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FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT, Complainant, v. RESPONDENT Respondent.	Disciplinary Proceeding No. 2012033393401 Hearing Officer–RES

ORDER GRANTING IN PART AND DENYING IN PART RESPONDENT MOTION IN LIMINE TO EXCLUDE THE TESTIMONY OF KA, BS, AND MC

I. Introduction

The Department of Enforcement ("Enforcement") brings this matter against Respondent alleging five causes of action. The first two concern Respondent's alleged failure to disclose to his employer firm that he was a successor trustee and beneficiary of a living trust established by EC, one of his brokerage customers. According to the first cause of action, Respondent's alleged failure to disclose these facts violated NASD Rule 2110 and FINRA Rule 2010. According to the second cause of action, Respondent violated FINRA Rules 3270 and 2010 by not disclosing to his employer firm his expectation of compensation from an outside business activity as a result of his position as successor trustee of EC's trust.[1]

II. Respondent's Motion To Exclude Witnesses

Enforcement filed its Witness List in this matter on December 23, 2015. The Witness List included KA, MC, BS, and others as proposed witnesses. Enforcement proffers the testimony of KA, MC, and BS to support its causes of action concerning EC. According to Enforcement's Witness List, each witness "is expected to testify about matters alleged in the Complaint, Respondent's defenses, and her relationship with [EC]." Enforcement included in its Exhibit List the depositions of KA and BS taken in probate litigation, described in more detail below, and averred that their deposition testimony "[s]hows conflict of interest regarding Respondent's role."

[1] The other three causes of action concern Respondent alleged conduct with respect to a different firm customer, KM. These causes of action are not relevant to this Order, and further discussion about them is not necessary.

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On January 13, 2016, Respondent filed a motion in limine seeking to exclude KA, MC, and BS as witnesses ("Motion"), on the ground that their testimony is not relevant.[2] Enforcement opposed Respondent's Motion ("Opposition"), contending that "the testimony of all three witnesses is relevant to the sanctions determination and to the issue of whether the Respondent violated FINRA Rule 2010 and NASD Rule 2110 by engaging in unethical conduct." For the reasons stated below, the Motion is granted in part and denied in part.

III. Discussion

Motions in limine seeking to exclude broad categories of evidence are disfavored.[3] A court (or Hearing Officer) should grant such motions only if the evidence at issue "is clearly inadmissible for any purpose."[4] This is a high standard. "[A] court is almost always better situated during the actual trial to assess the value and utility of evidence."[5]

On the other hand, when they meet the standard, motions in limine "permit[] the trial judge to eliminate from further consideration evidentiary submissions that clearly ought not to be presented to the [finder of fact] because they clearly would be inadmissible for any purpose."[6] Such motions "serve important gatekeeping functions by allowing the trial judge to eliminate from consideration evidence that should not be presented to the [finder of fact]."[7]

FINRA Rule 9263(a) provides as follows: "The Hearing Officer shall receive relevant evidence, and may exclude all evidence that is irrelevant, immaterial, unduly repetitious, or unduly prejudicial." The Federal Rules of Evidence define evidence as relevant if "(a) it has any tendency to make a fact more or less probable than it would be without the evidence; and (b) the fact is of consequence in determining the action."[8] As Enforcement points out in its Opposition, the "standard of relevance established by the Federal Rules of Evidence is not high."

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[2] Amde filed an objection to the introduction of the KA and BS depositions as well as other proposed hearing exhibits. That objection will be dealt with in a separate order.

[3] *Sperberg v. Goodyear Tire & Rubber Co.*, 519 F.2d 708, 712 (6th Cir. 1975).

[4] *Miller UK Ltd. v. Caterpillar, Inc.*, 2015 U.S. Dist. LEXIS 156874, at *5 (N.D. Ill. Nov. 20, 2015) (quoting *Noble v. Sheahan*, 116 F. Supp. 2d 966, 969 (N.D. Ill. 2000)); *Brock v. Harrison*, 2015 U.S. Dist. LEXIS 155242, at *4 (S.D. Ohio Nov. 17, 2015); *Wright v. Best Recovery Services LLC*, 2015 U.S. Dist. LEXIS 145212, at *3 (E.D. Mich. Oct. 27, 2015).

[5] *Wilkins v. Kmart Corp.*, 487 F. Supp. 2d 1216, 1218-19 (D. Kan. 2007).

[6] *Jonasson v. Lutheran Child & Family Services*, 115 F.3d 436, 440 (7th Cir. 1997). *Accord Walsh v. United States*, 2009 U.S. Dist. LEXIS 27238, at *4 (N.D. Okla. Mar. 31, 2009) ("The motion in limine allows the Court to decide evidentiary issues in advance of trial thereby avoiding delay and ensuring an evenhanded and expeditious trial.").

[7] *United States v. Verges*, 2014 U.S. Dist. LEXIS 17969, at *6 (E.D. Va. Feb. 12, 2014).

[8] Fed. R. Evid. 401. The formal rules of evidence do not apply in FINRA disciplinary proceedings. FINRA Rule 9145(a). However, the Federal Rules of Evidence are instructive for a FINRA Hearing Officer deciding an evidentiary motion. *Dep't of Mkt. Regulation v. Respondent*, OHO Order 15-11 (20090174025-02), 2015 FINRA Discip. LEXIS 41, at *2 (OHO Aug. 19, 2015).

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A. Relevance As To Liability

This Order is informed by the decision of the National Adjudicatory Council in *Department of Enforcement v. Butler*.[9] There, Enforcement filed a five-cause complaint alleging that Respondent Butler converted customer funds in violation of FINRA Rule 2010. Among other things, the customer's age (77 years old), her declining mental health, her difficulty taking care of her finances, and Butler's ill-gotten gains were relevant to the liability issue of whether Butler was liable for conversion.[10] Such factors were also relevant to the issue of the appropriate sanctions for such misconduct.[11]

In contrast to *Butler*, in this matter Enforcement does not allege that Respondent converted customer funds. Nor does Enforcement charge that Respondent violated FINRA Rule 2010 or NASD Rule 2110 by exercising undue influence over EC. Instead, the principal allegations of the first and second causes of action are that Respondent did not disclose to his employer firm his positions as successor trustee and beneficiary of the EC trust. The pleadings, the papers for and against summary disposition, and the pre-hearing briefs indicate that the facts of consequence to the determination of these causes of action are:

- Whether the position of successor trustee of EC's trust was a fiduciary position that Respondent was required to disclose to his employer firm pursuant to the firm's written supervisory procedures.

- Whether Respondent himself interpreted his employer firm's procedures as requiring disclosure of his position as successor trustee.

- Whether EC's advanced age (93 years plus) caused Respondent to have a reasonable expectation that her death was imminent and that he would thereafter receive compensation as trustee, bringing his position as successor trustee within the definition of outside business activity in FINRA Rule 3270.

- Whether a Trustee Certification of Investment Powers, submitted to Respondent's employer firm at the time EC opened a brokerage account in the trust's name, and which disclosed Respondent to be the successor trustee, was sufficient notice to the firm of Respondent's position as successor trustee.

- Whether naming Respondent and his wife as 100 percent beneficiaries of the trust's assets was a gift that Respondent had to disclose to his employer firm pursuant to the firm's written supervisory procedures.

[9] No. 2012032950101, 2015 FINRA Discip. LEXIS 35 (NAC Sept. 25, 2015), *appeal docketed*, No. 3-16912 (SEC Oct. 20, 2015).

[10] 2015 FINRA Discip. LEXIS 35, at *3-7.

[11] *Id*. at *28-29.

- Whether EC's right to change the designated beneficiaries of the trust meant that the beneficiary designation was not a gift.

- Whether Respondent knew that he and his wife were named as beneficiaries of the trust.

With one exception, discussed in Section III.C. below, it is very difficult to see how the testimony of KA, MC, or BS would make the existence of any of these consequential facts more or less probable. According to Enforcement's Opposition,[12] KA was a friend and next-door neighbor of EC. MC was EC's great-niece. BS was a friend and neighbor of EC, living two doors away from EC.[13] These proposed witnesses were not employees of Respondent's employer firm, and they have no personal knowledge of its written supervisory procedures or Respondent's disclosure obligations. They also have no knowledge whether the firm considered the position of successor trustee to be a fiduciary position that Respondent was required to disclose. And they have no knowledge of whether being named as a beneficiary to a trust was a gift that Respondent had to disclose. To say, as Enforcement does in its Witness List and Exhibit List, that each of the proffered witnesses "is expected to testify about matters alleged in the Complaint, Respondent's defenses, and her relationship with [EC]," and that their testimony "[s]hows conflict of interest regarding Respondent's role," is not sufficient to establish that the testimony would make any of the consequential facts as to Respondent's disclosure obligations more or less probable. The testimony of KA, MC, and BS is not relevant.

FINRA Rule 9263(a) provides that the Hearing Officer "may exclude all evidence that is . . . unduly repetitious or unduly prejudicial." Along similar lines, the Federal Rules of Evidence provide that a court may exclude relevant evidence "if its probative value is substantially outweighed by a danger of one or more of the following: unfair prejudice, confusing the issues, misleading the jury, undue delay, wasting time, or needlessly presenting cumulative evidence."[14]

Any probative value that the testimony of KA, MC, and BS might have is outweighed by the danger that it would be unduly prejudicial and confuse the issues. The testimony would inject into the hearing confusing, extraneous matters concerning an amendment to EC's trust, executed in July 2011, which named Respondent and his wife as 100 percent beneficiaries of the trust's assets, and whether Respondent exercised undue influence over EC to procure that amendment.[15] Two months after EC's death, the Attorney General for the State of Michigan filed in Probate Court an Objection to a petition to dissolve the trust and distribute the assets to Respondent and

[12] Any factual statements in this Order reflect representations made in the Opposition, the Complaint, and documents that Enforcement proposes as hearing exhibits. For purposes of deciding the Motion, the Hearing Officer interprets the facts and inferences in the light most favorable to Enforcement. The factual statements herein are for the purpose of deciding the relevance of the witnesses proffered by Enforcement only and do not constitute findings of fact for the purposes of deciding liability or sanctions, if any.

[13] KA lived in the house between EC and BS.

[14] Fed. R. Evid. 403.

[15] EC was 94 years old at the time of the amendment.

his wife.[16] On June 20, 2013, MC filed a petition to void the trust amendment. Probate litigation ensued. On November 19, 2013, the litigants agreed to a mediated settlement in which the Respondents, KA, MC, BS, and others divided the trust assets among themselves.[17] The principal allegation in the probate litigation was that Respondent and his wife had exerted undue influence to induce EC to sign the trust amendment.[18]

The highly contested circumstances of the trust amendment, if presented at the hearing, would distract the Hearing Panel from the principal allegation of the first and second causes of action, which is that Respondent allegedly violated a duty of disclosure to his employer firm regarding his positions as successor trustee and trust beneficiary. Furthermore, KA, MC, and BS themselves were trust beneficiaries who were displaced by Respondent and his wife. The proffered witnesses therefore had a personal financial stake in the outcome of the probate litigation. They would be subject to extensive cross-examination about whether they bear an animus toward Respondent and have their own agenda for testifying against him.[19] Additionally, the proffered testimony would be unduly repetitious, in that three witnesses would testify to the same matters when one, at most, would suffice.

In its Opposition, Enforcement contends that the testimony of KA, MC, and BS is relevant because it goes to the issue of Respondent's alleged undue influence over EC which, it contends, was in violation of the high standards of commercial honor and just and equitable principles of trade required by NASD Rule 2110 and FINRA Rule 2010. This argument misapprehends the nature of the first and second causes of action. Unlike *Butler*, the Complaint here does not allege that Respondent's alleged undue influence violated high standards of commercial honor and just and equitable principles of trade, but that his alleged failure to disclose his fiduciary position and beneficiary status violated such standards and principles. Broadening the scope of the hearing at this juncture to include generalized charges of unethical conduct that Enforcement failed specifically to charge in the Complaint would be prejudicial to Respondent and would confuse the issues which, in the first and second causes of action, are focused on Respondent's alleged disclosure obligations. The testimony of KA, MC, and BS is not relevant to those obligations, and its probative value is substantially outweighed by the danger of undue prejudice, undue repetition, and confusing the issues.

B. Relevance As To Sanctions

The testimony of KA, MC, and BS is not relevant or probative as to sanctions. In its pre-hearing brief, Enforcement relies on the following considerations in the Sanction Guidelines:

[16] Complaint ¶ 30. An amendment to the trust executed in January 2012 changed the successor trustee from Amde to Respondent wife. *Id.* ¶ 25.

[17] *Id.* ¶ 33.

[18] *Id.* ¶ 30.

[19] The depositions of KA and BS in the probate litigation indicate that they also had an animus toward each other and that MC rarely visited her great-aunt EC – additional subjects of distracting and unproductive cross-examination.

- Whether the outside activity involved customers of the employer firm.[20]
- Whether the activity resulted directly or indirectly in injury to customers of the firm or other parties.[21]
- The duration of the outside activity.[22]
- Whether the respondent concealed or misled the firm about the existence of the activity.[23]
- Whether the respondent obtained ill-gotten gains as a result of the activity.[24]

The matters underlying these considerations are either not disputed or are outside of KA, MC, and BS's personal knowledge: (1) Respondent's alleged conduct involved a customer of the employer firm; (2) Respondent was a successor trustee for more than four years from September 11, 2008, when EC opened a brokerage account in the trust's name at the firm, to 2013, when the account was transferred to another firm; (3) up to November 2011, Respondent did not disclose to the firm his positions as successor trustee and trust beneficiary on the firm's annual compliance questionnaires; (4) Respondent and his wife received real property and cash with a combined value of $382,023 as a result of the settlement of the probate litigation and the dissolution of the trust; and (5) if the employer firm did not know of Respondent's positions as successor trustee and trust beneficiary, it did not have the ability to supervise him with respect to those positions.[25] The testimony of KA, MC, and BS would add little, if anything, to these matters.

Enforcement also relies on the allegation that Respondent "advantaged himself over a highly vulnerable customer of advanced age (over 90) with declining mental and physical capacities."[26] This allegation does not make the testimony of KA, MC, or BS either relevant or probative. Unlike *Butler*, herein Enforcement neither alleges a cause of action that Respondent converted assets or funds from EC's trust nor that he acted unethically by exerting undue influence over EC.[27] Enforcement limits its claims to Respondent's alleged failure to disclose to

[20] FINRA Sanction Guidelines ("Guidelines") at 13 (2015), http://www.finra.org/sanction-guidelines.

[21] Guidelines at 6 (Principal Consideration No. 11).

[22] Guidelines at 6 (Principal Consideration No. 9).

[23] Guidelines at 6 (Principal Consideration No. 10).

[24] Guidelines at 7 (Principal Consideration No. 17).

[25] The parties have stipulated to a number of these matters. Joint Stipulations ("Stip.") ¶¶ 8, 10; Supplemental Stipulations ¶¶ 1, 2.

[26] Enforcement Pre-Hearing Brief at 20. *Accord id.* at 1 (Amde allegedly "placed his interests and advantaged himself over the vulnerable – in the first instance, his elderly customer suffering from dementia and declining health.").

[27] *Cf. Butler*, 2015 FINRA Discip. LEXIS 35, at *1, 3, 27.

his employer firm his positions as successor trustee and trust beneficiary. Thus. the vulnerabilities of the customer are irrelevant to Respondent's disclosure obligations.

In its Opposition, Enforcement contends that KA, MC, and BS can testify about the following issues pertaining to sanctions: (1) whether EC wanted charities, family, and friends to inherit her assets; (2) whether Respondent exercised a form of undue influence over EC; and (3) whether EC was financially sophisticated. But again, launching an inquiry into EC's intentions for the trust beneficiaries or Respondent's alleged influence over EC would go beyond the scope of the proper sanctions inquiry,[28] which is, what are the appropriate sanctions (if any) for a representative's alleged failure to disclose his position as successor trustee and beneficiary of a trust maintained by one of his customers? The proffered testimony of KA, MC, and BS would be irrelevant, unduly prejudicial, and confusing with regard to the issue of sanctions.

C. Relevance As To Respondent's Knowledge Of His Beneficiary Status

As mentioned in Section III.A. above, there is one area in which the testimony of one of the proffered witnesses would be relevant and probative. A fact of consequence contested in this matter is whether Respondent knew that he and his wife were named as 100 percent beneficiaries of the trust. Respondent put this in issue by contending that he had no such knowledge. KA's deposition testimony in the probate litigation indicates she has information that tends to undermine this contention: in July 2011, when KA went next door to EC's house to witness the execution of the trust amendment making Respondent and his wife 100 percent beneficiaries, Respondent was present with CWW, the putative attorney for EC.

KA's deposition testimony tends to indicate that Respondent was sufficiently involved with the trust amendment to accompany CWW to EC's house or meet her there for the execution of that document. If true, such involvement arguably makes it more probable that Respondent knew the amendment named him and his wife as 100 percent beneficiaries of the trust. If KA testifies to the same effect at the hearing, her testimony would be relevant and probative as to this consequential fact.

Therefore, MC and BS will be precluded from testifying at the hearing. KA will be allowed to testify, from her personal knowledge, about the execution of the amendment making Respondent and his wife 100 percent beneficiaries and the surrounding circumstances, and whether Respondent knew that he or his wife was a beneficiary of the trust.

D. Relevance Of The Testimony Of CWW

The reasoning of this Order applies to one of Respondent's witnesses, CWW. Like KA, MC, and BS, most or all of CWW's testimony, as described in Respondent's Witness List, is irrelevant to the facts of consequence in the first and second causes of action:

[28] As for EC's financial sophistication, the parties have stipulated that she "had a sixth grade education and had previously owned a hair salon and been a homemaker." Stip. ¶ 2.

> [CWW] is an attorney. She assisted [EC] with the drafting and execution of certain amendments to the [EC] trust. She is expected to testify about the process by which the trust amendments were prepared and executed, the absence of Respondent from the amendment process except for being nominated as successor trustee and the lack of undue influence or duress on [EC] in connection with her decision to make the amendments to her trust.

The lack or presence of undue influence or duress does not make any of the consequential facts more or less probable. The principal issue to be decided in the first and second causes of action is whether Respondent was required to disclose to his employer firm that he was a successor trustee and beneficiary of the trust. Additionally, the testimony of CWW would be unduly prejudicial because, like KA, MC, and BS, it would distract the Hearing Panel with confusing, unnecessary issues such as the validity of various trust amendments and whether Respondent exercised undue influence over EC. Extended testimony about the process of creating and executing several different trust amendments also may give rise to an unacceptable danger of inadvertently revealing confidential attorney-client communications between EC and CWW.[29] Therefore, like KA, CWW will be allowed to testify, without disclosing privileged communications, about the execution of the amendment making Respondent and his wife 100 percent beneficiaries only and the surrounding circumstances, and whether Respondent knew that he or his wife was a beneficiary of the trust.

IV. Order

For the reasons stated, Respondent's Motion to exclude the testimony of KA, MC, and BS is **GRANTED IN PART AND DENIED IN PART**. MC and BS are precluded from testifying at the hearing. KA's testimony is limited to her personal knowledge of the execution of the trust amendment making Respondent and his wife 100 percent beneficiaries and the surrounding circumstances, and whether Respondent knew that he or his wife was a beneficiary of the trust.

CWW's testimony is likewise limited. She shall be allowed to testify, without disclosing privileged communications, about the execution of the trust amendment making Respondent and his wife 100 percent beneficiaries and the surrounding circumstances, and whether Respondent knew that he or his wife was a beneficiary of the trust.

Respondent's request for leave to file a reply brief is **DENIED AS MOOT**.

SO ORDERED.

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[29] Except in litigation between testamentary heirs to a decedent's estate (the "testamentary exception"), courts generally presume that the attorney-client privilege survives the client's death. *Swidler & Berlin v. United States,* 524 U.S. 399, 404 (1998).

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Richard E. Simpson
Hearing Officer

Dated: February 3, 2016