This order has been published by the NASDR Office of the Hearing Officers and should be cited as OHO Order 97-4 (CMS960105).

NASD REGULATION, INC.
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT,	:	
Complainant,	:	Disciplinary Proceeding No. CMS960105
v.	:	
	:	Hearing Officer - GAC
Respondent.	:	

ORDER DENYING MOTION FOR DISQUALIFICATION OF HEARING OFFICER

Respondent ("Respondent") on October 8, 1997 filed a Motion for Disqualification of Hearing Officer Gary A. Carleton pursuant to Procedural Rule 9233(b). [1] The Department of Enforcement did not respond to Respondent's motion. The motion has been referred to the NASD Regulation's Chief Hearing Officer for decision as required by Rule 9233(c).

In support of its motion, Respondent states that Hearing Officer Carleton should be disqualified because "… it is inappropriate for a seven year veteran of the NASD Enforcement Department to act as a neutral Hearing Officer in a disciplinary hearing." See Respondent's Motion For Disqualification at ¶2. Respondent claims further that "neutrality is …

[1] On September 23, 1997, Respondent filed a motion requesting, among other things, that Hearing Officer Carleton's background and experience be disclosed, including but not limited to his prior affiliations with the NASD. In a September 24 , 1997 Order, the Hearing Officer stated that "Gary Carleton was employed in the NASD's Enforcement Department (previously known as the Anti-Fraud Department) from approximately December 1989 until January 1997." To the extent Respondent's motion requested additional information regarding Hearing Officer

compromised in this case by the appointment of an individual who until recently was responsible for prosecuting disciplinary actions." Id.

Rule 9233(b) requires that a motion to disqualify a Hearing Officer be based upon a "… reasonable, good faith belief that a conflict of interest or bias exists or circumstances otherwise exist where the Hearing Officer's fairness might reasonably be questioned." The Rule also requires that the motion be accompanied by an affidavit setting forth in detail the facts alleged to constitute grounds for disqualification, and the dates on which the Party learned of those facts.

Respondent's Motion for Disqualification of Hearing Officer Gary A. Carleton fails to set forth specific facts that identify any conflict of interest, bias, or other circumstances that would provide a reasonable basis for disqualification under Rule 9233(b). Moreover, Respondent's arguments fail to establish, as a matter of law, any basis for disqualification: Hearing Officer Carleton's former employment as a NASD Regulation enforcement attorney does not create a basis for disqualification when, as in this case, he had no prior connection to the investigation that resulted in this proceeding. Accordingly, Respondent's motion is denied.

CHIEF HEARING OFFICER'S INVESTIGATION

The Chief Hearing Officer, as required by Rule 9233(c), has investigated whether disqualification of Hearing Officer Carleton is required. The investigation revealed that Hearing Officer Carleton resigned from the Department of Enforcement and joined the Office of Hearing Officers in January 1997. See September 24, 1997 Order Regarding Request For Information and Motion For Extension of Time, supra, note 1. The Office of Hearing Officers is independent

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Carleton's background, that request was denied. However, at a pre-hearing conference on October 6, Hearing Officer Carleton provided additional information to the parties. See text, infra at 2-3.

of the Department of Enforcement and has no involvement in investigating allegations of misconduct or in determining whether to institute a disciplinary proceeding against any respondent. See Code of Procedure Rule 9144. Moreover, Hearing Officer Carleton has not participated in any investigations or prosecutions by the Department of Enforcement since joining the Office of Hearing Officers in January 1997. In addition, as Hearing Officer Carleton stated at the October 6, 1997 Pre-Hearing Conference in this proceeding, he had no role in the institution of this case. (See Transcript of October 6, 1997 Pre-Hearing Conference in Department of Enforcement v. _____, Disciplinary Proceeding CMS960105, at 25.) Hearing Officer Carleton further stated at the October 6, 1997 Pre-Hearing Conference that the underlying investigation relating to this disciplinary proceeding was conducted by the Department of Market Regulation, not the Department of Enforcement. Id. Mr. Carleton has never worked in the NASD Regulation Department of Market Regulation.

LEGAL STANDARD

The general standard for disqualification or recusal that applies in NASD Regulation disciplinary proceedings is found in Rule 9160. Rule 9160 provides "[n]o person shall participate as an Adjudicator in a matter governed by the Code as to which he or she has a conflict of interest or bias, or circumstances otherwise exist where his or her fairness might reasonably be questioned." Code of Procedure Rule 9160. Rule 9233(b) applies this standard to any motion seeking the disqualification of a Hearing Officer. The standard provided in Rules 9160 and 9233 borrows heavily from the conflict of interest standard applicable to federal judges found in Section 455(a) of Title 28 of the United States Code. See Exchange Act Release No. 38545, 64 SEC Docket 862, 909 (April 24, 1997).

Section 455(a) of the United States Code provides: "[a]ny justice, judge, or magistrate of the United States shall disqualify himself in any proceeding *in which his impartiality might reasonably be questioned*." 28 U.S.C. § 455(a).[2] NASD Regulation relies on judicial decisions interpreting the statutory standard applicable to federal judges when interpreting Rule 9233(b).[3] More specifically, when proposing the recusal and disqualification provisions as set forth in Rules 9160, 9233, 9234, and 9332, the NASD specifically noted:

> "[Rule 9233(b) will] be interpreted in a manner that accords with the operation of a self-regulatory disciplinary system in which members of the industry are intended to serve as Adjudicators. The judicial interpretation of 28 U.S.C. § 455(a) provides a basis for such an interpretation because the judicial interpretation relies upon additional objective factors used to determine a disputed claim of bias**.** *The Association intends to rely on such judicial interpretation of the clause "in which his impartiality might reasonably be questioned," in 28 U.S.C. § 455(a), in interpreting the proposed clause, "if circumstances otherwise exist where [the Adjudicator's] fairness might reasonably be questioned.")* See Exchange Act Release No. 38545, 64 SEC Docket 909 (April 24, 1997) *(emphasis added*).

Although the NASD uses the word "fairness" in Rule 9233(b) rather than the word "impartiality" in Section 455(a), the NASD emphasized in its rule filing with the SEC that "*The notions of impartiality and fairness are inextricably linked in an analysis of whether an Adjudicator fairly judges a proceeding."* Id.

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[2] Courts have interpreted the language of Section 455(a) to require parties to demonstrate a factual basis to support a claim of disqualification. United States v. Lovalgia, 954 F.2d 811, 815 (2d. Cir. 1992); United States v. Walker, 920 F.2d 513 (8th Cir. 1990); Parker v. Connors Steel Co., 855 F.2d 1510, 1524 (11th Cir.), reh'g denied, 864 F. 2d 795 (11th Cir.), cert. denied, 490 U.S. 1066 (1988); Pepsico v. McMillen, 764 F.2d 458 (7th Cir. 1985).

[3] See Exchange Act Release No. 38545, 64 SEC Docket 862, 909 (April 24, 1997). The NASD's proposed rule change, as amended, was approved by the Securities Exchange Commission on August 7, 1997. See Exchange Act Release No. 38908, 65 SEC Docket 237 (August 7, 1997). The NASD also looks to Section 556(b) of the Administrative Procedure Act for guidance. 62 Fed. Reg. at 25,226, 25,255 (1997) (quoting 5 U.S.C. § 556(b)). Like Rule 9233(b), Section 556(b) requires a party to have a "good faith" belief when filing a motion to disqualify an adjudicator. 5 U.S.C. § 556(b).

Courts have interpreted Section 455(a) to require parties to establish a factual basis that demonstrates a judge's inability to act in a fair and impartial manner before ordering disqualification. In Pepsico v. McMillen, the Seventh Circuit interpreted Section 455(a) to require recusal whenever there exists "'*a reasonable basis*' for finding an 'appearance of partiality under the facts and circumstances' of the case." 764 F.2d 458, 460 (7th Cir. 1985)(citing SCA Securities, Inc. v. Morgan, 557 F. 2d 110, 116 (7th Cir. 1977)) . The Court found that the *test for partiality* is whether "… *an objective, disinterested observer fully informed of the facts* underlying the grounds on which recusal was sought would entertain a significant doubt that justice would be done in the case." Id. at 460. Several other circuits have adopted similar interpretive language when construing this statutory standard.[4]

These cases illustrate a consistent approach to interpreting Section 455(a) by requiring parties to detail specific facts to support a motion for disqualification.[5] Rule 9233(b)'s provision for the disqualification of a Hearing Officer is substantially similar to the standard set forth in Section 455(a).

[4] See, e.g., Lovalgia, 954 F.2d at 815 ("Would a reasonable person, knowing all the facts, conclude that the trial judge's impartiality could reasonably be questioned?"); Walker, 920 F.2d at 517 (Would a "reasonable, uninvolved observer question the judge's impartiality … [and] [whether] an objective, disinterested observer fully informed of the facts underlying the ground on which recusal is sought would entertain significant doubt that justice would be done."); Parker, 855 F.2d at 1524 ("Whether an objective, disinterested, lay observer fully informed of the facts underlying the grounds on which recusal was sought would entertain a significant doubt about the judge's impartiality.").

[5] See, e.g., Rita H. Malm, Exchange Act Release No. 35000, 58 S.E.C. Docket 131 (Nov. 23, 1994), 1994 WL 665963, at *8 (finding that conclusory allegation that a panelist's prior working relationship with respondent is insufficient to establish bias); Robert E. Gibbs, 54 S.E.C. Docket 504 (June 3, 1993), 1993 WL 190913, at *2 (where respondent failed to produce any factual evidence that DBCC panelist was biased against him because he had previously testified against respondent's employer in an unrelated matter); Arthur J. Lewis, 49 S.E.C. Docket 1487, 1489 (Oct. 8, 1991), 1991 WL 294317, at *3 (respondent failed to produce evidence demonstrating that panel member had any improper bias or interest that would affect ability to render impartial decision).

LEGAL DISCUSSION

Respondent makes the broad argument that Hearing Officer Carleton's previous employment with NASD Enforcement mandates disqualification. See Respondent's Motion For Disqualification at ¶2. The logical result of Respondent's argument is that any judge who has served as a former prosecutor would automatically be disqualified from presiding over criminal cases simply by reason of prior employment. Id. This argument has been uniformly rejected by the courts.[6]

Before a federal judge will be considered biased based on past conduct as an attorney under Sections 455(a) and 455(b)(3),[7] a party seeking disqualification must demonstrate that the judge actually participated as counsel in the former case. DiPasquale, 864 F.2d at 278-79; Gipson, 835 F.2d at 1325-26.[8] Absent a specific showing that a judge was previously involved with the substance of a defendant's case, Sections 455(a) and 455(b)(3) do not mandate recusal. DiPasquale, 864 F.2d at 278-79. In fact, federal courts have refused to adopt a per se rule disqualifying trial judges from hearing even those cases brought in their districts while they were still former prosecutors. Kendrick, 995 F.2d at 1443-44; DiPasquale, 864 F.2d at 278-79. Mandatory disqualification has been restricted to cases where a judge has taken part in the

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[6] U.S. v. Voccola, 99 F.3d 37, 41-42 (1st Cir. 1996); U.S. v. Thompson, 76 F.3d 442, 451 (2d Cir. 1996); U.S. v. Arnpriester, 37 F.3d 466, 467 (9th Cir. 1994); Kendrick v. Carlson, 995 F.2d 1440, 1443-44 (8th Cir. 1993); U.S. v. DiPasquale, 864 F.2d 271, 278-79 (3rd Cir. 1988); U.S. v. Gipson, 835 F.2d 1323, 1325-26 (10th Cir. 1988).

[7] Title 28 U.S.C. § 455(b)(3) requires a federal judge to recuse himself in any matter "where he has served in governmental employment and in such capacity participated as counsel, adviser or material witness concerning the proceeding or expressed an opinion concerning the merits of the particular case in controversy."

[8] As noted in note 1, supra, Hearing Officer Carleton, in response to a request for information regarding his prior affiliations with the NASD, informed Respondent that he worked in the Enforcement Department from 1989 to January 1997. At the October 6, 1997 Pre-Hearing Conference, Hearing Officer Carleton further informed counsel for Respondent that he was not aware of the issues and had no involvement with the investigation that led up to the initiation of this formal disciplinary proceeding. See Transcript of October 6, 1997 Pre-Hearing Conference at 25.

investigation, preparation, or prosecution of the case. Arnpriester, 37 F.3d at 467; Kendrick, 995 F.2d at 1444; Gipson, 835 F.2d at 1325-26.

Applying these principles, the Chief Hearing Officer finds that Respondent's motion fails to meet the requirements of Rule 9233(b). Specifically, Respondent has failed to demonstrate a "reasonable basis" for finding that Hearing Officer Carleton's previous employment with NASD Enforcement would taint his ability to render an unbiased decision. Arnpriester, 37 F.3d at 467; DiPasquale, 864 F.2d at 278-79. Respondent does not allege that Mr. Carleton had any involvement in the investigation that led to the institution of this proceeding or participated in any determination to bring a formal disciplinary proceeding against Respondent. Moreover, Respondent has conceded that no "specific conflict of interest" exists between Hearing Officer Carleton and the parties in this matter.[9] See "Respondent's Motion For Disqualification" at ¶2. An adjudicator should be disqualified only where he participated in the investigation, preparation, or prosecution of a defendant in a case now before him. Gipson, 835 F.2d at 1325-26. Respondent does not assert that Hearing Officer Carleton participated in any of these activities, and his prior association with NASD Enforcement does not automatically or inferentially support disqualification .

[9] Respondent further concedes that it "… does not doubt Mr. Carleton's personal qualifications or integrity." See "Respondent's Motion For Disqualification" at ¶ 2.

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Accordingly, Respondent's Motion for Disqualification of Hearing Officer Gary A. Carleton is hereby denied.

SO ORDERED,

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Linda D. Fienberg
Chief Hearing Officer

Dated: Washington, DC
October 30, 1997