UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Administrative Proceedings Rulings
Release No. 5780 / June 7, 2018

Administrative Proceeding
File No. 3-18411

In the Matter of

Wedbush Securities, Inc.

Order Denying Motion to Disqualify Counsel

The Division of Enforcement moves to disqualify Charles B. LaChaussee from acting as counsel for Respondent Wedbush Securities, Inc., claiming that LaChaussee is conflicted. Wedbush opposes the Division's motion, arguing there is no conflict. Because the Division has not carried its burden, I DENY its motion. Nevertheless, to safeguard the integrity of the proceeding, I ORDER Wedbush to submit the documents discussed below for *in camera* inspection.

Wedbush is dually registered with the Securities and Exchange Commission as a broker-dealer and an investment adviser. The allegations in the order instituting proceedings (OIP) concern whether it failed to reasonably supervise Timary Delorme, one of it registered representatives. According to the OIP, Delorme settled two customer arbitrations in 2013 and, under a settlement she reached with the Commission in March 2018, is subject to a securities-industry bar.

In its motion, the Division asserts that LaChaussee "played an integral role in" what it says was "Wedbush's deficient internal investigation into Ms. Delorme's conduct."[1] It also claims that he represented "Delorme in connection with" the customer arbitrations.[2] Based on these assertions, the Division argues that LaChaussee is conflicted because:

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[1] Mot. at 1.

[2] *Id.* In its opposition, Wedbush says that LaChaussee only represented Delorme in the first of two customer arbitrations. Opp'n at 2. The Division does not challenge this assertion is its reply.

> (1) he may become a necessary witness at the hearing; (2) he may be taking an adversarial position to his former client, Ms. Delorme, and has not obtained a waiver of such conflict; and (3) he was an active participant in the events underlying the Division's claims.[3]

Based on the assertion that he is a necessary witness, the Division asks that I disqualify LaChaussee from appearing as counsel for Wedbush.[4] And if I do not disqualify LaChaussee, the Division asks that that I prohibit him from cross-examining Delorme because she is his former client whose position is adverse to Wedbush's position.[5] It also requests that I enforce requirements in the California Rules of Professional Responsibility and the ABA Model Rules and require Wedbush to affirm in writing that it has been informed that LaChaussee's conduct is at issue and that his personal interests may limit his ability to fully represent Wedbush.[6]

Discussion

Owing to the risk that a motion to disqualify might be used as a tactical device to disadvantage a movant's opponent and the disruptive consequences that would flow from disqualification, courts tend to view such motions "with extreme caution,"[7] if not outright skepticism.[8] A party moving to disqualify counsel thus bears "a heavy burden of proving" the grounds for disqualification.[9]

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[3] Mot. at 1.

[4] *Id.* at 6–7.

[5] *Id.* at 7–9.

[6] *Id.* at 9–10.

[7] *Freeman v. Chi. Musical Instrument Co.*, 689 F.2d 715, 722 (7th Cir. 1982); *see Shurance v. Planning Control Int'l, Inc.*, 839 F.2d 1347, 1349 (9th Cir. 1988).

[8] *Mills v. Hausmann-McNally*, S.C., 992 F. Supp. 2d 885, 891 (S.D. Ind. 2014); *see Bd. of Ed. of N.Y.C. v. Nyquist*, 590 F.2d 1241, 1246 (2d Cir. 1979) (describing the court's "considerable reluctance to disqualify attorneys").

[9] *Evans v. Artek Sys. Corp.*, 715 F.2d 788, 794 (2d Cir. 1983); *see United States v. Perry*, 30 F. Supp. 3d 514, 533 (E.D. Va. 2014); *Mills*, 992 F. Supp. 2d at 895 ("[T]he moving party bears a significant burden when it seeks the disqualification of opposing attorneys . . . ."); *Shurance*, 839 F.2d at 1349

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In arguing that LaChaussee is a necessary witness, the Division says that "[w]hat Mr. LaChaussee did, and more important, failed to do, in response to allegations of rampant fraud is highly relevant—indeed, central—to the Division's claim."[10] There are two problems with the Division's argument. First, it does not claim that it will be prejudiced if LaChaussee testifies.[11] Second, "[a] necessary witness is not the same thing as the 'best' witness."[12] Even if the Division has shown that LaChaussee is the best witness on the issue of Wedbush's response to allegations of fraud—which it has not—it has not shown that he is necessary, *i.e.*, that the testimony he might provide is unavailable from any other source.[13] Other than saying LaChaussee is necessary, the Division does not explain why. And given its burden, the Division's omission is fatal to this aspect of its motion.[14]

Additionally, without specific information, it is impossible to infer whether LaChaussee would actually be a necessary witness. This fact further supports the denial of the Division's motion.[15]

("Because of [the] potential for abuse, disqualification motions should be subjected to particularly strict judicial scrutiny." (quoting *Optyl Eyewear Fashion Int'l Corp. v. Style Cos.*, 760 F.2d 1045, 1050 (9th Cir. 1985))); *see also Freeman*, 689 F.2d at 721 ("[D]isqualification . . . is a drastic measure which courts should hesitate to impose except when absolutely necessary.").

[10] Reply at 3; *see* Mot. at 3–4 (describing LaChaussee's alleged role).

[11] *See FDIC v. U.S. Fire Ins. Co.*, 50 F.3d 1304, 1315 (5th Cir. 1995) ("Where an attorney's testimony may prejudice only his own client, the opposing party should have no say in whether or not the attorney participates in the litigation as both advocate and witness.").

[12] *Harter v. Univ. of Indianapolis*, 5 F. Supp. 2d 657, 665 (S.D. Ind. 1998); *see United States v. Melton*, 948 F. Supp. 2d 998, 1006–07 (N.D. Iowa 2013).

[13] *See United States v. Starnes*, 157 F. App'x 687, 693–94 (5th Cir. 2005) ("A lawyer is not 'likely to be a necessary witness' when evidence pertaining to each matter to which he could testify is available from another source."); *Mills*, 992 F. Supp. 2d at 895.

[14] *Cf. Mills*, 992 F. Supp. 2d at 895 (noting that courts should be skeptical of claims that opposing counsel is a necessary witness).

[15] *See Perry*, 30 F. Supp. 3d at 536 ("[T]he balancing tasked to this Court is necessarily difficult at this stage in the proceedings because the Court is required to prognosticate how complex ethical principles will apply in light of the evidence to be presented at trial, yet the Court lacks access to the bulk of the evidence to be presented at trial."); *cf. Mercury Vapor Processing Techs., Inc. v. Riverdale*, 545 F. Supp. 2d 783, 789 (N.D. Ill. 2008) (holding that a

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The Division next argues that LaChaussee should not be permitted to cross-examine Delorme because he represented her in a customer arbitration.[16] Wedbush responds that in conjunction with that representation, which occurred in 2012, Delorme signed a joint representation letter.[17] Wedbush also notes that although LaChaussee's prior representation of Delorme involved claims about how she handled her clients' accounts, what is at issue here is different.[18] As a result, it claims that whatever confidential information LaChaussee may have learned will not likely be relevant in this proceeding.[19]

The parties cite the California Rules of Professional Conduct and believe those rules should guide the determination of whether LaChaussee can examine Delorme during the hearing. But this proceeding was not instituted to determine whether LaChaussee violated a state ethical rule. Whether his representation of Wedbush would violate a California ethical rule is not directly relevant.[20] Instead, the Commission's interest, as it concerns LaChaussee's representation of a respondent in Commission administrative proceedings, relates to the integrity of the proceeding itself.[21] And since the

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disqualification motion was "premature" because "it is not known whether other witnesses would be able to testify to the same matters").

16 *See* supra note 2.

17 Opp'n at 2, 8. Wedbush's opposition is supported by LaChaussee's declaration in which he declares that Delorme agreed in the joint representation letter "that in the event a conflict developed between her and Wedbush and the members of the Legal Department had to withdraw from representing her, they would continue to represent Wedbush." LaChaussee Decl. at 9.

18 Opp'n at 9.

19 *Id.*

20 *Cf. Armstrong v. McAlpin*, 625 F.2d 433, 446 n.26 (2d Cir. 1980) (en banc) (noting that ethical standards were drafted for use in disciplinary proceedings, not for use in deciding disqualification motions), *vacated on other grounds*, 449 U.S. 1106 (1981); *UMG Recordings, Inc. v. MySpace, Inc.*, 526 F. Supp. 2d 1046, 1062 (C.D. Cal. 2007) (noting the "growing dissatisfaction with the use of disqualification as a remedy for ethical misconduct") (quoting Richard E. Flamm, *Lawyer Disqualification: Conflicts of Interest and Other Bases* § 23.1, at 443-45 (2003)).

21 *Trautman Wasserman & Co.*, Securities Exchange Act of 1934 Release No. 55989, 2007 WL 1892138, at *4 (June 29, 2007). A proceeding's integrity could be questioned, for example, if an attorney simultaneously represents a

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Commission's jurisdiction is not limited to any state or judicial district and attorneys in Commission proceedings are not required to be members of any particular state bar, any decision on disqualification must be guided by a generally applicable, national standard, rather than the specific requirements of any particular state's ethics rules.[22] I therefore consider the ABA Model Rules of Professional Conduct.[23]

There is no evidence that LaChaussee currently represents Delorme or that he has represented her in any matter since she settled an arbitration in 2013. ABA Rule 1.9(a) concerns an attorney's duty to a former client. It says:

> A lawyer who has formerly represented a client in a matter shall not thereafter represent another person in the same or a substantially related matter in which that person's interests are materially adverse to the interests of the former client unless the former client gives informed consent, confirmed in writing.

Given the allegations in the OIP, it is not possible to conclude that Delorme's 2012 customer arbitration or any information LaChaussee learned in 2012 while representing Delorme are irrelevant. It is likely the Division will question Delorme about that arbitration and the events that led to it. At the same time, however, Rule 1.9 allows current and former clients to waive conflicts.

Considering this circumstance and the rules in light of the Commission's interest in "search[ing] for the truth and [reaching] a just determination" and

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respondent and a witness whose interests are adverse to the respondent's interests; counsel's loyalties would be divided, "prevent[ing] him from fulfilling his duty to act in good faith." *Clark T. Blizzard*, Investment Advisers Act of 1940 Release No. 2032, 2002 WL 714444, at *2 (Apr. 24, 2002). And that would frustrate the Commission's interest in "search[ing] for the truth and [reaching] a just determination." *Id.*

[22] *See Scattered Corp.*, Exchange Act Release No. 40646, 1998 WL 774795, at *7 (Nov. 9, 1998) ("We look primarily to both the American Bar Association's Model Rules of Professional Conduct … and the American Law Institute Restatement (Third) of the Law: The Law Governing Lawyers … rather than … state law, for a national standard appropriate to a federal agency.").

[23] *See U.S. Fire Ins.*, 50 F.3d at 1312 (characterizing the ABA rules as "ethical rules announced by the national profession in the light of the public interest and the litigant's rights" (quoting *In re Dresser Indus., Inc.*, 972 F.2d 540, 543 (5th Cir. 1992))).

Wedbush's strong interest in retaining counsel of its choice, it is evident that so long as Delorme and Wedbush consent, LaChaussee may examine Delorme.[24]

Finally, the Division asks that I enforce requirements in the California Rules of Professional Responsibility and the ABA Model Rules and require Wedbush to affirm in writing that it has been informed that LaChaussee's conduct is at issue that his personal interests may limit his ability to fully represent Wedbush.[25] But this is not a disciplinary proceeding. And at this stage, it is not clear that LaChaussee's "interests concerning his own conduct" may affect his representation of Wedbush. Nevertheless, the Commission's interest in protecting the integrity of the proceeding would be served by requiring a written waiver from Wedbush of any conflict or appearance of a conflict resulting from LaChaussee's prior representation of Delorme.

Order

The Division's motion to disqualify LaChaussee is DENIED. By June 21, 2018, Wedbush or LaChaussee shall submit for *in camera* review, (1) the referenced joint representation agreement Delorme executed, and (2) evidence of Wedbush's consent in light of LaChaussee's prior representation of her. Alternatively, Wedbush may elect in writing by June 21, 2018, to have a counsel other than LaChaussee represent it in this proceeding.

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James E. Grimes
Administrative Law Judge

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[24] *See* Bruce A. Green, *"Through A Glass, Darkly": How the Court Sees Motions to Disqualify Criminal Defense Lawyers*, 89 Colum. L. Rev. 1201, 1219–20 (1989) ("[I]t is clear that an attorney may accept a case in which his former client will testify as long as both his former client and current client consent."); Stephen H. Goldberg, *The Former Client's Disqualification Gambit: A Bad Move in Pursuit of an Ethical Anomaly*, 72 Minn. L. Rev. 227, 271-72 (1987) ("As long as the current client has knowledge of the lawyer's potential handicap, the adversary system has no loyalty interest to pursue in successive conflict situations."); *cf. Holloway v. Arkansas*, 435 U.S. 475, 483 n.5 (1978) ("[A] defendant may waive his right to the assistance of an attorney unhindered by a conflict of interests.").

[25] Mot. at 10.