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2003 APR -8 P 3: 35

Arizona Corporation Commission

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MARC SPITZER, Chairman
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In the matter of:)
)
WESLEY KARBAN WYATT, et ux., et al.)
c/o Harry N. Stone, Esq.)
3030 North Third Street)
Phoenix, Arizona 85012,)
)
Respondents.)

DOCKET NO. S-03529A-03-0000
**RESPONSE TO MOTION TO
QUASH SUBPOENA DUCES TECUM
AND TO WES WYATT'S NOTICE
OF PRIVILEGE PURSUANT TO
A.R.S. § 41-1066**

The Securities Division ("Division") of the Arizona Corporation Commission ("ACC"), pursuant to the Hearing Officer's Procedural Order in this matter, responds to the Motion to Quash Subpoena Duces Tecum ("Motion to Quash") filed by counsel for Respondent Wesley Karban Wyatt ("Wyatt"). The grounds asserted for quashing the subpoena are baseless and overstated. The subpoena seeks relevant information from a target of a Division investigation, is within the scope of the Division's authority, and is a proper exercise of the Division's investigatory powers tailored to the particular issues in this case. As a result, instead of quashing the subpoena, the Hearing Officer should order Respondents to comply with the subpoena or to state with particularity any claims of privilege that may prevent them from complying.

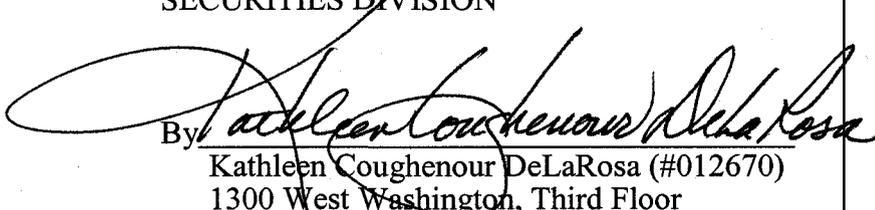
The Division also responds to Wyatt's Notice of Privilege Pursuant to A.R.S. § 41-1066, ("Notice of Privilege") and asserts that Wyatt interprets the privilege too broadly, and that some records sought by the Commission may not be within the scope of the privilege.

This response is supported by the record in this matter, and by the following Memorandum of Points and Authorities.

...

1 RESPECTFULLY SUBMITTED this 8th day of April, 2003.

2 ARIZONA CORPORATION COMMISSION
3 SECURITIES DIVISION

4 By 
5 Kathleen Coughenour DeLaRosa (#012670)
6 1300 West Washington, Third Floor
7 Phoenix, Arizona 85007
8 Attorneys for Arizona Corporation Commission

9 **MEMORANDUM OF POINTS AND AUTHORITIES**

10 **I. BACKGROUND.**

11 This case parallels a number of other pending cases against individuals and entities who
12 were involved in selling unregistered investment contracts involving pay telephone sale and
13 leaseback arrangements with Alpha Telecom, Inc. (the "Alpha investment contracts"). See Docket
14 Nos. S-03506A-02-0000, S-03507A-02-0000, S-03508A-02-0000, S-03509A-02-0000, and
15 S-03510A-02-0000. In March, 2003, the Division filed and served a Notice of Opportunity for
16 Hearing Regarding Proposed Order to Cease and Desist, for Restitution, for Administrative
17 Penalties, and for Other Affirmative Action ("Notice") in this matter, detailing the facts on which
18 its case against Wyatt is based.¹

19 The requests contained in the subpoena at issue were tailored to elicit responsive
20 documents that would be relevant to the Division's investigation and to the Alpha investment
21 contracts, requesting only information on pay telephone investment contracts "with which any of
22 the [subpoenaed] persons or entities have been associated or affiliated or in which any of the
23 [subpoenaed] persons or entities have any financial interest" (Subpoena, Exhibit "A",
24 attached to Motion to Quash).

25 Nevertheless, Respondents assert that the Hearing Officer should quash the subpoena as
26 overly broad, outside the scope of the Commission's investigatory authority, seeking documents

¹ That Notice is virtually identical to the Notices of Opportunity for Hearing filed in the related actions listed above, since all are based on similar facts, except for the separate sales activities of each individual or entity named.

1 neither relevant nor material to a pending investigation, seeking personal records from persons not
2 the subject of an investigation, seeking financial records without articulating specific grounds for
3 suspicion of liability, burdensome, and an “improper fishing expedition.” These objections are
4 without any reasonable basis in fact or law, and should be rejected.

5 **II. LEGAL ARGUMENT.**

6 **A. The Information Sought by the Division’s Subpoena Is Well Within the**
7 **Investigatory Power of the Commission.**

8 The inherent investigation powers of the Commission are established in the Arizona
9 Constitution, which provides that the Commission

10 shall have power to inspect and investigate the property, books,
11 papers, business, methods, and affairs of any corporation whose
12 stock shall be offered for sale to the public and of any public service
13 corporation doing business within the State, . . . ***shall have the power***
of a court of general jurisdiction to enforce the attendance of
witnesses and ***the production of evidence by subpoena***, . . . which
said power shall extend throughout the State. . . .

14 Ariz. Const. art. 15 sec. 4 (emphasis added). Although the Commission’s constitutional power
15 over the sale of securities is limited to the power to inspect and investigate, the legislature may
16 enlarge or extend the Commission’s powers over the same or similar subject matter. *Commercial*
17 *Life Ins. Co. v. Wright*, 64 Ariz. 129, 140, 166 P.2d 943, 950 (1946); *see also* Ariz. Const. art. 15
18 sec. 5.

19 Pursuant to that authority, the legislature has given the Commission extensive powers to
20 regulate the offer and sale of securities in Arizona. *See generally* Arizona Securities Act
21 (“Securities Act”), A.R.S. §§ 44-1801 through 44-2126. Included in the Securities Act are
22 provisions expressly authorizing just the type of investigation and document request the Division
23 made in this case. *E.g.*, A.R.S. §§ 44-1822 (investigations), 44-1823(A) (power to require
24 testimony and production of documents in connection with investigations and hearings).
25 Moreover, the Constitution and the legislature also have given the Commission the power to enact
26 rules and regulations necessary for enforcing the Securities Act. Ariz. Const. art. 15 sec. 6; A.R.S.

1 § 44-1821(A). Pursuant to that authority, the Commission has promulgated rules dealing with
2 subpoenas, subpoena enforcement, and the rights of witnesses subpoenaed to appear for
3 examination and produce documents and records. Ariz. Admin. Code R14-3-109(O), R14-4-304.

4 The subpoena in this case was issued in aid of a commission investigation, as authorized by
5 the Arizona Constitution, and the statutes and rules applicable to investigations and actions by the
6 Division. As such, it is not *ultra vires*, as Respondent seems to allege. Instead, it is well within
7 the Division's legal authority.

8 **B. The Subpoena Seeks Relevant Documents from a Target of a Division**
9 **Investigation, and Is Sufficiently Specific in Its Requests.**

10 The Arizona Court of Appeals reviewed a challenge to a similar Division subpoena in
11 *Carrington v. Arizona Corporation Commission*, 199 Ariz. 303, 18 P.3d 97 (App. 2000) (copy of
12 Exhibit "A" to Carrington subpoena attached hereto as Exhibit "A"). The Respondents in that
13 action challenged the Division subpoena as outside the Division's authority, vague, seeking
14 irrelevant information, and served for an improper purpose, and claimed the Division was acting
15 without any reasonable basis (*see* 199 Ariz. at 304 ¶ 4, 18 P.3d at 98)—claims similar to those
16 made by the Respondent in this case. Respondents took a special action to the Superior Court,
17 which rejected those challenges. *Id.* They then appealed to the Court of Appeals. *Id.*

18 The appellate court reviewed the Commission's power to conduct investigations pursuant
19 to the Arizona Constitution and the Securities Act, and acknowledged that "courts give the
20 Commission 'wide berth' when they review the validity of Commission investigations." *Id.* at 99
21 ¶ 8, 18 P.3d at 99).

22 In fact, "[a]n appropriately empowered agency 'can investigate
23 merely on suspicion that the law is being violated, or even just
24 because it wants assurance that it is not.'" In other words, "[t]he
25 Commission must be free without interference or delay to conduct an
26 investigation which will adequately develop a factual basis for a
determination as to whether particular activities come within the
Commission's regulatory authority."

Id. (citations omitted).

1 The appellant in *Carrington* argued that the Commission subpoena was invalid, in part,
2 because a federal court had determined that certain similar investments were not securities under
3 federal law. *Id.* ¶¶ 9, 10. The court responded by first pointing out that Arizona courts are not
4 bound by federal courts' interpretations of federal securities law. *Id.* at ¶ 10. In any case,
5 concluded the court, "even if the [federal] holding . . . was deemed to be the law in Arizona, the
6 Commission still would have the authority to subpoena information . . . to determine whether . . .
7 there is some material difference that would indicate that Carrington's transactions are securities
8 that fall within Arizona's act." *Id.* at 305-306 ¶ 11, 18 P.3d at 99-100.

9 In this case, the Division is conducting a similar investigation of the offer and sale of
10 certain pay telephone sale and leaseback contracts that have been held to be securities in a number
11 of other states and under federal law. *See* Notice, ¶¶ 6, 7, and actions cited therein. The Division
12 plainly has the authority to investigate whether Wyatt's actions fall within the proscriptions of the
13 Securities Act.

14 An administrative agency's subpoena carries with it a presumption that it was issued
15 legally, in good faith, and under proper authority for a proper purpose. *E.g., Shulansky v.*
16 *Cambridge-Newport Fin. Servs. Corp.*, 623 A.2d 1078, 1081 (Conn. Super. 1992).

17 In light of the presumption that the administrative subpoenas were
18 issued for a proper purpose, the burden is shifted to the defendant to
19 prove affirmatively that there was an improper purpose in issuing
20 them. The defendant must make a prima facie case through a
21 showing of independent evidence that the purpose behind the
issuance of the subpoenas was improper, i.e., that the subpoenas were
issued in order to harass or punish, rather than to gain information
relevant to the investigation.

22 *Id.* Wyatt has presented no such affirmative evidence. He has simply asserted, without any
23 evidence at all, that the Division's subpoena was improper. His claim must be rejected.

24 Moreover, to the extent Wyatt is interpreting the subpoena to request documents unrelated
25 to activities within Arizona, the Division is certainly willing to limit production to documents that
26 are relevant to Wyatt's activities within or from Arizona. The Notice in this case is limited to

1 offers and sales within or from Arizona, and it is not the Division's intent to make its subpoena any
2 broader than necessary to obtain information directly relevant to the claims included in the Notice.

3 As a result, the Division requests the Hearing Officer to deny the motion to quash, and to
4 require the Respondent to produce the records sought in the subpoena.

5 **C. The Respondent's Assertion of the Privilege Against Self-Incrimination Is**
6 **Overly Broad, and Does Not Apply to All the Information the Division Seeks.**

7 The Notice of Privilege asserts that "*any testimony* requested from Mr. Wyatt by the
8 Commission will be compelled testimony that may tend to incriminate him" Notice of
9 Privilege, (1) (emphasis added). Wyatt also asserts that "any documents requested to be produced
10 . . . are Mr. Wyatt's private papers." *Id.*, (2). The Division contends this assertion of the privilege
11 is overly broad, and does not apply to all the information the Division seeks. The privilege does
12 not apply to the documents of a collective entity. Furthermore, the privilege does not apply even to
13 personal documents absent a showing of a reasonable risk that the contents of the documents will
14 actually incriminate the party asserting the privilege.

15 Certainly a respondent in an administrative action has the right to assert his constitutional
16 right against compelled self-incrimination. *E.g., Application of Gault*, 387 U.S. 1, 47, 49 (1967).
17 A party who asserts the privilege against self-incrimination, however, must "show a 'real danger',
18 and not a 'mere imaginary possibility' of prosecution." *Thoresen v. Superior Ct. in and for*
19 *Maricopa Cty.*, 11 Ariz. App. 62, 66, 461 P.2d 706, 710 (1969). "The Fifth Amendment privilege
20 . . . does not prevent the asking of potentially incriminating questions, and it cannot be claimed in
21 advance of questions actually propounded." *Id.* at 66-67, 461 P.2d at 710-711 (citations omitted).
22 With respect to financial records, the party opposing discovery must make a "realistic showing of
23 possible jeopardy." *See id.* at 67, 461 P.2d at 711. Indeed, the *Thoresen* court noted a case that
24 involved a "comprehensive examination into the financial affairs of a judgment debtor," stating:

25 [T]he court was unable to find a realistic basis for a claim of
26 privilege against self-incrimination notwithstanding the judgment
debtor's recent indictment by a federal grand jury and the
investigation of his business affairs by various agencies with a view

toward possible prosecution.

1 *Id.* at 68, 461 P.2d at 712, *citing Kirtley v. Abrams*, 184 F. Supp. 65 (E.D.N.Y. 1960). Wyatt's
2 blanket assertion of the privilege against self-incrimination, without more, thus does not justify his
3 failure to produce records responsive to the subpoena, nor does it excuse his failure to provide any
4 testimony whatever at his examination under oath.

5 Moreover, Wyatt's blanket assertion of privilege as to the business records sought by the
6 Division's subpoena, without more, is unjustified. "Whatever limits there may be as to
7 [legislative] power to provide for the production of corporate or other business records, however,
8 they are not to be found . . . in any such absolute or universal immunity as petitioners seek."
9 *Oklahoma Press Pub. Co. v. Walling*, 327 U.S. 186, 208 (1946). Subpoenaed business records are
10 not privileged. *United States v. Doe*, 465 U.S. 605 (1984); *Fisher v. United States*, 425 U.S. 391
11 (1976). Moreover, artificial entities are not protected by the personal privilege of the Fifth
12 Amendment. *Bellis v. United States*, 417 U.S. 85 (1974).

13 The "collective entity rule" was first articulated in *Hale v. Henkel*, 201 U.S. 43 (1906),
14 which established that corporate books and records are not "private papers" protected by the Fifth
15 Amendment privilege against self-incrimination. The Supreme Court subsequently established that
16 a corporate officer could not resist a subpoena for corporate records by invoking his personal
17 privilege. *Wilson v. United States*, 221 U.S. 361 (1911). A labor union is a collective entity that is
18 not protected by the Fifth Amendment, *United States v. White*, 322 U.S. 694 (1944), and a partner
19 in a small partnership cannot properly invoke the privilege to avoid producing partnership records,
20 *Bellis v. United States*, 417 U.S. 85 (1974).

21 The plain mandate of these decisions is that without regard to
22 whether the subpoena is addressed to the [collective entity] or . . . to
23 the individual in his capacity as custodian . . . a [collective entity]
24 custodian . . . may not resist a subpoena for [collective entity] records
25 on Fifth Amendment grounds.

26 *Braswell v. United States*, 487 U.S. 99, 108-109 (1988). Although *Doe* may require that a sole
proprietor be provided the opportunity to show that his act of production would entail testimonial
self-incrimination, if the records are those of a collective entity, the Fifth Amendment does not

1 protect against compelled production.

2 In this case, it is unclear whether or not The Financial Greenhouse, or OMAC, or any other
3 entity named by the subpoena, is a collective entity. The Division has information suggesting the
4 entity is a limited liability company, but Wyatt asserts that the papers sought by the subpoena are
5 his personal and private papers. A party that holds itself out as a corporation will not be permitted
6 to deny its corporate existence. *See Charles Erlich & Co. v. J. Ellis Slater Co.*, 192 P. 526 (Cal.
7 1920). A similar principle would logically apply to any other collective entity. Therefore, if any of
8 the subpoenaed entities held themselves out as a collective entity—a corporation, a partnership, or
9 a limited liability company—that entity's records should not be protected by the personal privilege
10 against testimonial self-incrimination.

11 Since Wyatt has placed no evidence before the Commission to give it a basis for deciding
12 whether the privilege may apply to the documents sought by the Division's subpoena, his assertion
13 of the privilege against self-incrimination should be examined and limited. If he can demonstrate
14 that his testimony will entail a reasonable risk of prosecution, he may be able to assert the privilege
15 as to testimonial matters. With respect to the documents sought by the Division's subpoena,
16 however, to the extent they are business records, and/or to the extent the records may be those of
17 one or more collective entities, Wyatt should be required to produce them.

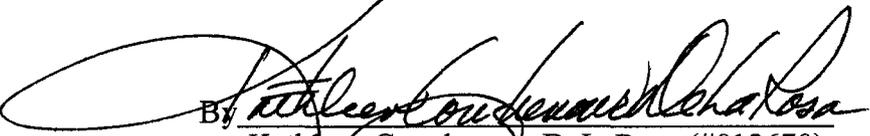
18 **III. CONCLUSION.**

19 Neither Wyatt's Motion to Quash nor his blanket assertion of a privilege against self-
20 incrimination as to all testimony and documents sought by the Division is well-founded. The
21 Division's subpoena is a proper exercise of the Division's investigatory and enforcement powers,
22 seeking relevant information regarding a possible violation of the Securities Act. Wyatt has given
23 no reasonable basis on which the Commission should quash that subpoena. He likewise has utterly
24 failed to provide any support for his assertion of the privilege against self-incrimination as to every
25 question that might be asked or every document sought by the Division. As a result, the
26 Commission should deny his Motion to Quash and require him to either establish the privilege with

1 reasonable certainty or provide testimony and documents pursuant to the subpoena.

2 RESPECTFULLY SUBMITTED this 8th day of April, 2003.

3 ARIZONA CORPORATION COMMISSION
4 SECURITIES DIVISION

5
6 By 
7 Kathleen Coughenour DeLaRosa (#012670)
8 1300 West Washington, Third Floor
9 Phoenix, Arizona 85007
10 Attorney for Arizona Corporation Commission

11 COPY of the foregoing
12 mailed/delivered this 8th
13 day of April, 2003, to:

14 Harry N. Stone, Esq.
15 3030 North Third Street
16 Phoenix, Arizona 85012
17 Attorney for Respondents

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