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 11 Yucatan Resorts S.A., RHI, Inc., and RHI, S.A.

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS:

11 **MARC SPITZER, Chairman**
 12 **WILLIAM A. MUNDELL**
 13 **JEFF MATCH-MILLER**
 14 **MIKE GLEASON**
 15 **KRISTIN K. MAYES**

In the matter of:

16 **YUCATAN RESORTS, INC., d/b/a**
 17 **YUCATAN RESORTS, S.A.,**

18 **RESORT HOLDINGS**
 19 **INTERNATIONAL, INC. d/b/a**
 20 **RESORT HOLDINGS**
 21 **INTERNATIONAL, S.A.,**

22 **WORLD PHANTASY TOURS, INC.**
 23 **a/k/a MAJESTY TRAVEL**
 24 **a/k/a VIAJES MAJESTY**

25 **MICHAEL E. KELLY and LORI**
 26 **KELLY,**

Respondents.

DOCKET NO. S-03539A-03-0000

**RESPONDENTS' JOINT MOTION
 TO COMPEL OR,
 ALTERNATIVELY, TO VACATE
 THE TEMPORARY ORDER TO
 CEASE AND DESIST.**

**(ASSIGNED TO THE HONORABLE
 MARC STERN, ADMINISTRATIVE
 LAW JUDGE)**

Arizona Corporation Commission

DOCKETED

MAR 18 2004

DOCKETED BY

I.
PRELIMINARY STATEMENT

1
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3 On January 23, 2004, Respondents Resort Holdings International, Inc., Resort Holdings
4 International S.A., Yucatan Resorts, Inc., and Yucatan Resorts S.A. (hereinafter collectively
5 referred to as "Respondents"), served the Securities Division of the Arizona Corporation
6 Commission (the "Division") with an initial Request for Information and Documents. The request
7 was made pursuant to and in compliance with both the administrative rules and the Arizona Rules
8 of Civil Procedure, which are both applicable to this proceeding. Moreover, the requests were
9 narrow in scope and reasonable. The Division has not produced a single sheet of paper in
10 response to the Respondents' requests.¹

11 To the contrary, the Division thumbed its nose at the requests and confirmed that it has no
12 interest in, or intentions of, affording the Respondents even the most basic due process rights. The
13 Division continues to use the distinction between the administrative rules and the Arizona Rules of
14 Civil Procedure as both a sword and a shield - - invoking the Rules of Civil Procedure when it
15 suits the Division, and excluding and/or avoiding the Rules of Civil Procedure when it does not.
16 Put another way, the Division wants to engage in trial by ambush and, in so doing, it is attempting
17 to rob the Respondents of due process and of the ability to effectively defend against the
18 Division's unmeritorious claims. Such conduct is wholly inconsistent with traditional notions of
19 fair play.

20 In light of the Securities Division's stance on discovery, it is clear that the only way the
21 Respondents will obtain some semblance of a fair trial, which necessarily involves basic
22 discovery, is for the Division to be ordered to produce the requested documents and information.
23 Therefore, the Respondents hereby request an order compelling the Division to produce the
24

25 ¹ The Division also has refused to answer the Respondents' outstanding Interrogatories, and has
26 rejected producing the documents and information requested by Respondents Michael Kelly, and
World Phantasy Tours.

1 requested documents or, alternatively, to vacate the Temporary Order to Cease and Desist.

2 **II.**
3 **THE ADMINISTRATIVE RULES AND THE ARIZONA RULES OF CIVIL**
4 **PROCEDURE PROVIDE FOR DISCOVERY WITHIN THE CONTEXT OF**
5 **ADMINISTRATIVE PROCEEDINGS.**

6 Respondents do not contest that administrative rules and statutes apply to this proceeding.
7 Moreover, in arguing that the Arizona Rules of Civil Procedure also apply, the Respondents are
8 not advocating that the Rules of Civil Procedure supercede the administrative rules. Rather, the
9 rules of Civil Procedure fill in the blanks, are instructive, and control where the administrative
10 rules and statutes do not explicitly regulate in a given area.

11 The first rule in the Arizona Rules of Practice and Procedure Before the Corporation
12 Commission (hereinafter "Commission Rules"), instructs that the Commission Rules shall govern
13 in all cases before the Corporation Commission. *See* R14-3-101(A). However, *this same rule*
14 provides:

15 . . . In all cases in which procedure is set forth neither by law, nor by these rules,
16 nor by regulations or orders of the Commission, the Rules of Civil Procedure for
17 the Superior Court of Arizona as established by the Supreme Court of the state of
18 Arizona shall govern . . . *Id.*

19 Thus, where the administrative rules do not explicitly regulate and/or provide the procedure for
20 how to operate before the Corporation Commission, the Administrative Law Judge or Hearing
21 Officer must look to Rules of Civil Procedure because they control.

22 **A. THE ADMINISTRATIVE RULES RELY ON THE ARIZONA RULES OF**
23 **CIVIL PROCEDURE TO PROVIDE THE FORMAT FOR HOW**
24 **DISCOVERY IS TO PROCEED IN ADMINISTRATIVE ACTIONS.**

25 The Division's representation that the Rules of Civil Procedure for discovery do not apply
26 in administrative proceedings is completely contradicted by the very administrative rules on which
the Division relies in refusing to comply with the Respondents' discovery requests. *See* Division's

1 Response to Respondents' Request for Documents and Information (hereinafter "Response") at p.
2 4, lines 4-8. As discussed above, R14-3-101(A) provides that where the rules of practice and
3 procedure do not provide the format for practice before the Corporation Commission, the
4 Administrative Law Judge and the parties should look to the Arizona Rules of Civil Procedure.

5 Importantly, there is a Commission Rule that addresses discovery, and it explicitly states
6 that the Arizona Rules of Civil Procedure *do apply* to discovery in administrative proceedings
7 before the Corporation Commission. Specifically, R14-3-109(P) addresses discovery in the form
8 of depositions, and provides: "The Commission, a Commissioner, *or any party* to a proceeding
9 before it may cause the deposition of a witness to be taken *in the manner prescribed by law and of*
10 *the civil procedure for the Superior Court of the state of Arizona.*" See R14-3-109(P)(emphasis
11 supplied).

12 This rule, which is the only rule that specifically addresses discovery under the
13 Commission Rules, indicates that discovery is allowed in administrative proceedings before the
14 Corporation Commission and, further, that the Commission defers to the Arizona Rules of Civil
15 Procedure to provide the format for how discovery should be undertaken by the parties.

16 Another relevant administrative rule that evidences the Corporation Commission's
17 adoption of the Arizona Rules of Civil Procedure is R14-3-106(K), which provides: "Motions
18 shall conform insofar as practicable with *the Rules of Civil Procedure for the Superior Court of*
19 *the state of Arizona.*" See R14-3-106(K)(emphasis supplied). Though this rule does not
20 specifically address how discovery practice is to be handled before the Corporation Commission,
21 it does provide that motion practice will follow the Arizona Rules of Civil Procedure and this, in
22 turn, impacts the discovery practice between the parties. Thus, it is evident that: (1) the
23 Commission Rules do provide for discovery; (2) the procedure for discovery before the
24 Corporation Commission is not exclusively regulated by the Commission Rules; and, most
25 importantly, (3) the Corporation Commission relies on the Arizona Rules of Civil Procedure to
26 provide the format for how discovery between the parties is to proceed.

1 The very rule that the Division cites in its Response to the Respondents' discovery requests
2 proves, not refutes, the Respondents' contention that discovery is permitted and that the Rules of
3 Civil Procedure provide the format for how discovery should be conducted. A.R.S. § 41-1062,
4 which addresses administrative procedure in adjudicative proceedings before the state
5 government, provides:

6 A. *Unless otherwise provided by law*, in contested cases the following shall
7 apply:

8 4. The officer presiding at the hearing *may* cause to be issued subpoenas for
9 the attendance of witnesses and for the production of books, records, documents
10 and other evidence and shall have the power to administer oaths. *Unless otherwise*
11 *provided by law or agency rule*, subpoenas so issued shall be served and, upon
12 application to the court by a party or the agency, enforced in the manner provided
13 by law for the service and enforcement of subpoenas *in a civil action . . .*
14 *Prehearing deposition and subpoenas for the production of document may be*
15 *ordered by the officer presiding at the hearing, provided that the party seeking*
16 *such discovery demonstrates that the party has reasonable need of the deposition*
17 *testimony or materials being sought . . .* Notwithstanding the provisions of 12-
18 2212, no subpoenas, depositions, or other discovery shall be permitted in contested
19 cases *except as provided by agency rule* or this paragraph. *See* A.R.S. § 41-
20 1062(A)(4)(emphasis supplied)(*see also* A.R.S. § 41-1092.07(F)(4) providing
21 uniform administrative hearing procedures in actions before the state
22 government)).

23 This statute does not refute that discovery is provided for in administrative proceedings, or
24 that the Arizona Rules of Civil Procedure do not apply in providing the format for how discovery
25 is to be undertaken in an administrative proceeding. At a bare minimum the statute provides the
26 hearing officer with one vehicle (the subpoena), out of many, by which to compel discovery
within the context of an administrative proceeding. Moreover, the rule once again refers to the
Rules of Civil Procedure to provide the format for compelling discovery if: (1) the administrative
rules do not already provide a discovery format, and (2) the hearing officer elects, in his or her
discretion, to compel compliance with the discovery request *via* subpoena.

Importantly, the statute begins by stating, "unless otherwise provided by law," and ends,

1 once again, by referring to other agency rules that address discovery - - “except as provided by
2 agency rule.” There is, as discussed above, a Commission Rule that provides for discovery in
3 actions before the Arizona Corporation Commission, and it explicitly provides: “The Commission,
4 a Commissioner, *or any party* to a proceeding before it may cause the deposition of a witness to
5 be taken *in the manner prescribed by law and of the civil procedure for the Superior Court of*
6 *the state of Arizona.*” See R14-3-109(P)(emphasis supplied).

7 There also is an explicit agency rule that provides the Corporation Commission’s standard
8 procedure for handling a situation where the administrative rules do not exclusively regulate the
9 practice procedure before the Corporation Commission: “. . . In all cases in which procedure is set
10 forth neither by law, nor by these rules, nor by regulations or orders of the Commission, the Rules
11 of Civil Procedure for the Superior Court of Arizona as established by the Superior Court of the
12 state of Arizona shall govern . . .” See R14-3-101(A).

13 **B. THE DIVISION HAS ACKNOWLEDGED THAT THE RULES OF CIVIL**
14 **PROCEDURE APPLY TO DISCOVERY IN THIS PROCEEDING.**

15 Lead counsel for the Division in this case, stated at the January 14, 2004 Prehearing
16 Conference:

17 Since the case is going to be extended for some time, *we would like to do*
18 *some type of formal discovery requests.* I know they’ve [the Respondents] been
19 saying we’ve [the Division] been indicating we’re going to do this for some time,
20 but we will try to get this out before March, and *hopefully they’ll comply.* See
21 January 14, 2004, Prehearing Conference transcript, at p. 28, lines 1-6 (emphasis
22 supplied).

23 The Division’s counsel further stated:

24 . . . Well, our proposal is that *the respondents produce all sale records*
25 involving Arizona investors of the universal lease through the year 2003 . . . *If the*
26 *respondents refuse to produce the records of 2003 showing the sales to Arizona,*
then we will be forced to go to the next level and, obviously, take the legal
remedies of the Superior Court that we need to take. *Id.* at p. 29, lines 7-10, and
16-20 (emphasis supplied).

1 Finally, the Division's counsel stated:

2 . . . We will be filing a request just for the 2003 sales records within the
3 next week, and we'll await their compliance with that request. If not, we'll move
4 forward [to the Superior Court]. And I just wanted to put that out so you know
5 what we'll be filing. *Id.* at pp. 29-30.

6 Yet, less than two months after the above referenced statements were made at the
7 Prehearing Conference on March 4, 2004, and after the Division's counsel allegedly claimed to
8 have received information that the Respondents are involved in a nation-wide ponzi scheme (a
9 claim that involves fraud allegations, but which has never been asserted in either the original or
10 amended Temporary Order to Cease and Desist), the Division completely changed its tune
11 regarding discovery in an administrative proceeding, stating:

12 The problem with the discovery that the respondents in this matter have
13 attempted to file with us is that they are following the civil rules of discovery, rules
14 that do not apply in this administrative forum. *See* March 4, 2004, Prehearing
15 transcript at p. 10, lines 19-22.

16 The Division is playing very loose with the facts and the law in using the distinction
17 between administrative rules and the Arizona Rules of Civil Procedure as both a sword and a
18 shield. When the Arizona Rules of Civil Procedure provided the Division with a vehicle to obtain
19 the discovery it claimed it desperately needed (but has not yet requested), the Division referenced
20 the Rules of Civil Procedure, and even threatened to take the Respondents to Superior Court to
21 compel compliance with a formal discovery request that the Division promised but failed to serve
22 on the Respondents. Conversely, when the Respondents requested basic documents and
23 information, the Division rejected the requests and advocated that the Respondents are not entitled
24 to discovery *under the administrative rules*. The Division's conduct tramples the Respondents'
25 due process rights, makes a mockery of traditional notions of fair play and, if allowed to continue,
26 will effectively deprive the Respondents of the ability to defend themselves at Hearing.

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III.
RESPONDENTS ARE ENTITLED TO DUE PROCESS.

“A fair trial in a fair tribunal is a basic requirement of due process.” *Withrow et al., v. Larkin*, 421 U.S. 35, 46 (1975)(quoting *In re Murchison*, 349 U.S. 133, 136 (1955)). “This applies to administrative agencies which adjudicate as well as to courts.” *Id.* (citing *Gibson v. Berryhill*, 411 U.S. 564, 579 (1973)(see also *Richardson v. Perales*, 402 U.S. 389, 401 (1971)(procedural due process is applicable and mandatory to the adjudicative administrative proceeding)). Thus, the Respondents are entitled to a fair trial and due process.

A. BASIC DUE PROCESS INVOLVES THE EXCHANGE OF DISCOVERY.

The United States Supreme Court established prerequisites for a fair hearing:

[t]he right to a hearing embraces not only the right to present evidence, **but also a reasonable opportunity to know the claims of the opposing party and to meet them.** The right to submit arguments implies that opportunity; otherwise the right may be but a barren one. Those who are brought into contest with the Government in a quasi-judicial proceeding aimed at the control of their activities **are entitled to be fairly advised of what the Government proposes** and to be heard upon its proposals before it issues its final command.” *Morgan v. United States*, 304 U.S. 1, 18 (1938) (emphasis added).

The Division is attempting to engage in litigation by ambush. By refusing to produce any of the requested documents and information, the Division is preventing the Respondents from the opportunity, must less a reasonable opportunity, to be apprised of the claims that the Division is making against them. The Division continued their ambush tactics in the last Prehearing Conference, when the Division claimed: “We have in our possession evidence to suggest that this is a *Ponzi scheme* on a national level, and because of this, we want to push the hearing as quickly as possible and get a quick resolution in light of the evidence we have in our possession showing what this program in fact is.” See March 4, 2004, Prehearing Conference transcript at p. 5, lines 4-9. Neither the Original Temporary Order to Cease and Desist nor the Amended Temporary Order to Cease and Desist alleged that a Ponzi scheme, at any level, was involved.

1 The Division was trying to end-run another claim into this proceeding without leave of the
2 presiding officer herein, as is required by R14-3-106(E). This is exactly the type of behavior that
3 the due process notice requirements are designed to prevent, and this is why discovery is
4 necessarily intertwined with parties' due process rights.

5 Additionally, the Division has been making misrepresentations to this Court. At the March
6 4, 2004, Prehearing Conference, the Division stated:

7 . . . there has been at least eight and probably more securities divisions
8 across the country that have issued rulings against the respondents in this case.
9 Clearly, they [the other securities divisions] have found it [the Universal Lease] to
10 be a security, and we intend to prove it is a security. We have evidence to that
11 effect. *See* March 4, 2004 Prehearing Conference transcript at p. 24, lines 9-14.

12 After this Court forced the Division to turn over public records relating to these
13 allegations, it became evident that the Division's representation was completely inaccurate.² The
14 Division's inaccuracies have already prejudiced the Respondents in this proceeding, and they
15 further support the need for this Court to issue an order compelling the Division to produce the
16 requested documents and information.

17 A mere exchange of witness and exhibit lists 30 or 60 days before a hearing will not afford
18 the Respondents sufficient time and/or opportunity to prepare a defense in this matter. Moreover,
19 the Division will only list those witnesses and exhibits that tend to support its unmeritorious claim
20 - - there will be no production of exculpatory evidence without an order by this Court compelling
21 the Division to produce the requested information. Therefore, an order compelling discovery is
22 the only way to balance the playing field and to ensure a fair hearing and due process.

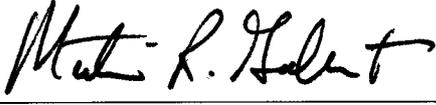
23 **B. THE DIVISION IS CAUSING THE DELAY IN THIS PROCEEDING.**

24 The Respondents have tried to push this action along by making themselves
25 available for Division EUOs, attempting to cross-notice the deposition of one of the witnesses the
26 Respondents are aware of, filing discovery requests and interrogatories, and the like. The

² *See* Respondents Motion for Sanctions.

1 Dated this 18th day of March, 2004.

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4 By 
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1 ORIGINAL and 13 copies of the foregoing
2 hand-delivered this 18th day of March, 2004 to:

3 Docket Control
4 Arizona Corporation Commission
5 1200 West Washington Street
6 Phoenix, Arizona 85007

7 COPY of the foregoing hand-delivered
8 this 18th day of March, 2004 to:

9 Honorable Marc Stern
10 Administrative Law Judge
11 Hearing Division
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