

UNITED STATES OF AMERICA  
Before the  
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDINGS RULINGS  
Release No. 730 / November 2, 2012

ADMINISTRATIVE PROCEEDING  
File No. 3-14862

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In the Matter of	:	
	:	ORDER ON EVIDENTIARY ISSUE
MIGUEL A. FERRER and	:	
CARLOS J. ORTIZ	:	

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The Securities and Exchange Commission (Commission) issued an Order Instituting Administrative and Cease-and-Desist Proceedings on May 1, 2012. I held nine days of hearing between October 9 and 19, 2012, in San Juan, Puerto Rico. The hearing scheduled to resume on October 29, 2012, in Washington, D.C., has been postponed because of Hurricane Sandy. At the hearing on October 11, 2012, the Division of Enforcement (Division) objected to a question posed to Carlos J. Ortiz (Ortiz) by his counsel as to whether the document that Ortiz used in making a presentation, and the underlying policy described in the document, were reviewed by UBS Financial Services Inc. of Puerto Rico's (UBS) Legal and Compliance Departments. Tr. 720. According to the Division:

During the investigation of this matter UBS asserted privilege and refused to allow us to question any witness about any matter involving - - I let this go a little bit yesterday - - involving their lawyer's review of documents or comments on any documents. And now Mr. Ortiz's counsel is attempting to introduce comments or reference to Legal's review of things. I think it's inappropriate. Tr. 720.

Ortiz's counsel responded that: (1) Ortiz has no power to assert or waive UBS's attorney-client privilege and has not asked UBS to do so; and (2) the evidence is not being used to show that UBS's Legal counsel approved the documents, but rather to show that Ortiz checked with Legal and Compliance to refute the Division's expected claim that Ortiz was negligent. Tr. 721-22. UBS is Ortiz's employer and is providing him with legal counsel. Tr. 725. I sustained the Division's motion to strike Ortiz's answer and sustained several similar objections during Ortiz and Miguel A. Ferrer's (Ferrer) testimony; I also allowed Respondents' counsel to make offers of proof of the material sought to be introduced. Tr. 732-33, 1486; 17 C.F.R. § 201.321. After some on-the-record discussion on October 15, 2012, it was decided that the Division should make a filing to support its position that during the investigation it was not allowed to question

witnesses about their communications with lawyers, and that Respondents would submit offers of proof. Tr. 1071-77.

On October 23, 2012, the Division sent me a Submission in Support of Its Objection to Respondents' Testimony on Consulting with Legal Department (Division Support), with Exhibits 1-3. Exhibit 1 contains about twenty transcript references involving four witnesses, including Ortiz, where the Division claims UBS lawyers would not let witnesses answer questions about discussions with lawyers. Exhibit 2 cites about fifteen situations where the Division, in response to UBS's regular warnings, told witnesses to exclude discussions with lawyers from their answers. Exhibit 3 contains about eight letters between the Division and UBS counsel addressing UBS's exercise of privilege.

The Division's position is that it "was prevented on several occasions from inquiring into matters involving discussions with lawyers," during the investigation; therefore, witnesses should not be allowed to testify "about consulting with UBS' legal department." Division Support at 1.

On October 26, 2012, Ortiz submitted his Offer of Proof Regarding Consultations with Counsel (Ortiz Offer of Proof) with Exhibits A-E. Ortiz argues that the Division Support Exhibits 1 and 2 are irrelevant and Division Support Exhibit 1 shows the Division was allowed to ask questions about non-privileged communications and UBS "merely objected to questions regarding the *substance* of witnesses' discussions with lawyers." Ortiz Offer of Proof at 3, 5. Ortiz maintains that he is not asserting a reliance-on-counsel defense but that he should have the opportunity to defend himself by showing that before he made any kind of statement or presentation concerning the securities that are the subject of this proceeding he had the underlying information checked by the Legal Department. Tr. 724.

On October 26, 2012, Ferrer submitted a Submission in Support of Offer of Proof and Joinder to Respondent Carlos J. Ortiz's Offer of Proof Regarding Consultations with Counsel (Ferrer Support), with Exhibits A and B. Ferrer cites to his investigative testimony on December 16, 2009, and James Price on February 23, 2010, as additional material supporting Ortiz's claim that the Division was permitted to explore the circumstances surrounding consultations that Ferrer and Ortiz had with counsel. Ferrer requests that his answer at the hearing on October 16, 2012, Tr. 125, lines 7-13, should be allowed to stand or, alternatively, that counsel's offer of proof at Tr. 125, lines 14-22, be accepted as evidence in the proceeding. Ferrer Support at 2.

### **Ruling**

Rule 320 of the Commission's Rules of Practice, which allows the admission of relevant, material, and not unduly repetitious evidence, does not prohibit unfairly prejudicial evidence. Other knowledgeable authorities take a different position. The Financial Industry Regulatory Authority (FINRA) provides for the exclusion of evidence that is "unduly prejudicial." FINRA Rule 9263(a). "Undue prejudice" is defined as "The harm resulting from a fact-trier's being exposed to evidence that is persuasive but inadmissible (such as evidence of prior criminal conduct) or that so arouses the emotions that calm and logical reasoning is abandoned." Black's Law Dictionary 1198 (7th ed. 1999). And, perhaps more significantly, Rule 401 of the Federal Rules of Evidence provides that:

The court may exclude relevant evidence if its probative value is substantially outweighed by a danger of one or more of the following: unfair prejudice, confusing the issues, misleading the jury, undue delay, wasting time, or needlessly presenting cumulative evidence.<sup>1</sup>

“Situations in this area call for balancing the probative value of and need for the evidence against the harm likely to result from its admission,” and “‘Unfair prejudice’ within its context means an undue tendency to suggest decision on an improper basis, commonly, though not necessarily, an emotional one.” Fed. R. Evid. 403, Advisory Committee Notes 2012, Revised Edition, West.

Respondents seek to use evidence of UBS’s Legal Department’s involvement or participation in the matters at issue as part of their defense. My concern is that if the Division was not allowed to explore the Legal Department’s involvement because of objections by UBS counsel based on an undue exercise of the attorney-client privilege during the investigation, it would be unduly prejudicial for Respondents to use as a defense what the Division was not allowed to investigate. The attorney-client privilege is the “client’s right to refuse to disclose and to prevent any other person from disclosing confidential communications between the client and the attorney.” Black’s Law Dictionary 1215 (7th ed. 1999).

Witnesses answered some questions about involvement with the Legal Department without objection during the investigation and the hearing. Division Support Exhibit 1, October 26, 2009, at Tr. 408-09; Ferrer Support at 1-2. There are other situations where there was simply dialogue over privilege. Division Support at Exhibit 1, June 22, 2010, Tr. 35-37. And there are situations where the attorney-client privilege was simply stated or appropriately invoked. Division Support Exhibit 1, October 8, 2009, Tr. 17; October 26, 2009, Tr. 239, 389; February 22, 2010, Tr. 74, 92. None of these situations are problematic.

The Division does, however, identify problems. For example, Ortiz interprets Division Support Exhibit 1, October 8, 2009, Tr. 190-92, as showing that “UBS expressly instructed Ortiz that he *could* testify to the fact that he conferred with persons in the Legal department, when he conferred, and with which lawyers.” Ortiz Offer of Proof at 4. I read the material as showing that UBS effectively squelched the line of interrogation. UBS only allowed Ortiz to describe what was discussed on a phone call “if there were no lawyers involved.” Tr. 190. After a lot of back and forth among UBS lawyers, they permitted the Division to ask “just who [was on that call], not what was said, just who.” Division Tr. 191-92. UBS established there were two lawyers on the phone call and the Division stopped asking questions. Tr. 192.

Division Support Exhibit 1, October 8, 2009, Tr. 206, lines 16-19, shows a brief discussion of a document that required consultation before it was used with the witness because it “has a lawyer[’s name] on it.” At Division Support Exhibit 1, October 26, 2009, Tr. 368, lines 2-11, the Division struck use of an exhibit because UBS was concerned that an e-mail used to

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<sup>1</sup> The Commission’s case law is that the Federal Rules of Evidence do not govern Commission proceedings, however, they are often used as a reference point.

question the witness was “possibly privileged and as Counsel would agree, if it was produced, it was an inadvertent production.” At Division Support Exhibit 1, February 22, 2010, Tr. 80, lines 22-24, a witness was cautioned “not to testify about the substance of what was discussed at that meeting,” because one of the participants was an attorney. At Division Support Exhibit 1, February 22, 2010, Tr. 84, lines 14-15, a witness was instructed not to answer anything related to the substance of a call “to the extent there were lawyers present on the call.”

At Division Support Exhibit 1, February 22, 2010, Tr. 87, line 2, UBS counsel advised the witness to exclude whatever he learned from conversations with UBS lawyers in answering the questions. After which, the witness’s response to the question of how he had come to learn of an inventory limit on the desk trading of the closed-end funds was “I don’t have a specific recollection of conversations or parsed conversations with whether an attorney was there or wasn’t there.” At Division Support Exhibit 1, February 22, 2010, Tr. 121, a witness was asked what caused his efforts at changing customer disclosure and was cut off and told not to testify by UBS counsel when he began his answer with “My legal colleagues had asked me –.” It appears that the same witness was not allowed to testify about conversations in which Ortiz participated because there may have been lawyers on the phone. Division Support Exhibit 1, February 22, 2010, Tr. 175-76. When asked if he was aware that investor conferences were held in Puerto Rico, a question without any confidential ramifications, the witness was warned that “Other than what you may have discussed with counsel.” Division Support Exhibit 1, February 22, 2010, Tr. 197.

My review of the Division Support shows that UBS counsel, on occasion, over-zealously invoked the attorney-client privilege to prevent the Division from exploring how and to what extent UBS’s Legal Department participated in the events at issue. While Ortiz and Ferrer are not making a technical reliance-on-counsel defense, they are attempting to defend themselves by showing that the UBS Legal Department reviewed and presumably approved materials. The Division has the burden of showing that the allegations in the OIP are true by a preponderance of the evidence. Steadman v. SEC, 450 U.S. 91, 101-02 (1981). The testimony that Respondents want in the record could have considerable probative weight. Since UBS prevented the Division from investigating the Legal Department’s involvement in these issues, the Division is unfairly prejudiced if Respondents are allowed to show they consulted UBS’s Legal Department and it allowed or approved use of the materials, which are the bases of the allegations.

On these facts, the unfairly prejudice standard is a valid consideration in determining admissibility as part of conducting a fair, impartial hearing. 17 C.F.R. §§ 201.111, .300. For these reasons, I sustain the Division’s objections to questions about clearance of material by UBS’s Legal Department. I will not use that material in making a decision. Respondents may make offers of proof so that the material is available in the event that others that may examine these issues later in the process may decide to use the material in making a decision. 17 C.F.R. § 201.321.

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Brenda P. Murray  
Chief Administrative Law Judge