This order has been published by the NASDR Office of the Hearing Officers and should be cited as OHO Order 97-18 (CAF970001).

NASD REGULATION, INC.
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT,	:	
Complainant,	:	Disciplinary Proceeding No. CAF 970001
v.	:	Hearing Officer - SW
Respondent.	:	

ORDER REGARDING MOTION TO STRIKE AFFIRMATIVE DEFENSES

On November 14, 1997, the Department of Enforcement ("Enforcement") filed its Motion to Strike Respondent's three affirmative defenses. On December 10, 1997, Respondent filed a Memorandum in Opposition to Enforcement's Motion to Strike and a Motion for Judgment on the Pleadings.[1] An Order from the Hearing Panel addressing the Motion for Judgment on the Pleadings is being issued separately.

The Hearing Officer has carefully reviewed the Motion to Strike with the attached memorandum and Respondent's Memorandum in Opposition to Enforcement's Motion to Strike.

First Affirmative Defense: Five Year Statute of Limitations

Respondent's first affirmative defense is that Enforcement is time-barred from bringing an action because of a five-year statute of limitations. Respondent's argument is based on 28 U.S.C. § 2462 ("§ 2462"), a federal five-year statute of limitations applicable to judicial and

[1] The Respondent also filed an amended Answer to the amended Complaint. However, the amendments to the Answer did not change the affirmative defenses.

administrative governmental proceedings brought for the enforcement of any civil fine, penalty, or forfeiture. In 3M Co. v. Browner, 17 F.3d 1453 (D.C. Cir. 1994), the United States Court of Appeals for the District of Columbia Circuit reversed the holding of an Administrative Law Judge for the Environmental Protection Agency ("EPA") that §2462 was inapplicable to an EPA proceeding on the ground that §2462 only applied to judicial proceedings. The court in the 3M case held that an agency adjudication of civil penalties was a proceeding within the definition of §2462.

Respondent specifically relies on Johnson v. SEC, 87 F.3d 484 (D.C. Cir. 1996), where the United States Court of Appeals for the District of Columbia Circuit, applying its reasoning in 3M, held that the five year statute of limitations of §2462 applied to administrative enforcement proceedings of the Securities and Exchange Commission ("SEC"). The Respondent takes the position that an NASD Regulation disciplinary proceeding, which is modeled in part on the Administrative Procedure Act,[2] is substantially identical to a SEC proceeding, and, therefore, should be included within the meaning of proceeding for purposes of §2462.

Subsequent to the 1996 Johnson decision, the SEC considered the applicability of §2462 to disciplinary proceedings initiated by self-regulatory organizations. The SEC unequivocally held that the five year limitation period of §2462 does not apply to disciplinary proceedings initiated by self-regulatory organizations, such as the NASD. The SEC, among other things, observed that applying a statute of limitations to a self-regulatory organization would impair the organization's statutory obligation and duty to protect the public and discipline its members. See In re the Application of Henry James Faragalli, Jr., Securities Exchange Act Release. No. 37991,

63 SEC Docket 651, 1996 SEC LEXIS 3263, at *36 (Nov. 26, 1996) and In re Larry Ira Klein, Securities Exchange Act Release No. 37835, 1996 SEC LEXIS 2922 (Oct. 17, 1996). In Respondent's Memorandum in Opposition to Enforcement's Motion to Strike, the Respondent failed to cite or acknowledge the Faragalli or Klein cases.

The Office of Hearing Officers is subject to the precedents of the National Business Conduct Committee, the SEC, and the federal courts. Since the SEC has ruled definitively on this issue, the Department of Enforcement's Motion to Strike the first affirmative defense is granted.

Second Affirmative Defense: Failure to File U-5

Respondent's second affirmative defense is that the action is time-barred under Article IV, Section 4(a) of the NASD By-Laws. Article IV, Section 4(a) provides that the NASD retains jurisdiction over registered persons for "two years after the effective date of termination of registration. The Respondent argues that the purpose of the Article IV, Section 4(a) was to retain jurisdiction for two years after termination of employment and that the Respondent terminated his employment in August 1992 more than six years before the Complaint was filed. The SEC has clearly stated that the NASD's jurisdiction is predicated not on termination of employment or association but on termination of registration, which is effective upon receipt of the Form U-5 termination notice. See In re the Application of Donald M. Bickerstaff, Securities Exchange Act Release No. 35607, 1995 SEC LEXIS 982, at *5 (April 17, 1995). The NASD also has stated clearly that the termination of its jurisdiction is predicated upon the receipt of a Form U-5 termination notice. See NASD Notice to Members, 92-19 (April 1992).

---

[2] See Exchange Act Release No. 38545, 1997 SEC LEXIS 959, at *20 (April 24, 1997).

According to Respondent's Form U-5, his termination date was August 4, 1995. The termination of Respondent's registration, however, did not become effective until Daiwa filed Respondent's Form U-5 with the NASD on October 9, 1995. Enforcement filed the Complaint against the Respondent on October 7, 1997, within the two year deadline. With respect to the second affirmative defense, Enforcement's Motion to Strike is granted.

Third Affirmative Defense: Good Faith

Respondent's third affirmative defense is that he "acted in good faith according to the instructions of his supervisors and at no time did he intend to violate the applicable rules or regulations." Acting in good faith is not an affirmative defense to allegations of violations of Conduct Rules 2110 and 2120, Section 10(b) of the Securities Exchange Act of 1934, as amended, and Rule 10b-5 thereunder, or aiding and abetting violations of Sections 10(b) and 15(c) of the Securities Exchange Act of 1934, as amended. See In re: Jeffrey L. Feldman, Admin. Proc. File No. 3-8063, 1994 SEC LEXIS 186 (Jan. 14, 1994). The issue of good faith goes to the issue of intent or scienter, elements of the alleged violation which must be proven by the Department of Enforcement. With respect to the third affirmative defense, Enforcement's Motion to Strike is granted.

Issues Other Than Liability

Nothing in this Order precludes Respondent from introducing evidence that relates to Respondent's intent or state of mind. Information or evidence with respect to intent or scienter will be considered by the Hearing Panel in determining whether Enforcement has met its burden with respect to establishing liability in connection with the Complaint's allegations that Respondent violated Section 10(b) of the Securities Exchange Act and Conduct Rule 2120.

The Hearing is a unitary proceeding; all evidence bearing on liability and sanctions, including any evidence of mitigation, must be presented at the Hearing. The Hearing Officer will address specific evidentiary issues as they arise.

SO ORDERED.

____
Sharon Witherspoon
Hearing Officer

Dated: Washington, DC
December 26, 1997