UNITED STATES OF AMERICA
BEFORE THE
SECURITIES AND EXCHANGE COMMISSION

SEP 17 2012

ADMINISTRATIVE PROCEEDING
File No. 3-14862

In the Matter of

MIGUEL A. FERRER, and
CARLOS J. ORTIZ,

Respondents.

RESPONDENT MIGUEL A. FERRER'S PRE-HEARING MEMORANDUM

STROOCK & STROOCK & LAVAN LLP
180 Maiden Lane
New York, New York 10038
(212) 806-5400

Attorneys for Miguel A. Ferrer

September 14, 2012

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

CASES

PRELIMINARY STATEMENT

The Division of Enforcement's (the "Division") Order Instituting Administrative And Cease-And-Desist Proceedings (the "OIP") opens with the sweeping allegation that "[t]his case concerns the significant roles [Mr.] Ferrer and [Mr.] Ortiz played in ***misleading thousands of customers*** of UBS Financial Services Inc. of Puerto Rico ('UBS PR') into buying and holding hundreds of millions of dollars in UBS PR-affiliated, non-exchange-traded closed-end funds . . . in 2008 and 2009." OIP ¶ 1 (emphasis added). Yet, the Division abandoned this claim when, in response to Mr. Ferrer's Motion for More Definite Statement, it:

- Directed this Court to only one alleged "communication" by Mr. Ferrer to customers, namely a newspaper article in which he was quoted as making demonstrably true, general statements about the Puerto Rican financial market;
- Conceded that it is "not seeking to hold Mr. Ferrer liable for the statements of financial advisors to investors, but for his statements to financial advisors"; and
- Disavowed any obligation to prove that Mr. Ferrer's "statements [to the FAs] . . . reached a single investor."

Division of Enforcement's Response to Respondent Miguel A. Ferrer's Motion for More Definite Statement, at *11, *13 (June 8, 2012) (citing OIP ¶ 74) (hereinafter "Division's Response to Motion for More Definite Statement").

Rather than basing its case against Mr. Ferrer on any alleged misrepresentations made to UBS PR's customers, the Division is seeking to hold Mr. Ferrer liable almost entirely on the strength of eight short e-mails, which he sent internally to UBS PR's financial advisors (the "FAs"), in accordance with his long-held practice of occasionally sending the FAs brief, motivational communications. Thus, we are left with a case that, with a few insignificant exceptions, merely involves e-mails of the most conclusory nature sent from Mr. Ferrer and circulated only internally to the FAs and others at UBS PR. Importantly, none of the statements

contained in the handful of internal e-mails cited by the Division were factually incorrect or misleading, nor did they omit any facts necessary to make the statements made not misleading.

The e-mails on which the Division's charges are based essentially fall into one of three categories. The first category consists of three e-mails in which Mr. Ferrer referred the FAs to the historic performance of UBS PR's closed-end funds (the "CEFs" or the "Funds"), noting, for example, that the Funds had "superior performance" and "low volatility." Importantly, although UBS PR managed or co-managed 23 individual Funds, Mr. Ferrer's comments were all of a *general* nature and did not refer to the attributes of the shares of any of these Funds. The e-mails did not provide the FAs with the prices, yields, investment philosophies or, for that matter, any information regarding any individual Fund. Since the e-mails said almost nothing, it should be self-evident that they were never intended to provide, nor could they have been construed as providing, anything other than the most superficial, general, reminders about the Funds' past performance.

Moreover, to the extent Mr. Ferrer's statements could even be considered factual assertions, they were all true. Indeed, in his Opening Expert Report, the Respondents' expert, Dr. Erik R. Sirri, concludes that none of the statements about Fund performance made in these e-mails were, as the Division alleges, "misleading." Expert Report of Erik R. Sirri, at 36-37 (July 23, 2012).[1] Significantly, the Division's expert, Dr. Edward S. O'Neal, does not conclude that Mr. Ferrer's e-mails were incorrect or misleading in any regard, and Dr. O'Neal does not dispute, or even address, the accuracy of Dr. Sirri's analysis on this point.

---

[1] Dr. Sirri's Opening and Rebuttal Expert Reports are appended as Tab 1 and Tab 2 respectively to Respondent Carlos J. Ortiz's Pre-Hearing Submission (hereinafter "Ortiz Submission"). For the Court's convenience, copies of all other documents referenced herein, in addition to Dr. Sirri's expert reports, will be provided with the full set of market exhibits. Should the Court require a copy of any specific document in advance of the hearing, we will provide such copies upon request.

The second category consists of three brief e-mails in which Mr. Ferrer expressed to the FAs his personal opinion that shares of new Funds being issued or reissued by UBS PR would "provide good yields." Here again, there was a sound basis for Mr. Ferrer's opinion and in fact, consistent with his opinion, within the first eight months of their issuances, those Funds had tax-advantaged yields of 7.19% and 6.14%.

The final category consists of two e-mails which the Division itself fundamentally misrepresents to the Court. The first of these e-mails merely contained truisms, and the second accurately described a reduction in prices of the Fund shares and recommended how the FAs could use those price reductions to their customers' advantage. As with the other e-mails, neither was factually incorrect or misleading, nor did they omit any facts necessary to make them not misleading.

Although all of Mr. Ferrer's statements were true, were never remotely intended to resemble the disclosure of all relevant characteristics of the CEFs, and were too general and conclusory in nature to be deemed actionable, the Division has nevertheless sought to hold Mr. Ferrer liable because his e-mails allegedly omitted from them basic information about perceived liquidity issues, UBS PR's role in facilitating a secondary market for the Funds, and UBS PR's parent company's, UBS Financial Services, Inc. ("UBS FS"), decision to reduce UBS PR's inventory limits. But since Mr. Ferrer's e-mails say nothing about any of these subjects, they cannot possibly give rise to an obligation to make the additional disclosures the Division claims were omitted. The Division's theory further ignores the indisputable fact that Mr. Ferrer was not involved in making a market for or in otherwise pricing the Funds, in facilitating the secondary market, or in UBS FS's decision to reduce UBS PR's inventory levels. He neither participated in, directed, nor supervised those activities.

The OIP is also based on the faulty premise that the FAs (1) could have possibly construed the statements in Mr. Ferrer's e-mails as comprehensive disclosures of all material aspects of the CEFs; and (2) had their heads collectively "buried in the sand" when it came to knowing and understanding basic information about the Funds. This could not be further from the truth. The FAs were knowledgeable professionals who were well-versed in the unique nature of the Puerto Rican financial market and in the Funds, specifically. It was their job to know as much, if not more, about the Funds as Mr. Ferrer. Based on their own experience, training, and the information made available to them by UBS PR over the years, they were all keenly aware of the basic, regularly discussed facts that Mr. Ferrer is alleged to have omitted from his e-mails. Indeed, without an understanding of the characteristics of one or more of the 23 individual Funds (which the FAs regularly obtained from sources other than Mr. Ferrer or his e-mails), none of the FAs could have responsibly recommended the purchase or sale of any Fund to their customers.

Accordingly, and not surprisingly, UBS PR disclosed the allegedly omitted information about the Funds to the FAs in numerous written documents (including, for example, prospectuses, brochures, compliance presentations, and other internal guides), during presentations, in sales meetings, and in informal conversations with the FAs. Even assuming Mr. Ferrer's statements could possibly be actionable – and we submit they are not – he nevertheless had no duty to disclose to the FAs information that was already part of the "total mix" of information available to them. He did not have to tell the FAs what they already knew.

The Division's claim boils down to the rather extraordinary position that, because Mr. Ferrer said nothing of substance in any of his e-mails, those e-mails necessarily omitted material facts. However, if you say nothing about a specific subject, no additional facts regarding that subject are necessary to make the statements you have made not misleading. There is no theory,

or case law, that supports the imposition of liability under the securities laws urged by the Division. To the contrary, as we explain below, the e-mails sent by, or the newspaper quotes attributed to, Mr. Ferrer do not support a claim under the federal securities laws on any basis at all. For these and the other reasons discussed below, Mr. Ferrer respectfully requests that the OIP be dismissed.

STATEMENT OF FACTS

I. MR. FERRER'S BACKGROUND AND ROLE AT UBS PR

Mr. Ferrer, who is 74 years old, has worked in the securities industry in Puerto Rico for over 50 of those years. He was born in Ithaca, New York, and moved to Puerto Rico with his family at a young age. He returned to Ithaca for college and graduate school, receiving a bachelor's degree in Arts and a master's degree in Business Administration from Cornell University. Over the course of his long, distinguished career, Mr. Ferrer has played a significant role in the development of the securities industry in Puerto Rico while also serving on the boards of public corporations and nonprofits both in Puerto Rico and the United States. He is one of the recognized leaders in the Puerto Rican financial community. Mr. Ferrer is passionate about Puerto Rico and, in addition to his many charitable and philanthropic endeavors, he has served as a resource to Governors, the Legislature, and the Presidents of the Government Development Bank for Puerto Rico, Puerto Rico's equivalent to the Federal Reserve System.

Mr. Ferrer began his career as a financial advisor with Merrill Lynch in 1961 before moving to Eastman Dillon Union Securities (later, Blythe, Eastman Dillan and Co.), where he was a financial advisor and then a branch manager. In 1979, Blythe, Eastman Dillan and Co. merged with Paine Webber Jackson & Curtis Inc. (later, PaineWebber Incorporated of Puerto Rico), and, over the course of several decades, Mr. Ferrer rose to the title of President. In 2000,

PaineWebber Incorporated of Puerto Rico merged with UBS PR. Although organized as a corporation for tax purposes, functionally, and for support, legal, and compliance purposes, UBS PR operates as a regional office of its parent company, UBS FS, which is headquartered in Weehawken, New Jersey.

During the time period relevant to the Division's investigation, Mr. Ferrer served as the Chief Executive Officer of UBS PR, reporting to James Price, the head of UBS Wealth Management Advisor Group for the Americas, who was based in Weehawken, New Jersey. Mr. Ferrer had only one direct report, Carlos Ubiñas, the President and Chief Operating Officer of UBS PR. Mr. Ferrer's responsibilities as CEO included business planning for UBS PR, budgets, strategic business initiatives and general business results such as revenues and expenses. Mr. Ferrer was not in charge of any unit of UBS PR, and supervised only Mr. Ubiñas, and then, only in certain matters. Mr. Ferrer did not supervise, direct, or assist UBS PR's FAs, or their communications with investors. There were, in fact, multiple layers of management between the FAs and Mr. Ferrer, including the sales managers, the branch office managers (who were directly responsible for supervising the FAs), and senior officers Eugenio Belaval, the head of UBS PR's Wealth Management Division, and Mr. Ubiñas. Mr. Belaval also supervised UBS PR's Capital Markets Group, including Respondent Carlos Juan Ortiz, the Managing Director of the Capital Markets Group, who ran UBS PR's trading desk (the "Trading Desk").

The UBS Wealth Management Americas Risk Control Committee (the "RCC"), which was comprised of UBS FS executives located in Weehawken, New Jersey, was responsible for approving the inventory limits that UBS PR could maintain in connection with its best efforts to facilitate a market in, and provide extra liquidity for, the Funds. Mr. Ferrer was not a member of

the RCC; the RCC did not consult with Mr. Ferrer before making inventory decisions; and Mr. Ferrer had no role in implementing the RCC's decisions.

II. UBS PR'S CLOSED-END MUTUAL FUNDS

A. Regulatory Background And Advantages Of The Funds

In 1995, the Commonwealth of Puerto Rico enacted legislation providing special tax advantages for qualifying mutual funds that primarily invest in Puerto Rico securities. See, e.g., P.R. Laws Ann. tit. 10, § 666; P.R. Laws Ann. tit. 13, § 8659(a)(2). Shortly after the Commonwealth enacted this tax-advantaged legislation, Paine Webber Incorporated of Puerto Rico, UBS PR's predecessor company, and Banco Popular, Inc., jointly sponsored their first CEF: Puerto Rico Investors Tax Free Fund. From 1995 through 1999, UBS PR and Banco Popular jointly sponsored eight additional Funds. In addition to these nine jointly sponsored Funds, since 2001, UBS PR has sponsored 14 additional closed-end funds.[2]

All 23 of these Funds are regulated by the Office of the Commissioner of Financial Institutions of Puerto Rico ("OCFI"), which approved the issuance of each Fund. The OCFI also conducts regular examinations of UBS PR and its affiliated trust companies. As part of these examinations, the OCFI reviews the secondary market for the Funds and UBS PR's related disclosures. In addition, UBS PR must file with the OCFI Fund prospectuses, quarterly reports, and other customer documents.

The Funds are exempt from the registration requirements of the Investment Company Act of 1940. See 15 U.S.C. § 80a-6(a)(1); see also Puerto Rico Balanced Fund, Inc., SEC No-Action Letter, 1997 WL 206106 (Apr. 29, 1997); Puerto Rico Investors Tax-Free Fund, Inc., SEC No-

[2] Of those 14, one was jointly sponsored with Doral Securities, Inc./Doral Bank, one was jointly sponsored with R-G Premier Bank of Puerto Rico, and the rest are solely sponsored by UBS PR. Doral and R-G are no longer joint sponsors; their agreements terminated effective August 24, 2009 and June 15, 2009 respectively.

Action Letter, 1994 WL 570701 (Oct. 5, 1994). In addition, Fund shares offered to investors in Puerto Rico are not subject to the registration requirements of the federal securities laws.

Pursuant to the enabling legislation, investors who reside in Puerto Rico receive significantly advantageous income tax treatment if they purchase shares of the Funds. In addition, investors who both reside in and were born in Puerto Rico also receive advantageous estate tax treatment.[3] The Funds have enormously benefitted the Puerto Rican economy and have been highly successful investments for thousands of Puerto Rican residents.

B. Characteristics Of The Funds

Although each of UBS PR's 23 separate CEFs were established as closed-end funds, many of them have different attributes, and their yields, prices, dividends, and the inventory levels, if any, maintained by the Trading Desk vary from Fund-to-Fund. Thus, some of the Funds invest their assets in securities that are rated investment grade, whereas other Funds invest their assets in AAA securities. In some Funds, a portion of the dividends are subject to a 10% withholding tax, while, for other Funds, the dividends are 100% tax free. Some of the Funds are perpetual, while others are target maturity funds with a specific redemption date. Since each of the Funds were formed at different times, the securities held by each Fund differ based on, among other things, the securities available at the time the Funds had cash available to invest, the prevailing interest rates, and the amounts available to be invested. In addition, some of the Funds allow investors to reinvest their dividends back into the Funds.[4]

---

[3] For a full recitation of the applicable tax advantages, the Court is respectfully referred to the affidavit of Fernando Goyco, annexed as Exhibit 24 to the Rebuttal Expert Report of Erik R. Sirri, attached as Tab 2 to the Ortiz Submission. Mr. Goyco is a founding partner of Adsuar Muñiz Goyco Seda & Pérez-Ochoa, P.S.C., a full service law firm with offices located in San Juan, Puerto Rico, and has 36 years of experience in Puerto Rico corporate tax matters.

[4] This is commonly referred to as the Dividend Reinvestment Program (the "DRIP"). Dividends for the Funds are issued monthly at the Funds' net asset value ("NAV"). Funds that have a DRIP give investors the option to receive their monthly dividends in additional shares of the Funds, rather than in cash. If the Funds are trading at

C. Management Of The Funds

UBS Asset Managers of Puerto Rico ("UBS Asset Managers") manages or co-manages each of UBS PR's 23 CEFs. As manager or co-manager of the Funds, UBS Asset Managers "provide[s] a complete and continuous investment program for the Fund[s] and make[s] investment decisions and places orders to buy, sell or hold particular securities and other investments." Puerto Rico Fixed Income Fund V, Inc., Prospectus Supplement to Prospectus dated May 29, 2007, at 33 (April 28, 2008). UBS Asset Managers is a division of UBS Trust Company of Puerto Rico ("UBS Trust Company"), which, itself, is an affiliate of UBS PR.[5] During the relevant time periods, Mr. Ferrer served as the CEO of UBS Trust Company, and Eugenio Belaval was the President. Although Mr. Ferrer was the CEO of UBS Trust Company and served as one of the several directors of the 23 CEFs, he, like the other directors, was not involved in the day-to-day investment decisions made by the managers.

D. Inherent Constraints Of The Market For Puerto Rico Tax-Advantaged Closed-End Funds

UBS PR markets the Funds as long-term investments. The pool of potential investors is necessarily limited to individuals who reside in Puerto Rico,[6] and, even then, only to those residents who have sufficient income available to make such investments. Moreover, the Funds are not traded on any exchange, and, unlike open-ended funds, the individual CEFs each offer a set number of shares for purchase through an Initial Public Offering, and, thereafter can only be

---

premiums to NAV, investors participating in the DRIP are able to sell the reinvested dividend shares they received at NAV on the secondary market, just as they can sell any other shares, and earn additional returns on their investments.

[5] Leslie Highley, Jr., is the Managing Director of UBS Asset Managers, and Ricardo Ramos is the Executive Director.

[6] Prior to investing in the Funds, all investors must provide a letter confirming their Puerto Rican residency, and, if their residency status changes, they must liquidate their shares in the Funds as soon as it is economically feasible to do so.

purchased in the secondary market from shareholders wishing to sell. Unlike mutual funds in the United States, which often have multiple brokerage firms acting as market makers, UBS PR serves as the predominant liquidity provider for the CEFs' secondary market, even for those Funds in which it co-manages. Accordingly, for these and other reasons, the market for Fund shares may be less liquid than shares of exchange-traded mutual funds or mutual funds for which there are a variety of market makers. UBS PR has, for years, disclosed this information in, among other materials, the individual prospectuses for the Funds: "***If at any time UBS Puerto Rico (and other dealers, if any) ceases to maintain a market, the Shares will become illiquid until a market is reestablished.***" Puerto Rico Fixed Income Fund IV, Inc., Twelfth Prospectus Supplement to Prospectus dated March 29, 2005, at 8 (Oct. 31, 2005) (emphasis added).

E. UBS PR's Role In Facilitating A Secondary Market

Since the issuance of the first Fund, and solely as a service to its customers, UBS PR's Capital Markets Group has operated the Trading Desk to facilitate a secondary market in the Funds on a best efforts basis. Carlos Rosado, a director in the Capital Markets Group, is charged with pricing the Funds and maintaining an orderly market by executing trades in the Funds. Mr. Ortiz supervises Mr. Rosado. The Trading Desk provides liquidity to UBS PR's customers both by executing "riskless principal" transactions and by maintaining its own inventory account, from which the Trading Desk is able to both buy and sell shares of the Funds. Mr. Ferrer did not supervise the Trading Desk, Mr. Ortiz, or Mr. Rosado, and was not involved in the Trading Desk's pricing of, or maintaining a market in, the CEFs.

The Trading Desk did not have the authority to set its own inventory levels. Rather, those levels were set by the RCC, a UBS FS committee based in Weehawken, New Jersey. Starting in March 2009, as part of a global risk assessment, the RCC began re-evaluating the

Trading Desk's inventory levels. At all relevant times prior to March 19, 2009, the RCC had permitted UBS PR to maintain an inventory limit of approximately $30 million. From time to time, the Trading Desk required increased limits to supply additional liquidity to the markets and would request and receive approval from the RCC to temporarily increase its inventory limit. As of March 2009, the $30 million limit had been temporarily extended to $50 million. On March 19, 2009, Mr. Ortiz requested an additional temporary increase to $55 million. The RCC declined Mr. Ortiz's request and instead directed the Trading Desk to enforce the standing $30 million limit. Then, on May 22, 2009, the RCC instructed the Trading Desk to further reduce its inventory to $12 million.

It is ironic that the Division would charge Mr. Ferrer with having failed to disclose to the FAs that the RCC had directed UBS PR's Trading Desk to reduce its inventory when Mr. Ferrer was not a member of the RCC, did not participate in the decisions made by the RCC, was not consulted by the RCC (and was only informed of the decisions after the fact), and had no role in implementing the RCC's directives to the Trading Desk. To the contrary, from the beginning, Mr. Ferrer disagreed with the RCC's decisions, supported and joined his colleagues in objecting, and ultimately wrote to Mr. Price, his supervisor and a member of the RCC, to inform him of the negative impact of the decision directing the Trading Desk to reduce its inventory to $12 million, and to request that the higher inventory limits be restored.

Mr. Ferrer neither engaged in a primary violation of the federal securities laws as it pertains to the decision of the RCC to reduce the inventory limits of UBS PR (or otherwise), nor did he assist, much less substantially assist, the supposed violations that the Division argues emanated from the decision of the RCC. He simply had no role in the RCC's decisions, or determining what, if any, disclosures were required following those decisions. That was the

responsibility of the RCC with the assistance of UBS FS's Legal and Compliance Department ("Legal and Compliance"), which, like the RCC, is based in Weehawken, New Jersey.

III. FA KNOWLEDGE OF MATERIAL ASPECTS OF THE FUNDS

The Funds' individual attributes and their inherent market constraints is information well-known, or available, to the FAs. Indeed, before an FA can even recommend an individual Fund to a customer, he or she must possess sufficient information regarding the specific nature of the Fund, its share price, yield, performance, and other characteristics of the Fund necessary to assess whether a particular Fund is a suitable investment for a customer. See, e.g., FINRA Rule 2310 ("In recommending to a customer the purchase, sale or exchange of any security, a member shall have reasonable grounds for believing that the recommendation is suitable for such customer upon the basis of the facts, if any, disclosed by such customer as to his other security holdings and as to his financial situation and needs,") superseded by FINRA Rule 2111.

A. Written Disclosures[7]

To ensure that the FAs were properly educated about each Fund and the advantages, and constraints, of the Funds, UBS PR provided abundant information to them in, among other sources, prospectuses, brochures, reports, and other information guides.[8] Specifically, at all relevant times, the prospectuses for the 23 CEFs contained a disclosure either identical or substantially similar to the following:

> The Shares are a new issue of securities. Therefore, prior to this offering there has been no market for the Shares. UBS Puerto Rico currently intends to maintain a market in the Shares commencing after the final closing of the initial public offering of the Shares, although it is not obligated to do so. ***No assurance can be given***

---

[7] This is not an exhaustive description of the written disclosures about the Funds made available to the FAs.

[8] Mr. Ferrer was not responsible for preparing or reviewing any of these documents. He was, however, certainly aware that such information was made available to the FAs.

> ***as to the liquidity of, or the trading market for, the Shares as a result of any activities undertaken by UBS Puerto Rico.*** Such purchases and sales, if commenced, may be discontinued at any time. ***If at any time UBS Puerto Rico (and other dealers, if any) ceases to maintain a market, the Shares will become illiquid until a market is reestablished.***

Puerto Rico Fixed Income Fund IV, Inc., supra at 8 (emphasis added). In addition, the prospectuses also disclosed that "the Shares may not be suitable to all investors as they are ***designed primarily for long-term investors***, and investors in the Shares should not view the Fund ***as a vehicle for trading purposes.***" Id. (emphasis added).

It is well-known to the FAs that the liquidity of one or more of the Funds will vary from time to time. Thus, in a May 15, 2006 memorandum distributed to the FAs and other recipients, Mr. Ortiz and Mr. Belaval discussed a market imbalance that occurred almost two years ***before*** the period focused on by the Division: "As many of you are already aware, as a result of various factors impacting the local market and products, UBS has received an increase in sale orders for local products, particularly the [CEFs]. This has, at times, resulted in more sellers than buyers and thus, ***limited liquidity.***" Memorandum entitled "Trading of Puerto Rico Closed-End Investment Funds," at 1 (May 15, 2006) (emphasis added). In the same memorandum, Mr. Ortiz and Mr. Belaval advised the FAs that "[d]uring ***any periods of limited liquidity***, it is important that Financial Advisors and Client Service Associates disclose to clients ***the possibility that there may be a delay in executing a sales order***, and that the execution price may differ from the current price shown by the Trading Desk." Id. (emphasis added).

Similarly, in February 2008, UBS PR distributed to all of the FAs the "UBS Puerto Rico Family of Funds" brochure (the "Family of Funds Brochure"), which was intended to be used by

the FAs during their communications with customers and prospective customers.[9] The Family of Funds Brochure, like the prospectuses, fully disclosed the potential for periods of illiquidity with the CEFs, as well as the role UBS PR played in facilitating the secondary market:

> While UBS Financial Services Incorporated of Puerto Rico currently intends to maintain a market in the shares, and has since 1995, it is under no obligation to do so. ***Therefore, there may be occasions when you may be unable to sell your fund shares or may be able to sell them at a loss or at times at a significant loss.***

(Emphasis added.) Moreover, the Family of Funds Brochure disclosed that: (1) UBS PR "is the principal secondary market dealer for the UBS Puerto Rico closed-end funds"; (2) "Shares of the UBS Puerto Rico funds do not trade on any exchanges"; and (3) "The fund company is not required to purchase shares of a closed-end fund from clients seeking to sell their shares."

In advance of new issuances, UBS PR also distributed to the FAs, for their own internal use, Question and Answer Guides for some of the individual CEFs, which likewise contained similar disclosures. The "Puerto Rico Fixed Income Fund V, Inc.: Question & Answer Guide," for example, contained the following disclosure:

> **Liquidity and Restrictions on the Transfer of Shares:** . . . The Shares are a new issue of securities and therefore prior to this offering there has been no market for the Shares. No assurance can be given as to the liquidity of, or the trading market for, the Shares as a result of any activities undertaken by the Underwriter.

This Guide was distributed to the FAs on May 1, 2007, shortly before the Fund was issued. UBS PR also distributed similar Guides to the FAs on September 17, 2008, in advance of the issuance of Puerto Rico Fixed Income Fund VI ("PRFIF VI") and the reissuance of Puerto Rico AAA

---

[9] Specifically, the Family of Funds Brochure was developed, after consultation with the OCFI, to provide concise disclosures of the relevant risk factors associated with the CEFs. It was intended to compliment the detailed disclosures contained in the prospectuses.

Portfolio Bond Fund II ("AAA Bond Fund II"). Both Guides contained the same or similar disclosures regarding liquidity and UBS PR's role in the secondary market.[10]

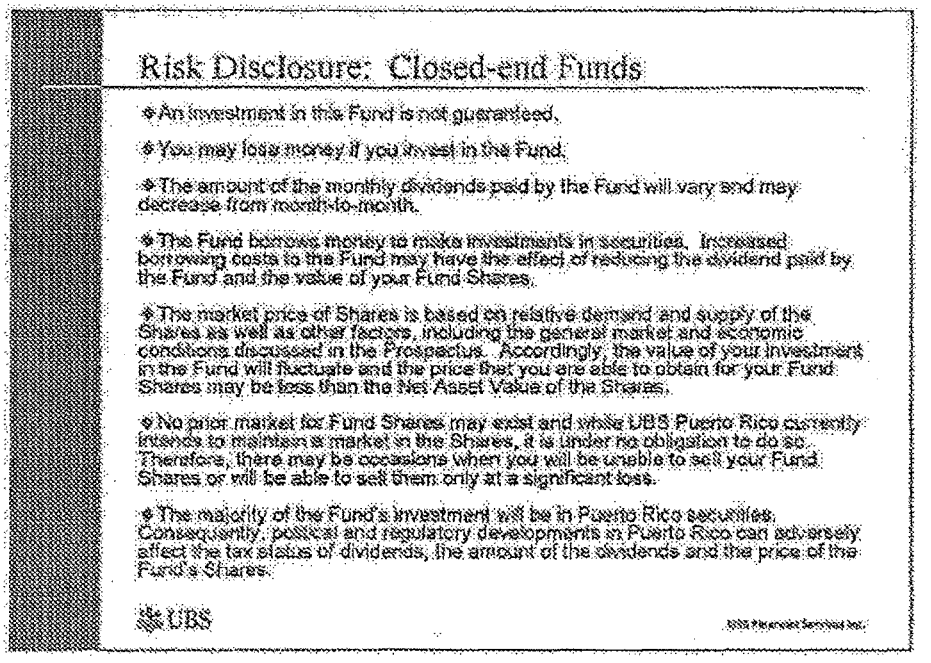
B. Presentations and Sales Meetings

In addition to the foregoing sources of information, on June 19, 2007, Legal and Compliance provided compliance training to the FAs and the branch office managers in UBS PR, which not only discussed the FAs obligations generally, but specifically went over their disclosure obligations for the CEFs (the "June 19, 2007 Compliance Presentation"). Thus, almost one year ***before*** the period focused on by the Division, Legal and Compliance informed the FAs, among other things:

- "An FA should have a reasonable belief that his or her recommendation is suitable in light of the facts the client disclosed."
- "Ask yourself before each transaction: Is this security or product right for this client?"
- "Provide the client with sufficient investment alternatives and information, including risks and benefits, to allow the client to make an informed decision."
- "As an FA you MUST have a 'reasonable basis' for believing the product you are recommending is suitable."
- One "relevant" factor to consider when making a suitability determination is the "[l]iquidity needs" of a customer.

June 19, 2007 Compliance Presentation, at 3, 5. The June 19, 2007 Compliance Presentation also addressed specific disclosures that should be made to customers and prospective customers who would be investing in the CEFs:

[10] The Guides also provided the FAs with information about the specific Fund, such as, the Fund's investment policies, the Fund's use of leverage, and ways in which the Fund differed from UBS PR's other Funds.



Risk Disclosure: Closed-end Funds

- An investment in this Fund is not guaranteed.
- You may lose money if you invest in the Fund.
- The amount of the monthly dividends paid by the Fund will vary and may decrease from month-to-month.
- The Fund borrows money to make investments in securities. Increased borrowing costs to the Fund may have the effect of reducing the dividend paid by the Fund and the value of your Fund Shares.
- The market price of Shares is based on relative demand and supply of the Shares as well as other factors, including the general market and economic conditions discussed in the Prospectus. Accordingly, the value of your investment in the Fund will fluctuate and the price that you are able to obtain for your Fund Shares may be less than the Net Asset Value of the Shares.
- No prior market for Fund Shares may exist and while UBS Puerto Rico currently intends to maintain a market in the Shares, it is under no obligation to do so. Therefore, there may be occasions when you will be unable to sell your Fund Shares or will be able to sell them only at a significant loss.
- The majority of the Fund's investment will be in Puerto Rico securities. Consequently, political and regulatory developments in Puerto Rico can adversely affect the tax status of dividends, the amount of the dividends and the price of the Fund's Shares.

UBS

Id. at 13.

Six days after the presentation, Frank Pluchino, the Executive Director of UBS FS's Compliance Department, e-mailed a copy of the June 19, 2007 Compliance Presentation to the FAs. In his cover e-mail, he reiterated some of the same disclosures quoted above. He, for example, again reminded the FAs:

- "Before you solicit a client, you should consider[, among other things,] . . . [whether] the security or product is right for this client."
- "[Y]ou should . . . [p]rovide the client with sufficient investment alternatives and information, including risks and benefits, to allow the client to make an informed decision."
- "As a Financial Advisor you must have a 'reasonable' basis for believing the product you are recommending is suitable."
- One "relevant" piece of information to consider is "the clients . . . liquidity needs."

E-Mail from Mr. Pluchino to DL-Puerto Rico Financial Advisors, dated June 25, 2007.

Mr. Pluchino also noted that "[m]ore detailed information is available in the prospectus, which clients can obtain from [UBS PR's] public website." See also E-Mail from Javier Vila to DL-Puerto Rico et al., dated March 16, 2009 and Slides 13 and 14 of attached PowerPoint Presentation (circulating presentation entitled "UBS Puerto Rico Individual Retirement Account (IRA)," which reiterated some of the same disclosure obligations).

C. The FAs Knew About The Fall 2008 Market Imbalance

Consistent with the direction of Legal and Compliance that the FAs should disclose to investors that "there may be occasions when you will be unable to sell your Fund Shares or will be able to sell them only at a significant loss," it was no secret that during the Fall of 2008 and the Winter of 2009, in the midst of a global financial crisis, certain Funds experienced periods of market imbalance, in which it took longer than usual for the Trading Desk to execute sale orders. And, contrary to the Division's suggestion in the OIP, this was not the first time such imbalances existed. Rather, as the FAs well knew, the market for individual Funds would, at times, fluctuate based on the relative supply and demand for the specific Funds. See, e.g., "Trading of Puerto Rico Closed-End Investment Funds," supra at 1 (discussing "limited liquidity" for shares of CEFs in May 2006).

Indeed, several of the e-mails Mr. Ferrer sent to the FAs during this period, which are discussed in more detail below, openly acknowledged these very same issues. See, e.g., E-Mail from Mr. Ferrer to DL-Puerto Rico Financial Advisors, dated October 8, 2008 (noting: "When there are more sellers and few buyers, prices of all securities decrease. Such is the situation with some of our Funds at times . . . ."). Similarly, Mr. Ferrer also discussed with others at UBS PR

the concerns expressed by the FAs about market imbalances in certain Funds. The possibility and fact of market imbalances was not a secret.[11]

IV. MR. FERRER'S COMMUNICATIONS WITH THE FAs

A. Mr. Ferrer's Historic Practice Of Communicating With The FAs

Since at least the time Mr. Ferrer became President of PaineWebber Incorporated of Puerto Rico, it has been his practice to send memoranda and e-mails to the FAs to motivate them and to notify them of certain investment opportunities. At all times, Mr. Ferrer was writing to a sophisticated audience of FAs, who, as Mr. Ferrer rightly understood, were knowledgeable about the instruments involved and had available to them all relevant information. None of Mr. Ferrer's general communications with the FAs could ever be considered a disclosure document, a "script" for the FAs to use when discussing investments with their customers, or a recommendation on the part of Mr. Ferrer for a particular client to invest in a particular security.

Although the Division has seized on a handful of these e-mails, written between September 2008 and August 2009, the FAs had been receiving these types of communications from Mr. Ferrer for years and could not have misinterpreted their intended purpose. A sampling of some of Mr. Ferrer's pre-September 2008 communications with the FAs vividly demonstrates this point. For example, in a memorandum he sent to the FAs on May 20, 2005, Mr. Ferrer provided words of encouragement to the FAs following Moody's decision to downgrade Puerto Rico's general obligation bond: "Maybe I am the ultimate dreamer, but I am bullish on Puerto Rico, precisely because this bad news will cause a better future." Similarly, on August, 26, 2005, in a clear attempt to motivate the sales force, Mr. Ferrer wrote:

---

[11] The FAs were also aware of the RCC's directive to the Trading Desk to reduce its inventory. See Ortiz Submission, supra at Section IV(B) (discussing, among other things, the daily inventory sheets and the "Good-til-Cancelled" book (the "GTC Book")).

> I ask you now to be the defining organization against which others will be measured worldwide. In accepting this further challenge, we accept being the standard against which excellence in the financial world will be measured. This will require great effort from all of us to deliver excellent products and services in a way that is client friendly.[12]

Prior to September 2008, Mr. Ferrer also wrote to the FAs, in the most general and conclusory fashion, about the CEFs. On November 1, 2005, for example, without discussing any individual Fund, Mr. Ferrer underscored to the FAs that "when you buy Fund shares, you are letting proven professionals take care of investing these at the appropriate time, in the appropriate vehicles." And then, on March 10, 2008, again speaking in the most conclusory manner, Mr. Ferrer sent an e-mail to the FAs, in which he stated: "[Our Funds] present[] good opportunities for clients facing reduced interest rates in other investment vehicles; such as CDs and who understand the pros and cons of Funds. And, certainly our new Fund should be considered."

The purpose of these communications is self-evident. They are reminders, "wake up" calls, motivational pieces, and efforts by Mr. Ferrer to share his opinions with the FAs. They were not intended to be, nor could they ever be construed as, a recitation of all, or even of any, of the material facts that the FAs must know in order to recommend any securities to their customers. Mr. Ferrer's statements did not supply the FAs with sufficient information to even

---

[12] In the same vein, on September 23, 2005, Mr. Ferrer wrote to the FAs:

> Great brands achieve a distinct quality . . . . To maintain this distinctive benefit we want continue to deliver excellent products and services to our clients, in the context of a client friendly attitude. . . . Those many [clients] that cannot properly benefit from the full breadth of our resources must be attended to with the same care and shown the particular services and products they can benefit from and which distinguish UBS from the other financial firms in the market place.

discuss the securities with their customers, and certainly do not give rise to an inference that they were intended to deceive or mislead the FAs.

In the OIP, the Division makes no mention of Mr. Ferrer's practice to send these sorts of communications to the FAs since long before the Fall of 2008. Nor does the OIP refer to other communications of a similar category sent by Mr. Ferrer during 2008-2009. Thus, although Mr. Ferrer had no obligation to tell the FAs what they already knew or to instruct them on what their obligations were to their clients, in an e-mail he sent to the FAs on October 9, 2008 (not included in the OIP), he reminded them of their responsibility: "***The Fund that fits the particular needs of each client is the decision of each Financial Advisor to make. We provide the varied vehicles for each Financial Advisor to choose among.***"[13]

While we believe that this Court need not look beyond the four corners of the e-mails set forth in the OIP to reach the conclusion that not one of them violates the federal securities laws, particularly when viewed against this backdrop of the types of communications Mr. Ferrer has sent to the FAs over the years, we respectfully submit that one cannot help but seriously question why Mr. Ferrer has been charged in this case.

B. Mr. Ferrer's E-Mails About The Funds' Performance And Volatility

As noted above, the e-mails cited in the OIP fall into three categories. The three e-mails in the first category simply contained general statements about the historic performance of the Funds and suggested the FAs consider the Funds as investment opportunities for their clients. Mr. Ferrer did not send these e-mails to any customers, nor did he have any expectation that the

[13] Similarly, on May 6, 2009, in another e-mail omitted from the OIP, Mr. Ferrer underscored for the FAs that "Our, your challenge is to show more appropriate investments to those investors whose particular needs and risk profiles are suited to our Funds and Puerto Rico bonds."

FAs would parrot his words to customers without making full disclosures about the Funds.

Thus, on September 18, 2008, Mr. Ferrer wrote:

> In the midst of all the turmoil, I note the superior performance of our local Funds. They seem to be weathering the "Wall Street Storm" in a pretty good fashion, which gives me great comfort.
>
> Thus, you should look at these for clients searching for low volatility and respectable returns.

OIP ¶ 40. Mr. Ferrer sent this e-mail to the FAs as an obvious response to Lehman Brothers filing for bankruptcy on September 15, 2008 and to Bank of America announcing its plan to purchase Merrill Lynch on September 14, 2008. See, e.g., Andrew R. Sorkin, Lehman Files For Bankruptcy; Merrill Is Sold, N.Y. Times, Sept. 15, 2008.

Similarly, on September 30, 2008, Mr. Ferrer sent another e-mail to the FAs in which he stated:

> Did you note our Funds did not budge in the midst of all the bad news yesterday? Their low volatility and low coefficient to equities are a great reason to consider them as a timely investment. Plus their returns are superior! Need I say more?

OIP ¶ 40. Mr. Ferrer sent this e-mail one day after the United States House of Representatives rejected a $700 billion financial bailout plan, which caused the stock market to crash (the Dow Jones industrial average dropped 778 points, or nearly 7%). See, e.g., Vikas Bajaj & Michael M. Grynbaum, For Stocks, Worst Single-Day Drop In Two Decades, N.Y. Times, Sept. 29, 2008.

In the last e-mail of this category, dated October 9, 2008, Mr. Ferrer stated as follows:

> It seems the bloodletting has continued way beyond the anticipation of the "best minds" in the different Central Banks, the Fed and US Treasury Department.
>
> The negative psychology is now a world-wide contagion and the investors have become, if not irrational, at least immune to the massive salvage efforts being conducted.

> One thing is definite; at some point the situation will come to a stand still and begin its healing process, leading to the improvement of market prices.
>
> I trust we will feel the progress soon, rather than later.
>
> I am confident in a couple year's time we will remember this historic period, not only for enormous losses, but also for the incredible opportunities it offered.
>
> It is important we all keep in mind that local investors have side stepped the wrath of the marketplace and have been enjoying superior returns from our Funds.
>
> So we have sustained some wounds, but remain totally able to go to the next rounds, hopefully good rounds.

OIP ¶ 40.

It is self-evident that not one of these e-mails could ever be construed as providing any level of detail regarding any one of UBS PR's 23 individual CEFs. The information contained in the e-mails is all high-level and general in nature. Mr. Ferrer was merely reminding the FAs that, even in times of economic turmoil, they should remember that, for certain customers, the Funds were still viable investment opportunities. No FA could have properly recommended any of the 23 CEFs to their clients based on anything contained in Mr. Ferrer's e-mails. Given the general, conclusory, and truthful nature of his statements and opinions, Mr. Ferrer did not have an obligation to say anything further.

It bears repeating that the affirmative statements made by Mr. Ferrer regarding the performance of the Funds were, in all instances, truthful and accurate. Mr. Ferrer based his statements about the Funds' performance and volatility on, among other sources, regular reports produced by the Funds' managers. After reviewing the relevant data available to Mr. Ferrer at the time he sent the e-mails, Respondents' expert, Dr. Sirri, concluded that the data is "consistent with Mr. Ferrer's comments [about the Funds' superior performance and low volatility] and

inconsistent with the SEC's allegations that Mr. Ferrer's comments regarding the Funds were misleading." Expert Report of Erik R. Sirri, at 6.

According to Dr. Sirri, "over the one- and three-year periods prior to the dates the statements were made . . . the median returns of the Funds exceeded the index returns." Specifically, the Funds provided a median tax-advantaged annualized return of 12.3% in the year prior to Mr. Ferrer's e-mails and a median tax-advantaged annualized return of 5.1% over the three years preceding Mr. Ferrer's e-mails. Id. at Ex. 16. All of this, of course, occurred in the throes of an economic crisis. Against any standard of measurement, these returns were, as Mr. Ferrer put it, "superior."[14]

Significantly, the Division does not claim in its OIP that any of Mr. Ferrer's statements were false, and the Division's own expert, Dr. Edward S. O'Neal, neither concluded that Mr. Ferrer's e-mails were misleading, nor did he dispute any of Dr. Sirri's findings regarding the performance of the Funds or the accuracy of Mr. Ferrer's statements. Dr. O'Neal did not touch the subject, although the data was readily available to him.

In addition, although we fundamentally disagree with the Division's assertion that these e-mails somehow gave rise to an obligation on the part of Mr. Ferrer to "disclose to the financial advisors the liquidity problems the CEFs were having because of weakening demand, or that the high, stable CEF prices were being maintained only because UBS PR was buying millions worth of CEF shares into its inventory," OIP ¶ 41, information concerning the liquidity of the CEFs was well-known to the FAs, was consistent with the disclosures in every prospectus, Fund

[14] Dr. Sirri also confirmed the accuracy of Mr. Ferrer's statements regarding the Funds' "low volatility." After reviewing the data, Dr. Sirri concluded that, consistent with Mr. Ferrer's statements, "the volatility of the Funds was relatively low." Expert Report of Erik R. Sirri, at 37 & Ex. 17 annexed thereto.

brochure, and compliance training they had received from UBS PR, and was openly discussed with, and among, the FAs.[15]

C. Mr. Ferrer's E-Mails Regarding The Issuances Of New Fund Shares

In the second group of e-mails to the FAs cited by the Division, Mr. Ferrer discussed UBS PR's upcoming issue of PRFIF VI and the reissue of AAA Bond Fund II. Specifically, Mr. Ferrer wrote the following three e-mails to the FAs:

> **September 10, 2008:**
>
> Some of you rejoiced upon hearing new funds are available, happy to be able to better serve your clients while enjoying good gross.
>
> Others were concerned, because of their worry secondary market activity would be reduced and prices affected in old Funds. Not to worry!!!
>
> No one should feel discomfort for our opening new Fund opportunities; because the local marketplace in a very rapid consolidation and we are positioning ourselves to be a beneficiary of this situation.
>
> We have put in place a growth strategy in a consolidating market! It is bold, but it is right.
>
> This move should have little direct effect on secondary market activity, and if any, a positive one.
>
> Those that have the agility will find plenty of swaps between old Funds.
>
> For new money, the two newly launched Funds present a unique opportunity to offer very competitive yields with no premiums, a way to tap on the millions of dollars seeking a new home; better yields.
>
> I suggest you all look at the opportunity seriously and not let past issues prevent you from a killer last quarter.

OIP ¶ 43.

---

[15] For a discussion about how the Division incorrectly assumes that there were liquidity problems in the CEFs during this period, the Court is respectfully referred to Section II of the Ortiz Submission.

> **September 23, 2008**
>
> There is a certain comfort in owning our Funds; low volatility, attractive returns (in fact very attractive).
>
> Conclusion: Worth considering!!!
>
> Look at Fund VI . . .; it will presently provide good yields.

OIP ¶ 46.

> **September 24, 2008**
>
> It is our expectation that due to particular and favorable circumstances, Fund VI will promptly show attractive returns.
>
> I urge you to focus your efforts in what we expect will have stellar performance.

Id.

As is evident from the e-mails themselves, these statements were simply expressions of Mr. Ferrer's opinions. They were not guarantees, nor could they reasonably be construed by the FAs as guarantees, and Mr. Ferrer had a reasonable basis for expressing these opinions. Specifically, he knew there were high yielding investments available for purchase by the new Funds at the time and that interest rates had reverted to what might have been an all time low, which would have allowed the Funds' managers to use cheap leverage to purchase additional securities and increase the yields. Based on this information, which was all public and available to the FAs, Mr. Ferrer expressed his opinion that the new Funds' yields would be attractive. Consistent with Mr. Ferrer's opinions, within the first eight months of their issuance, PRFIF VI had a yield of 7.19% and AAA Bond Fund II had a yield of 6.14%. In addition, because PRFIF VI was sold at NAV during its initial public offering, investors would not have to pay a premium over NAV to purchase shares in this new Fund, as Mr. Ferrer said in his September 10 e-mail.

Once again, the Division does not allege that Mr. Ferrer's statements were false. Instead, it claims that they were misleading because "[Mr.] Ferrer failed to disclose to financial advisors that: (1) secondary markets for CEFs were illiquid; and (2) UBS PR routinely acquired CEFs for its inventory and supported CEF market prices and liquidity to prevent price declines and maintain yields." OIP ¶ 47. While we believe that the Division has its facts wrong on the subject of liquidity, among other subjects, nothing that Mr. Ferrer stated in these e-mails gave rise to an obligation to make any additional disclosures. In addition, with respect to the specific Funds involved – PRFIF VI and AAA Bond Fund II – the inventory levels maintained by UBS PR remained low throughout the entire period focused on by the Division. See Expert Report of Erik R. Sirri, Ex. 9. In other words, UBS PR did not, as the Division alleges, use inventory purchases "to prevent price declines and maintain yields." Although the Division tries to obscure the fact that the 23 Funds are individual securities, each with their own characteristics, prices, yields, and liquidity profiles, this point was not lost on the FAs.

D. The E-Mails Mr. Ferrer Sent To The FAs During The Period When UBS PR Was Forced By UBS FS To Reduce Its Inventory

In addition to the six e-mails discussed above, the Division takes Mr. Ferrer to task for two e-mails he sent during the period when, at the direction of the RCC, UBS PR was reducing its inventory in the Funds. It is important to reiterate that, while the Division attempts to implicate Mr. Ferrer in the RCC's two decisions to reduce UBS PR's inventory, Mr. Ferrer had no role in either the decisions or their implementations.

The Division completely mischaracterizes the first e-mail, which was sent by Mr. Ferrer on April 24, 2009. In its OIP, the Division does not quote from the e-mail, but rather alleges that "[Mr.] Ferrer sent an email entitled 'Creation of Value' in which he misrepresented to the financial advisors [sic] the CEFs would continue to trade at significant premiums to NAV and

provide the 'reinvestment kickers' of the dividend reinvestment program." OIP ¶ 75. No fair reading of Mr. Ferrer's e-mail supports this allegation. That e-mail states in full text as follows:

> Many of you have asked I touch you all with my understanding of The Creation of Value, as relates to our Funds.
>
> This is not a theory; it is the appropriate answer to the premiums that our Funds enjoy over NAV. The portfolio of assets provides the revenues; the leverage covers costs and provides the extra returns that allow very competitive yields through dividends to be paid. You add the reinvestment kickers and you end up with above market relative returns.
>
> The marketplace awards our Funds a price indicative of its returns, a price which generally is at a premium over NAV.
>
> This premium is the value created by professional management and a Fund structure that works well in our marketplace. This value is for the benefit of Fund shareholders.
>
> One should want that such value is created because it directly reflects the success of the Funds in working for the investors benefit.
>
> NAV only reflects the valuation the market awards to the various assets in the portfolio, something we do not control.
>
> What we do control is the results of our Funds and the premiums awarded clearly spell out we create good value for our Fund shareholders.
>
> Needless to state that premium will vary from Fund to Fund, affected on the short term by supply and demand issues and reflect at different times the interest cycles. But, as long as we can maintain attractive relative returns, we should expect premiums over NAV to be there.
>
> You should relate this to your clients.

The e-mail was not intended to be, nor could any FA conclude that it was, a guarantee about the future performance of any Fund. Mr. Ferrer made no such guarantee. Instead, he merely reiterated to the FAs a fundamental truism inherent in the Funds, namely that, if the

Funds' managers can generate "attractive relative returns," then one would expect investors to continue purchasing Fund shares at "premiums over NAV," as they had done historically.

Moreover, although he had no obligation to do so, in language ignored by the Division, Mr. Ferrer specifically cautioned the FAs in that very e-mail: "Needless to state that ***premium will vary from Fund to Fund***, affected on the short term by supply and demand issues and reflect at different times the interest cycles. But, ***as long as we can maintain attractive relative returns, we should*** expect premiums over NAV to be there." (Emphasis added.) And, shortly after he sent the initial e-mail, Mr. Ferrer sent the FAs a second e-mail, reminding them that: "[i]nvesting in the Funds do carry risks," and referring them to UBS PR's Funds website "[f]or a full discussion of the risks that you and your clients should be aware of." While that second e-mail was unnecessary under the circumstances, Mr. Pluchino, the Executive Director of UBS FS's Compliance Department, suggested it be sent and Mr. Ferrer complied.[16]

In the only other e-mail cited by the Division during this period, Mr. Ferrer wrote, again to the FAs, and not to customers, on August 3, 2009, as follows:

> Have you noticed our Funds have continued to pay dividends monthly and in many instances in increasing amounts to provide pretty good yields?
>
> In our local market paying dividends is quite an accomplishment.
>
> Think about it! And consider the present price of our Funds.
>
> Is this an opportunity to consider Funds for long term investments?

OIP ¶ 77. Once again, in this e-mail Mr. Ferrer did not recommend a particular Fund as an investment and did not provide any details about a particular Fund. Rather, he told the FAs factual information that they already knew or should have known – i.e., that the Funds had

[16] Members of Legal and Compliance routinely reviewed Mr. Ferrer's, and others, e-mails for compliance purposes.

continued to pay dividends and that the price of the Funds had decreased overall. Mr. Ferrer's statements were true and, importantly, were not based on any information that was not also available to the FAs.

The Division does not claim that the statements in this e-mail were false, but rather alleges that they were misleading because Mr. Ferrer "omitted any mention of the UBS PR's inventory or share price reductions, or his belief the [sic] ongoing inventory dump had drastically reduced market prices." OIP ¶ 77. Here again, given the limited, conclusory nature of the e-mails, no additional disclosures were necessary to make the statements not misleading. Further, the Division is flatly incorrect in so far as it alleges that there was an "ongoing inventory dump." This e-mail was sent more than two months after the RCC directed UBS PR to reduce its inventory to $12 million. As Dr. Sirri concludes, "as of the date of this e-mail, UBS PR already had reduced its inventory from a maximum of nearly $50 million to the $12 million limit imposed by UBS FS." Expert Report of Erik R. Sirri, at 38. The "inventory dump" was not "ongoing." In any event, Mr. Ferrer did, in fact, disclose the existence of the reduced prices – not that he had to, as every FA who turned his or her computer on in the morning was aware of the price reductions that had occurred during that period.

Finally, in light of the fact that the RCC, and not Mr. Ferrer, decided to reduce UBS PR's inventory, if any disclosure obligations flowed from those decisions, it was the responsibility of UBS FS, the RCC, and Legal and Compliance to bring that to the attention of the persons at UBS PR who would be implementing those decisions. Neither the Trading Desk, which was responsible for the implementation of those decisions, nor anyone else at UBS PR, including Mr.

Ferrer, who had no role or supervisory role in the matter, were ever informed of any additional disclosures that should have been made.[17]

V. MR. FERRER'S COMMUNICATIONS WITH CUSTOMERS

It should come as no great surprise that the Division has disavowed any obligation to prove that Mr. Ferrer's allegedly fraudulent statements "[to the FAs ever] reached a single investor." Division's Response to Motion for More Definite Statement, supra at *11. In its OIP, the Division identifies only one instance in which Mr. Ferrer's allegedly fraudulent statements ever reached customers, albeit indirectly: an article published on April 24, 2009 in El Vocero, a local Puerto Rican newspaper, which contains quotes attributed to Mr. Ferrer. OIP ¶ 74; see also Division's Response to Motion for More Definite Statement, supra at *13.[18]

To support its allegation that Mr. Ferrer's comments quoted in the El Vocero article "misled investors about the state of the CEF market," OIP ¶ 74, the Division only cites the following portion of the article:

---

[17] It should be perfectly clear from the communications cited in the OIP that Mr. Ferrer never intended to deceive, or deceived, the FAs. The OIP refers to an e-mail that Mr. Ferrer wrote on August 29, 2008, in which Mr. Ferrer writes to UBS PR's President, Mr. Ubiñas, and the head of UBS PR's Wealth Management Division, Mr. Belaval, telling them that they have to "fix" a supply and demand problem by "generat[ing] [a] story for each Fund." The Division suggests, disparagingly, that this was an effort by Mr. Ferrer to fabricate a false story about the Funds. Nothing can be further from the truth. Indeed, Mr. Ubiñas's response, in an email omitted by the Division, noted that one of the ways UBS PR had already addressed Mr. Ferrer's concerns about fostering demand on the part of the FAs and their clients, was through "[c]lient and FA education." No false story was ever discussed, drafted, or distributed.

[18] Mr. Ferrer also gave brief welcoming remarks at two investor conferences – one in June 2008 and one in March 2009. We do not understand the Division to be alleging that Mr. Ferrer's remarks – which were non-substantive – were misleading. See OIP ¶¶ 34, 69, 71; see also Division's Response to Motion for More Definite Statement, supra at *13. Although it is unclear what, if any, legal significance the Division places on its characterization that Mr. Ferrer "hosted" these conferences, at this stage, we merely note that Mr. Ferrer did not draft or assist in the preparation of any of the presentations, which were all reviewed and approved in advance by Legal and Compliance, and, in any event, were all truthful and not misleading.

Similarly, we do not understand the Division to be seeking to impose liability on Mr. Ferrer for the CEF prices published on a weekly basis in El Vocero. Mr. Ferrer simply had nothing to do with, and no responsibility for, publishing the prices or any other information UBS PR may have provided to El Vocero on this subject. Regardless, we do not see how the publication of those prices was fraudulent or otherwise misleading. For a more complete discussion of this subject, we respectfully refer the Court to Section III(A) of the Ortiz Submission.

> "Local mutual funds have had an excellent yield throughout this process," explains Ferrer. But despite this, many investors call scared, because of the news about the lows in financial markets, "when in reality that news does not have any relevance to the investor. In general, the Puerto Rican investor that has his/her money invested in bonds and mutual funds have obtained fantastic results."
>
> Local mutual funds have had results over the years comparable to shares. "The result of an investor in local mutual funds who has been able to reinvest the dividends has been higher, and in some cases, comparable to the market of shares Index", says Ferrer, and assures that this type of investment offers much less volatility, and good relative results.

However, the Division fails to quote the ***very next paragraph***, in which Mr. Ferrer explicitly cautions that his statements are of a ***general*** nature only:

> "***This does not mean that each investor should not look at his/her particular situation, and adjust his/her decisions to the risks he/she is willing to consider***," warns the executive. "But having said that, ***in general terms***, the Puerto Rican investor has not been involved in the crisis."

(Emphasis added.) Mr. Ferrer further noted that, although he believed "that the market of shares has reached its minimum levels, and now just remains to go up[,] . . . 'the rally is not necessarily to continue'" – i.e., he did not "believe that we have touched the bottom, that perhaps it may go down before coming up." Again, the Division does not quote this language in its OIP.

Aside from omitting the portion of the article containing the cautionary language, the Division misleadingly asserts that the statements attributed to Mr. Ferrer are related to "the state of the CEF market" – i.e., to UBS PR's CEFs. OIP ¶ 74. As the article makes clear, the quotes are related to the market for "local mutual funds" generally. That includes ***all*** local mutual funds, including those offered by UBS PR's competitors. Even if Mr. Ferrer's statements could be construed as referring only to UBS PR's CEFs, and even if Mr. Ferrer's cautionary language is ignored, as noted above, Dr. Sirri concludes in his Expert Report that Mr. Ferrer's statements

about the CEFs' performance and their relative low volatility were true. Expert Report of Erik R. Sirri, at 36-37.[19]

VI. THE SHARE REPURCHASE PROGRAM

Lastly, to the extent the Division's claims against Mr. Ferrer are premised on his role as one of many Directors of the Funds in approving the share repurchase program, see OIP ¶¶ 79-81, it fundamentally misunderstands the share repurchase program. The facts and testimony presented at the hearing will demonstrate that the approval of the share repurchase program was a routine function of the Board of Directors, that it had been put in place years before the RCC decided to reduce inventory, that approval of the share repurchase program bore no relationship to the RCC's decision to reduce UBS PR's inventory to $12 million, and that the transactions stemming from the share repurchase program were highly beneficial to UBS PR's customers. The Division's suggestion to the contrary is completely baseless.

ARGUMENT

I. MR. FERRER'S COMMUNICATIONS WITH THE FAs DID NOT VIOLATE THE FEDERAL SECURITIES LAWS

We respectfully submit that the assertion that Mr. Ferrer's handful of brief e-mails of a general nature sent internally to the FAs violated Section 10(b), Rule 10b-5(b), and Section 17(a)(2), should fail as a matter of law. First, Mr. Ferrer's statements were all true, a factual matter uncontested even by the Division's own expert, and did not "omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading," 17 C.F.R. § 240.10b-5. Second, Mr. Ferrer's statements were of the most conclusory nature or were merely expressions of his own opinions, which, as a matter of law, are not actionable. Third, any supposed omissions were immaterial because they

[19] Moreover, the Division does not allege that Mr. Ferrer controlled the content of article.

would not have altered the total mix of information available to the FAs: the FAs were sophisticated participants in the CEF market and knowledgeable about the basic facts that the OIP claims were not disclosed to them. Fourth, Mr. Ferrer neither made the statements with scienter, nor acted negligently in making the statements. Finally, Mr. Ferrer's internal statements to the FAs cannot be deemed statements "made" by Mr. Ferrer "in connection with the purchase or sale of securities" or "in the offer or sale of securities." Any one of the foregoing is grounds for the dismissal of the Division's claims.

A. Mr. Ferrer Did Not Violate Section 10(b) and Rule 10b-5(b)

To establish liability under Section 10(b) and Rule 10b-5(b), the Division must prove that Mr. Ferrer: (1) "made a material misrepresentation or a material omission as to which he had a duty to speak, . . . ; (2) with scienter; (3) in connection with the purchase or sale of securities." SEC v. Slocum, Gordon & Co., 334 F. Supp. 2d 144, 170 (D.R.I. 2004) (emphasis added); see also SEC v. Tambone, 550 F.3d 106, 130 (1st Cir. 2008), rev'd on other grounds, 597 F.3d 436 (1st Cir. 2010) (en banc).

1. Mr. Ferrer Did Not Make Any Material Misstatements or Omissions

a. Mr. Ferrer's Statements To The FAs Were True

As an initial matter, all of Mr. Ferrer's statements to the FAs were true. Specifically, Dr. Sirri states in his expert report that, as of the time of Mr. Ferrer's e-mails, the CEFs, in fact, had "superior performance" and "low volatility." Expert Report of Erik R. Sirri, at 36-37. The Division's expert, Dr. O'Neal, does not dispute these conclusions. Moreover, Mr. Ferrer's e-mail of October 8, 2008 even focused the FAs on the supply and demand imbalance, which the Division alleges he was attempting to hide from them. See E-Mail from Mr. Ferrer to DL-Puerto Rico Financial Advisors, dated October 8, 2008, supra at *17. Mr. Ferrer's opinions regarding

the favorable yields that would be generated by the two new Funds were also grounded in fact, and the two e-mails he sent to the FAs in 2009 were likewise true.

b. The Allegedly Omitted Information Was Not Material Because Mr. Ferrer's Statements Were Non-Actionable Expressions of Opinion or Loosely Optimistic Statements

As a matter of law, none of Mr. Ferrer's statements are actionable as violations of the federal securities laws. They were not intended to be, nor could they have been construed to be, comprehensive statements of fact. Courts have routinely held that statements amounting to nothing more than expressions of opinion or optimistic statements, like the ones Mr. Ferrer made to the FAs, are not material statements of fact actionable under the federal securities laws:

> [C]ourts have demonstrated a willingness to find immaterial as a matter of law a certain kind of rosy affirmation commonly heard from corporate managers and numbingly familiar to the marketplace -- loosely optimistic statements that are so vague, so lacking in specificity, or so clearly constituting the opinions of the speaker, that no reasonable investor could find them important to the total mix of information available.

Shaw v. Digital Equip. Corp., 82 F.3d 1194, 1217 (1st Cir. 1996).

Mr. Ferrer's statements were nothing more than non-actionable expressions of opinion. With few exceptions, Mr. Ferrer made no statements, nor did he even express any opinions, about any one of the 23 individual CEFs. His statements that the Funds had "superior performance" and "low volatility" are the rough equivalent of telling a group of brokers that they should consider "technology stocks" as good investment vehicles for their clients because they have been performing well. Such statements are not actionable as material statements of fact. The same is true of Mr. Ferrer's opinion that PRFIF VI would "presently provide good yields" or "promptly show attractive returns," his obvious comments about how the Funds *could* continue

to trade at premiums to NAV, and his suggestion to look at the Funds as investment opportunities because of reduced prices.

When compared to the statements that Courts have historically found to be immaterial as a matter of law, it is clear that Mr. Ferrer's statements do not begin to rise to the level of material statements that may be challenged as violations of the federal securities laws. The First Circuit, for example, has held that "upbeat statements of optimism" – such as "Sales continue to be strong in both our U.S. and international channels" and "Our new ventures are also off to a good start with revenues of $2.7 million" – are not actionable. Greebel v. FTP Software, Inc., 194 F.3d 185, 189-90, 207 (1st Cir 1999). Mr. Ferrer's statements are no different.

While we appreciate that conclusory statements that are knowingly false and made with an intent to deceive may be actionable, that is simply not this case. To the contrary, none of the statements here were false, knowingly or otherwise, and Mr. Ferrer never intended to mislead the FAs. Statements, such as the ones at issue here, that are based in fact, loosely optimistic, of a conclusory nature, and demonstrably true, do not violate the federal securities laws.

When faced with claims involving statements almost identical to the ones Mr. Ferrer made to the FAs, the Second Circuit has held that "relatively subdued general comments, such as the company '***should*** deliver income growth consistent with its ***historically superior performance***'" were not actionable because they "lack the sort of definite positive projections that might require later correction." San Leandro Emergency Med. Group Profit Sharing Plan v. Philip Morris, 75 F.3d 801, 811 (2d Cir. 1996) (emphasis added). The Second Circuit has likewise held that statements that a company had a "commitment to create earnings opportunities" and that certain "business strategies [would] lead to continued prosperity" were immaterial as a matter of law. According to the Court, by making those statements, the company

was not "certify[ing] that [it] would not suffer losses," "insuring that dividend rates would remain constant, or [insuring] that the stock price would not decline." Lasker v. N.Y. State Elec. & Gas Corp., 85 F.3d 55, 59 (2d Cir. 1996) (per curiam); see also ECA & Local 134 IBEW Joint Pension Trust of Chi. v. JP Morgan Chase Co., 553 F.3d 187, 206 (2d Cir. 2009) ("Finding that JPMC's statements constitute a material misrepresentation would bring within the sweep of federal securities laws many routine representations made by investment institutions. We decline to broaden the scope of securities laws in that manner.").

In Lasker, the plaintiffs alleged that "[the] defendants had misled shareholders by making [these] unduly optimistic statements . . . about the likely financial effect of diversification." 85 F.3d at 57. The Court affirmed the dismissal of the complaint, holding that "[a] reasonable investor would not believe that, by merely making [these] broad, general statements, [the company] had insured against the risks inherent in diversification." Id. at 59. The same is true here. Mr. Ferrer made broad, general, and truthful statements about the CEFs. Without even considering the other information made available to them, no reasonable FA could have concluded that these statements guaranteed future performance, that the Funds' secondary market would remain wholly liquid, or that the Trading Desk would continue to maintain inventory at the same levels as it had historically.

Moreover, Mr. Ferrer made no statements about the overall liquidity of the Funds or about the inventory levels of the Funds. Thus, he did not "put the subject . . . in play" by merely noting general, demonstrably true characteristics of the Funds. SEC v. Mozilo, No. CV 09-3994-JFW (MAN), 2010 U.S. Dist. LEXIS 98203, at *36-37 (C.D. Cal. Sept. 16, 2010).

Accordingly, Mr. Ferrer's communications did not give rise to an obligation to provide any "further disclosures" to the FAs. In re Boston Tech. Sec. Litig., 8 F. Supp. 2d 43, 71 (D.

Mass. 1998) (holding that "remarks as to the existence of market opportunities and [company's] prospects in that market do not support 10b-5 liability"); see also Searls v. Glasser, 64 F.3d 1061, 1067 (7th Cir. 1995) (defendant's assurance "that disposition gains would be 'high'" held not actionable); Hillside Partners Ltd. P'ship v. Adage, Inc., 42 F.3d 204, 212 (4th Cir. 1994) (prediction of "significant sales gains . . . as the year progresses" held too vague to be material).

c. The Allegedly Omitted Information Was Not Material Because It Did Not Alter The "Total Mix" Of Information Available To The FAs

Assuming, arguendo, the statements made by Mr. Ferrer are actionable, in determining whether those statements are violative of the federal securities laws, they must be judged against the knowledge and information that was possessed by, or otherwise available to, the FAs at the time Mr. Ferrer made the allegedly misleading statements. A statement is "material only if its disclosure would alter the total mix of facts available to the investor and if there is a substantial likelihood that a reasonable shareholder would consider it important to the investment decision." Lucia v. Prospect Street High Income Portfolio, Inc., 36 F.3d 170, 175 (1st Cir. 1994) (internal quotation marks omitted). "The 'total mix' of information may also include 'information already in the public domain and facts known or reasonably available to shareholders.'" United Paperworkers Int'l Union v. Int'l Paper Co., 985 F.2d 1190, 1999 (2d Cir. 1993). Because the Division has conceded that it is seeking to hold Mr. Ferrer liable for his statements to the FAs and "not . . . for the statements of financial advisors to investors," the proper inquiry here is whether the allegedly omitted information would alter the "total mix" of facts available to ***the FAs*** and if there is a substantial likelihood that a ***reasonable FA*** would consider it important to an investment recommendation. In making this determination, facts known or reasonably available to ***the FAs*** must be included in the "total mix" of information. See Panter v. Marshall

Field & Co., 646 F.2d 271, 289 (7th Cir. 1981); Seibert v. Sperry Rand Corp., 586 F.2d 949, 952 (2d Cir. 1978) ("Although the underlying philosophy of federal securities regulations is that of full disclosure, there is no duty to disclose information to one who reasonably should already be aware of it.") (internal citations and quotation marks omitted); In re Flannery, Initial Decision Release No. 438, File No. 3-14081, at *40 (Oct. 28, 2011).

Here, the "total mix" of information necessarily includes the FAs' fundamental understanding of the Puerto Rican financial market and UBS PR's individual CEFs. See, e.g., Seibert, 586 F.2d at 952. The FAs, who were all trained financial professionals, already knew everything that the Division claims Mr. Ferrer omitted in his e-mails – (1) the Funds could experience periods of illiquidity; (2) UBS PR facilitated a secondary market, but it was not obligated to do so; (3) when there were imbalances in the market, UBS PR would use inventory purchases to provide its customers with additional liquidity; (4) during the Fall of 2008, there were imbalances in the markets for some of the individual Funds; and (5) during the Spring of 2009, the Trading Desk was reducing its inventory.[20] Indeed, the FAs had a fiduciary duty to not only know and understand much of this information, but to also have "an adequate basis for the opinions [they] render[ed]" when advising their customers on the suitability of a particular investment. Hanley v. SEC, 415 F.2d 589, 596 (2d Cir. 1969); see also FINRA Rule 2310, superseded by, FINRA Rule 2111.

In addition, UBS PR provided the FAs with a wealth of information, all of which disclosed the information Mr. Ferrer allegedly omitted. To name just a few, the prospectuses,

---

[20] We submit that UBS PR had no duty to disclose its inventory decisions to the market or to the FAs. See Norman S. Poser & James A. Fanto, Broker-Dealer Law & Regulation § 16.03[A][2] at 16-78 (4th ed. 2010) (appended as Tab 3 of the Ortiz Submission). Even if, however, such an obligation exists, it was nevertheless Legal and Compliance's responsibility to make and implement decisions regarding disclosures, and it decided that no disclosures were necessary.

the Family of Funds Brochure, the Question and Answer Guides, and the 2007 Legal and Compliance Presentation, all disclosed the liquidity risks associated with the Funds and UBS PR's role as a market facilitator. The inventory sheets and the GTC Book disclosed when the Trading Desk began reducing inventory and when the Trading Desk had stopped purchasing shares into its inventory. And that says nothing of the informal disclosures that were made.

In light of the wealth of information readily available to the FAs regarding all material aspects of the Funds, the Division's suggestion that Mr. Ferrer had to supplement his truthful, general e-mails to the FAs with additional disclosures has no support in the case law. The mere fact that Mr. Ferrer chose to discuss the Funds with the FAs does not ipso facto impose on him an obligation to disclose ***all*** details about the Funds. None of Mr. Ferrer's statements "omit[ted] to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading." 17 C.F.R. § 240.10b-5.

Indeed, although the Division challenges Mr. Ferrer's e-mails for their failure to discuss liquidity, pricing, and inventory, under the Division's theory, he would also be liable for failing to disclose the fact that there were 23 different Funds, that each of the Funds have different attributes, prices, and yields, that the Funds hold a variety of different assets, and that the prospectuses contain dozens of pages of additional disclosures. The federal securities laws impose no such obligations on a speaker who makes the types of casual and general statements that Mr. Ferrer made to the professional FA staff at UBS PR. See Gross v. Summa Four, Inc., 93 F.3d 987, 992 (1st Cir. 1996), partially superseded by statute on other grounds as recognized in Greebel, 194 F.3d at 197 ("[W]hen a corporation does make a disclosure – whether it be voluntary or required – there is a duty to make it complete and accurate. ***This, however, does not mean that by revealing one fact about a product, one must reveal all others that, too,***

would be interesting, market-wise, but means only such others, if any, that are needed so that what was revealed would not be so incomplete as to mislead.") (internal quotation marks and citation omitted) (emphasis added).

2. Mr. Ferrer Did Not Act With Scienter When He E-Mailed the FAs About the Funds

There can, of course, be no violation of Section 10(b) or Rule 10b-5(b) unless Mr. Ferrer acted with scienter, which refers to "a mental state embracing intent to deceive, manipulate, or defraud." Rizek v. SEC, 215 F.3d 157, 162 (1st Cir. 2000) (quoting Ernst & Ernst v. Hochfelder, 425 U.S. 185, 194 n.12 (1976)). Scienter requires "a showing of either conscious intent to defraud or a high degree of recklessness." ACA Financial Guaranty Corp. v. Advest, Inc., 512 F.3d 46, 58 (1st Cir. 2008) (internal quotation marks omitted). "Reckless conduct" is defined as a highly unreasonable omission, involving not merely simple, or even inexcusable, negligence, but an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known to the defendant or so obvious the actor must have been aware of it." Rizek, 215 F.3d at 162.

There is simply no basis to suggest that any statement attributed to Mr. Ferrer was made with a "conscious intent to defraud" UBS PR's FAs. Particularly when viewed against the back drop of similar memoranda and e-mails that Mr. Ferrer had been sending to the FAs for years, and his knowledge of the information the FAs knew or should have known in discharging their responsibilities to their customers, it is clear that the challenged e-mails were, at best, intended to be reminders to the FAs of categories of investment opportunities that they should consider exploring. Moreover, as is readily apparent from the e-mails, Mr. Ferrer passionately believed in Puerto Rico and in the favorable investment opportunities that the CEFs presented. It is also patently apparent that the e-mails were not written with a belief that any FA would, or could,

make a recommendation on the strength of Mr. Ferrer's statements without properly understanding and disclosing the attributes of the Fund they recommended and whether such Fund was suitable for their clients. Accordingly, Mr. Ferrer did not act with scienter. See In re Flannery, Release No. 438, File No. 3-14081, at *40; Martin v. Steubner, 485 F. Supp. 88, 97 (S.D. Ohio 1979) (holding that defendant's honest belief that plaintiff was a sophisticated investor who understood the nature of investment defeated finding of an intent to defraud).

3. Mr. Ferrer Did Not Make Any Statements "In Connection With" The Purchase Or Sale Of A Security

The Division has conceded that it is "not seeking to hold [Mr.] Ferrer liable for the statements of financial advisors to investors," but rather seeks to hold him liable for allegedly misleading communications made internally to UBS PR's own FAs, "even if his statements never reached a single investor." Division's Response to Motion for More Definite Statement, supra at *11, *13. But Mr. Ferrer's internal statements to the FAs can only be deemed "in connection with the purchase or sale of securities" if Mr. Ferrer "***anticipated and intended*** that his concealment . . . would result in the [FAs] ***misleading investors***" and if Mr. Ferrer's "omissions ***had the intended result of deceiving investors***." SEC v. Nacchio, 438 F. Supp. 2d 1266, 1282 (D. Colo. 2006) (emphasis added); see also SEC v. Wolfson, 539 F.3d 1249, 1261 (10th Cir. 2008) ("The relevant question is only whether he can fairly be said to have caused F10 to make the relevant statements, ***and whether he knew or should have known that the statements would reach investors***,") (emphasis added). Thus, the Division must prove what it concedes that it cannot: that Mr. Ferrer's statements to the FAs ***did*** reach investors. In any case, far from anticipating and intending that his statements would be used to mislead investors, at all times Mr. Ferrer knew that his statements were true; that he was speaking to experienced professionals; and that, if and when the FAs recommended ***a specific Fund*** to a customer, they

would only do so after carefully fulfilling their legal duty to consider the benefits and risks of the Fund and after determining that the Fund in question was suitable for the customer. None of Mr. Ferrer's emails ever suggested they do otherwise. To the contrary, Mr. Ferrer always emphasized the importance of these obligations.

In addition, Mr. Ferrer's internal statements to the FAs can only be deemed to have been "made" by Mr. Ferrer if he had "ultimate authority over the [FA's] statement[s to customers], including [their] content and whether and how to communicate [them]"; and, even then, only if the statements were attributed to Mr. Ferrer when they were repeated to customers. Janus Capital Grp. Inc. v. First Derivatives Traders, 131 S. Ct. 2296, 2302, 2305 & n.11 (2011). Janus has abrogated earlier cases holding that it is sufficient merely for a speaker to anticipate and intend that his statements would be used by someone else to mislead investors. Indeed, contrary to the Division's position that Mr. Ferrer can be held liable even if his statements to the FA's "never reached a single investor," the first post-Janus federal court to consider a case in which the Division sought to hold an executive liable for internal statements determined that liability could only exist "so long as it is proven that the statement was made to the investing public." SEC v. Daifotis, No. C 11-00137 WHA, 2012 U.S. Dist. LEXIS 81306, at *23 (N.D. Cal. June 12, 2012) (holding defendant/speaker could be liable for internal statements only where he had ultimate authority to tell company employees to use statements as "sounding points" when communicating with clients, and employees expressly attributed statements by name to defendant when repeating them).

The Division may seek to sidestep the requirements imposed by Janus, Wolfson, Nacchio, and Daifotis,[21] by relying, as it did in its Response to Mr. Ferrer's Motion for More Definite Statement in support of this position, on the case of United States v. Naftalin, 441 U.S. 768 (1979). That case, however, stands for the wholly unremarkable proposition that brokers, and not just investors, can be the victims of securities frauds. But here, unlike in Naftalin, the FAs were not the victims of a fraud. All of the statements Mr. Ferrer made to them were true, and the FAs were well-aware of ***all*** relevant information, including the information which the Division alleges was omitted by Mr. Ferrer.[22]

B. Mr. Ferrer Did Not Violate Section 17(a)(2)

For its Section 17(a)(2) claims, the Division must prove that Mr. Ferrer:

> (1) directly or indirectly (2) obtained money or property (3) by means of any untrue statement of material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, such statement having been made (4) with negligence (5) in the offer or sale of any securities.

Tambone, 550 F.3d at 125.

As an initial matter, Mr. Ferrer did not violate Section 17(a)(2) for many of the same reasons already discussed above, namely, because: (1) his statements were true, and they did not

---

[21] To be sure, adopting the Division's theory of this case would, as a practical matter, render Janus's holding meaningless. Under Janus, a respondent who makes an internal statement to an innocent third party cannot be liable if the innocent third party repeats the statement to an investor, unless the respondent has "ultimate authority" over the innocent third party's statements, and, when repeating the statement to the investor, the innocent third party attributes the statement to the respondent. The Division will undo this requirement by simply seeking to hold the respondent liable for making the statement to the innocent third party with no consideration of whether the statement was repeated to investors or attributed to the respondent. This, Janus forbids. See Janus Capital Grp. Inc., 131 S. Ct. at 2302, 2305 & n.11.

[22] Other cases cited by the Division in its Response to Mr. Ferrer's Motion for More Definite Statement similarly involved situations where the SEC alleged the brokers themselves were victims of fraud. See Graham v. SEC, 222 F.3d 994, 1000-02 (D.C. Cir. 2000) (affirming § 10(b) and Rule 10b-5 liability in case where brokers were themselves defrauded regardless of fact that no actual or potential investors were defrauded); In re Jett, SEC Release No. 49366, 2004 SEC LEXIS 504, File No. 3-8919 (Mar. 5, 2004) (holding broker liable for defrauding his brokerage firm).

"omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading," 17 C.F.R. § 240.10b-5; (2) the allegedly omitted information was already known to the FAs and was otherwise part of the "total mix" of information available to the FAs; and (3) his statements were his own opinions, which none of the FAs could have considered to be statement of facts. See SEC v. Monarch Funding Corp., 192 F.3d 295, 308 (2d Cir. 1999) (noting that the elements of Rule 10b-5(b) and Section 17(a)(2) are "[e]ssentially the same."). In addition to those reasons, Mr. Ferrer did not violate Section 17(a)(2) because: (1) he did not act negligently; (2) his conduct did not occur in the offer or sale of any securities; and (3) he obtained no money or property from the statements.

1. Mr. Ferrer Did Not Act Negligently When E-Mailing The FAs About The Funds

For largely the same reasons that Mr. Ferrer did not act with scienter when e-mailing the FAs, supra Section I(A)(2), he likewise did not act negligently. Specifically, Mr. Ferrer's statements were all truthful and accurate, and otherwise expressions of opinion that were grounded in fact. He did not mislead the FAs, nor was it necessary to provide them with additional information. To the contrary, consistent with their legal and ethical obligations to discharge their duties to their customers, the FAs could not rely on Mr. Ferrer's superficial e-mails. They had to inform themselves of all relevant facts for each specific Fund they recommended. Equally as important, Mr. Ferrer knew, or reasonably believed, that the FAs knew or had access to all relevant information.

2. Mr. Ferrer Did Not Engage In Any Conduct "In The Offer Or Sale" Of The Funds

The Division's concession that it is "not seeking to hold [Mr.] Ferrer liable for the statements of financial advisors to investors, but for his statements to financial advisors,"

Division's Response to Motion for More Definite Statement, supra at *13, is, on its own, fatal to its Section 17(a)(2) claims because Mr. Ferrer's statements to the FAs were not made "in the offer or sale" of the Funds. A statement is made "in the offer or sale" of a security when it is made at some point during the "selling process." Naftalin, 441 U.S. at 773. Wholly internal communications within a brokerage firm, such as Mr. Ferrer's motivational e-mails to the FAs, cannot be considered part of the "selling process." Id.; see also SEC v. Brown, 740 F. Supp. 2d 148, 163 (D.D.C. 2010) (noting that Section 17(a) "typically involves omissions and misstatements made in securities registration statements"). Mr. Ferrer did not sell or offer to sell any securities to the FAs, nor did he place sell orders with the FAs so that they could act as agents and execute the orders. He merely gave the FAs his generalized and truthful opinions about the Funds in a series of mass, informal e-mails. These types of general statements – entirely removed from the actual selling process – are not actionable under Section 17(a)(2).[23]

3. Mr. Ferrer Obtained No Money Or Property From The Statements He Made To The FAs

Mr. Ferrer did not personally receive any money or property "by means of" the e-mails he sent to the FAs. See SEC v. Daifotis, No. C 11-00137 WHA, 2011 U.S. Dist. LEXIS 60226, at *27 (N.D. Cal. June 6, 2011) (holding that SEC must prove that the defendant *personally* received money or property to establish liability under Section 17(a)). Mr. Ferrer's

---

[23] It is Mr. Ferrer's position that the term "in," as used in Section 17(a)(2), proscribes a narrower range of conduct than the term "in connection with," as used in Section 10(b) and Rule 10b-5(b). See Klamberg v. Roth, 473 F. Supp. 544, 556 (S.D.N.Y. 1979); but see Naftalin, 441 U.S. at 773 n.4. Specifically, as set forth above, for Section 17(a)(2), the challenged conduct must have occurred during some part of the actual selling process, whereas, under Section 10(b) and Rule 10b-5(b), it is sufficient for the challenged conduct to merely "'coincide' with a securities transaction." Tambone, 550 F.3d at 122. Regardless, even if "in" is synonymous with "in connection with," Mr. Ferrer's statements still were not made "in the offer or sale" of the Funds for the reasons discussed above in Section I(A)(3), namely, because Mr. Ferrer did not (1) intend or reasonably anticipate that the FAs would use his e-mails to defraud customers; or (2) have "ultimate authority" over the FAs statements to customers. See In re Flannery, SEC Initial Decision Release No. 438, at *41-43 (holding that Janus applies to Section 17(a)(2)); see also SEC v. Kelly, 817 F. Supp. 2d 340, 345-46 (S.D.N.Y. 2011) (same).

compensation was in no way – directly or indirectly – tied to the Funds generally or the secondary market for the Funds specifically. UBS FS determined Mr. Ferrer's compensation based on a subjective determination of Mr. Ferrer's worth to the firm. The secondary market is not a profit center, and the fact that UBS PR facilitated a secondary market in the Funds for the benefit of its customers did not factor into Mr. Ferrer's salary.

II. MR. FERRER DID NOT MAKE ANY MISLEADING STATEMENTS TO UBS PR'S CUSTOMERS

There is also no basis under Section 10(b), Rule 10b-5(b), or Section 17(a)(2), to hold Mr. Ferrer liable for making allegedly false or misleading statements to UBS PR's customers via the April 24, 2009 El Vocero article. First, the statements attributed to Mr. Ferrer in El Vocero were true and, in any event, were non-actionable expressions of opinion. The article does not quote Mr. Ferrer as having mentioned any one of UBS PR's individual Funds. In fact, the article quotes Mr. Ferrer as only referring to "[l]ocal mutual funds," rather than any product issued by UBS PR. Further, the OIP completely ignores that portion of the article in which Mr. Ferrer is quoted as having made certain precautionary statements. Thus, the OIP omits, among other precautionary statements, the following: "'This does not mean that each investor should not look at his/her particular situation, and adjust his/her decisions to the risks he/she is willing to consider,' warns the executive. 'But having said that, in general terms, the Puerto Rican investor has not been involved in the crisis.'" Nothing that was said in that article was misleading or gave rise to any further disclosure obligations on the part of Mr. Ferrer.

Finally, as a general matter, the Division cannot rely on Mr. Ferrer's quotes in El Vocero to support is claims absent a showing that Mr. Ferrer had control over the final version of the article. See In re Cable & Wireless, PLC, 321 F. Supp. 2d 749, 769 (E.D. Va. 2004); Strassman v. Fresh Choice, No. C-95-20017 RPA, 1995 U.S. Dist. LEXIS 19343, at *22-25 (N.D. Cal. Dec.

7, 1995); Schwartz v. Novo Industri, A/S, 658 F. Supp. 795, 799 (S.D.N.Y. 1987). The reason for this is simple. Absent proof of control, statements published in a newspaper article "could be taken out of context, incorrectly quoted, or stripped of important qualifiers." Raab v. Gen. Physics Corp., 4 F.3d 286, 288-89 (4th Cir. 1993). Indeed, the article does not even consistently quote directly from Mr. Ferrer, but rather consists of a mixture of quotes and unquoted statements that were simply attributed to him.[24]

III. MR. FERRER DID NOT AID AND ABET ANY OF UBS PR'S ALLEGED VIOLATIONS OF THE SECURITIES LAWS

To establish its claims that Mr. Ferrer aided and abetted UBS PR's violations of Section 10(b), Rule 10b-5, and Section 17(a), the Division must prove: "(1) a primary violation was committed; (2) the defendant was generally aware that his role or conduct was part of an overall activity that was improper; and (3) the defendant knowingly and substantially assisted in the primary violation." Tambone, 550 F.3d at 144. Simply stated, the facts do not support attaching secondary liability to Mr. Ferrer.

First, we strongly believe that there has been no primary violation on the part of any person associated with UBS PR. Mr. Ferrer, therefore, cannot be liable for allegedly aiding and abetting UBS PR's purported securities violations.

Second, Mr. Ferrer did not knowingly and substantially assist any alleged violations of the securities laws by any person. Mr. Ferrer did not participate in, or supervise, any of the day-to-day pricing decisions. Similarly, Mr. Ferrer was not involved in managing UBS PR's inventory, in seeking increases to its inventory limits, or in handling buy and sell orders. He did not participate in either of the RCC's decisions to reduce inventory – in both instances, he did

[24] In addition, for largely the same reasons discussed above, Mr. Ferrer did not act with scienter or negligently – i.e., he honestly believed that his statements were true. Supra Sections I(A)(2) and I(B)(1).

not learn about the decisions until after they were made. And, once the decisions were made, Mr. Ferrer did not participate in their implementation. Far from supporting the RCC's decision, Mr. Ferrer explicitly urged the RCC to reverse its directive. All of this is at odds with the notion that Mr. Ferrer substantially assisted the purported violations.[25]

IV. MR. FERRER CANNOT BE LIABLE FOR SCHEME LIABILITY

The Division's claims under Section 17(a)(1) and (3) and Rule 10b-5(a) and (c) address so-called "scheme liability." These sections "prohibit the use of 'any device, scheme, or artifice to defraud' or the participation 'in any act, practice, or course of business' that would perpetrate fraud on investors." SEC v. Lucent Techs., Inc., 610 F. Supp. 2d 342, 349-50 (D.N.J. 2009). To establish its claims for scheme liability under Rule 10b-5(a) and (c), the Division must prove that Mr. Ferrer: (1) "committed a deceptive or manipulative act, (2) in furtherance of the alleged scheme to defraud, (3) with scienter." Id. at 350. Claims under Section 17(a)(1) and (3) are generally analyzed under the same standard. See SEC v. Kelly, 817 F. Supp. 2d 340, 346 (S.D.N.Y. 2011). However, while scienter is an element of a Section 17(a)(1) claim, negligence is all that is required for Section 17(a)(3).[26] See Aaron v. SEC, 446 U.S. 680, 695 (1980).

Scheme liability "hinges on the performance of an ***inherently deceptive act*** that is distinct from an alleged misstatement." Kelly, 817 F. Supp. 2d at 344 (emphasis added); see also SEC v. Daifotis, No. C 11-00137 WHA, 2011 U.S. Dist. LEXIS 60226, at *24 (N.D. Cal. June 6, 2011) ("Scheme liability under [Rule 10b-5 and Section 17(a)] exists when a 'defendant's conduct or role ***in an illegitimate transaction*** has the principal purpose and effect of creating a false

---

[25] To establish its aiding and abetting claims under Section 15(c)(1) of the Exchange Act, the Division is "required to prove [the same elements as] required under . . . section 17(a), including that the defendant acted negligently." Tambone, 550 F.3d at 147. Accordingly, the Division's Section 15(c)(1) claims fail for the same reasons as its Section 17(a) claims.

[26] Mr. Ferrer did not act with scienter, supra Section I(A)(2), or negligently, supra Section I(B)(1).

appearance of fact in the furtherance of a scheme to defraud,'") (emphasis added); Lucent Techs., Inc., 610 F. Supp. 2d at 360-61 (dismissing claims under Rule 10b-5(a) and (c) where "[t]he alleged deception . . . arose from the failure to disclose the real terms of the deal" because such allegations were "nothing more than a reiteration of the misrepresentations and omissions") (internal quotation marks omitted).

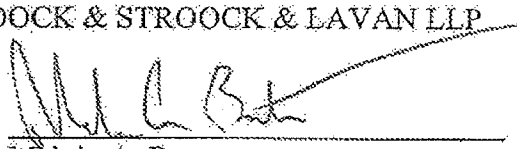
The only allegations of specific acts performed by Mr. Ferrer are: (1) he participated in two investor conferences in June 2008 and March 2009; (2) he gave an interview, portions of which were published in El Vocero; and (3) he e-mailed the FAs about the Funds. None of these acts were deceptive, much less ***inherently*** deceptive. Accordingly, they cannot support a charge of scheme liability.

Lastly, to the extent the Division's scheme liability claims appear to be based on pricing and the RCC's inventory decisions, the simple fact is that Mr. Ferrer had no role in those activities. Thus, even if those acts are somehow deemed to be inherently deceptive – and we submit that they were not – Mr. Ferrer still did not personally engage in any deceptive or manipulative conduct ***in furtherance of*** those acts. See Lucent Techs., Inc., 610 F. Supp. 2d at 350.

CONCLUSION

For the reasons set forth above, this Court should dismiss the OIP as against Mr. Ferrer.

STROOCK & STROOCK & LAVAN LLP

By: 

Melvin A. Brosterman
180 Maiden Lane
New York, New York 10038
(212) 806-5400

Attorneys for Miguel A. Ferrer

Of Counsel:

Francis C. Healy
David M. Cheifetz
Stephanie A. Cournoyer
Patrick N. Petrocelli
***
Guillermo J. Bobonis
Bobonis, Bobonis & Rodríguez Poventud
129 Ave. De Diego
San Juan, P.R. 00911
(787) 725-7941