. 30, 2007) (Order Denying Interlocutory Review), the Commission rejected a party's argument that the burden of complying with an ALJ's discovery order rendered the circumstances of that discovery order "extraordinary." It held that pre-trial discovery orders, even burdensome ones, are almost never immediately appealable.

As an illustration of the defects in OCIE's motion to quash, the Commission is respectfully invited to review OCIE's response to Request No. 4 of the subpoena (July 20 Order at 2). That request seeks materials relating to a sweep discussed by a senior Commission official in a newspaper article.

OCIE has failed to show that it made a good faith effort to conduct a search for the records sought in Request No. 4, using methods which can be reasonably expected to produce the information sought. Neither the John Walsh Declaration of June 16, 2010, ¶¶ 31-34 (OCIE's Motion to Quash, Exhibit B), nor the Christopher Bruckman letter of July 1, 2010, at 2-3 & n.1 (Respondents' Opposition to OCIE's Motion to Quash, Exhibit B), demonstrate that OCIE has met the required standard. Cf. Aguirre v. SEC, 551 F. Supp. 2d 33, 60-62 (D.D.C. 2008). As a result, it is difficult to know which documents responsive to Request No. 4 are actually in OCIE's custody. Certification under Rule of Practice 400(c)(1) is not available under these circumstances.

OCIE's narrow understanding of "relevance" is at odds with Commission precedent. When it comes to admitting evidence at a Commission administrative hearing, the standard of relevance is very broad. See City of Anaheim, 54 S.E.C. 452, 454 & nn.5-7 (1999); Alessandrini & Co., 45 S.E.C. 399, 408 (1973); Charles P. Lawrence, 43 S.E.C. 607, 612-13 (1967). The standard of relevance is even broader when it comes to document subpoenas. Cf.

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<sup>5</sup> The General Litigation Group of the Office of General Counsel, which represents OCIE in this proceeding, has been delegated authority to process the Commission's docket of FOIA appeals. A Commission declaratory order finding merit to OCIE's Section 929I argument would provide a convenient basis for eliminating much of the backlog of aging FOIA appeals.

Fed. R. Civ. P. 26(b)(1). Under that Rule, relevance does not hinge on admissibility at trial. Rather, a court need only determine if the information sought “appears reasonably calculated to lead to the discovery of admissible evidence.”<sup>6</sup>

OCIE is well aware of this precedent. See Putnam Inv. Mgmt., LLC, 82 SEC Docket 2580 (Apr. 7, 2004). However, it has not even attempted to reconcile its narrow understanding of relevance with the Commission’s rulings in City of Anaheim, Alessandrini, and Lawrence, or with Federal Rule of Civil Procedure 26(b)(1). The documents sought by Respondents under Request No. 4 are “relevant.”

OCIE may not assert “blanket claims” of privilege, nor may it assert its claims of privilege seriatim. OCIE initially alleged that any documents responsive to Request No. 4 would be subject to “many” privileges, “including” the attorney-client and deliberative process privileges, and a so-called SEC examination privilege (OCIE’s Motion to Quash at 17). Ten days later, OCIE conceded that the deliberative process privilege would not apply to Request No. 4, but that “some” responsive documents “could be” subject to a law enforcement privilege (OCIE Supplemental Memorandum at 5, 7). OCIE’s most recent position was that, if the motion to quash was not granted, it “would like to preserve the right to raise” the attorney-client, law enforcement, and SEC examination privileges “on a document-by-document basis in the future” (OCIE Reply Brief at 13). This language raised a red flag.<sup>7</sup>

A “blanket claim” as to the applicability of a privilege does not satisfy the government’s burden of proof. See In re Grand Jury Subpoena, 831 F.2d 225, 226-27 (11th Cir. 1987); McCoo v. Denny’s Inc., 192 F.R.D. 675, 680 (D. Kan. 2000). Nor may the government assert its claims of privilege seriatim (Order of June 18, 2010, at 2) (collecting cases); cf. Gavin v. SEC, 2006 U.S. Dist. LEXIS 75,227, at \*23 (D. Minn. Oct. 13, 2006) (“The Court will not allow the SEC to circumvent its statutory obligations by ping-ponging from one [FOIA] exemption to another.”).

#### Motion for Stay

OCIE asserts that the July 20 Order imposes substantial obligations on it, and that a stay should be issued until the Commission has had an opportunity to review the Order. I reject OCIE’s analysis. The July 20 Order did not impose any obligations on OCIE; the

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<sup>6</sup> While the Federal Rules of Civil Procedure do not govern administrative proceedings before the Commission, they often provide helpful guidance in resolving issues not directly addressed by the Commission’s Rules of Practice. See Blizzard, 55 S.E.C. at 761-62 nn.17, 19.

<sup>7</sup> Cf. Gavin v. SEC, 2006 U.S. Dist. LEXIS 41,550, at \*6-7 (D. Minn. June 20, 2006) (“The SEC has continually and deliberately stalled in fulfilling its obligations to conduct a document-by-document review of material it seeks to withhold pursuant to [FOIA] Exemption 7(A). In doing so, the SEC has attempted to play by its own rules and disregard the law. The Court refuses to allow such maneuvering.”).

relevant portion of that Order merely denied parts of its motion to quash.<sup>8</sup> Under the terms of the June 1 subpoena, OCIE was required to produce responsive materials by June 16, 2010. The filing of the motion to quash did not automatically relieve OCIE of its obligation to produce responsive materials by the return date specified in the subpoena.<sup>9</sup> If OCIE wanted to delay its duty to produce responsive materials pending a ruling on the motion to quash, it should have filed a motion requesting that relief no later than June 16. Cf. In re Grand Jury Subpoena, 841 F.2d 230, 232 (8th Cir. 1988); In re Grand Jury 95-1, 59 F. Supp. 2d 1, 4-6 (D.D.C. 1996). In the alternative, it should have reached a stipulation with Respondents to postpone the return date. There is no evidence that OCIE did either.<sup>10</sup>

As a result, OCIE's July 27, 2010, motion to stay is untimely by nearly six weeks, and it addresses the wrong document. OCIE cannot now bootstrap itself into claiming "changed circumstances," *i.e.*, enactment of a new law, based on its own dilatory conduct in complying with a subpoena that it never properly sought to stay.

Respondents oppose OCIE's request for a stay. They argue that OCIE's intransigence in producing responsive documents is merely a device to delay the hearing, thereby allowing the Division more time to prepare its case. They do not want the hearing postponed beyond September 13, 2010. Respondents also note that the July 20 Order imposed a protective order to mitigate any legitimate concerns OCIE may have regarding the confidentiality of documents produced in response to the subpoena. OCIE's motion fails to explain why the protective order will not suffice.

The Division's "limited response" to OCIE's motion asserts that the Division has no position on OCIE's motion to quash or OCIE's motion for reconsideration. However, the Division claims that it would be substantially prejudiced in the presentation of its own case if Respondents file their witness and exhibit lists and the direct written testimony of their experts later than August 10, 2010.

The Division's first statement shows how far afield this matter is about to stray: the party that brought the case asks to be treated as a passive bystander while a non-party hijacks the proceeding to obtain a declaratory order on a tangential subject. The Division's second

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<sup>8</sup> The July 20 Order also adjusted the prehearing schedule. As a non-party, OCIE lacks standing to object to that part of the Order.

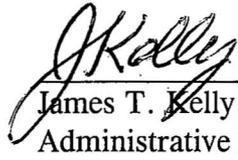
<sup>9</sup> Pursuant to 11 U.S.C. § 362(a), the filing of a petition in bankruptcy triggers an automatic stay. A motion to quash does not carry with it some form of automatic stay, making it the functional equivalent of a petition in bankruptcy.

<sup>10</sup> OCIE's approach contrasts with that of other non-parties who received subpoenas from Respondents. See, e.g., Stipulation between Respondents and Morgan Stanley & Co., filed May 27, 2010. Neither OCIE nor Respondents have informed me of any agreement to extend the return date of the subpoena beyond June 16, 2010. See Prehearing Conference of June 2, 2010, at transcript page 2.

statement is disingenuous. OCIE's dispute with Respondents has no bearing on the Division's ability to start and complete the presentation of its case-in-chief in a timely manner. It is worth remembering that the OIP seeks to impose cease-and-desist orders. The applicable statutes require the hearing to begin no earlier than thirty days and end no later than sixty days after the service date of the OIP. On April 16, 2010, I asked the Division for a written assurance that it was prepared to complete the presentation of its case-in-chief within that timeframe (i.e., by June 10, 2010). The Division provided that written assurance on April 21, 2010. The hypothetical concern the Division now presents involves an issue that may arise when Respondents present their defense, or that the Division may wish to address during its rebuttal case, once Respondents have rested their defense.<sup>11</sup> It has nothing to do with the Division's ability to complete the presentation of its case-in-chief. I agree with Respondents that a delay in starting the hearing beyond September 13, 2010, is unwarranted.

IT IS ORDERED THAT OCIE's motion for reconsideration, certification, and a stay is denied; and

IT IS FURTHER ORDERED THAT, on or before August 5, 2010, OCIE must clarify the record as to whether it reached a stipulation with Respondents whereby it was not required to turn over any responsive documents until after there was a ruling on its motion to quash. If OCIE reached such a stipulation, it shall supplement the record by providing evidence to that effect. If OCIE never sought, or did not reach, such a stipulation, it must so state.

  
James T. Kelly  
Administrative Law Judge

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<sup>11</sup> For example, if OCIE has not produced responsive documents before the Division rests its case-in-chief, the hearing could be continued at that juncture.