

*Required fields are shown with yellow backgrounds and asterisks.*

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SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
Form 19b-4

File No.\* SR - 2020 - \* 030

Amendment No. (req. for Amendments \*)

Filing by Financial Industry Regulatory Authority

Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial \* ☒ Amendment \* ☐ Withdrawal ☐Section 19(b)(2) \* ☒ Section 19(b)(3)(A) \* ☐ Section 19(b)(3)(B) \* ☐

Rule

Pilot ☐ Extension of Time Period  
for Commission Action \* Date Expires \* ☐ 19b-4(f)(1) ☐ 19b-4(f)(4)  
☐ 19b-4(f)(2) ☐ 19b-4(f)(5)  
☐ 19b-4(f)(3) ☐ 19b-4(f)(6)

Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010

Security-Based Swap Submission pursuant  
to the Securities Exchange Act of 1934Section 806(e)(1) \* ☐Section 806(e)(2) \* ☐Section 3C(b)(2) \* ☐

Exhibit 2 Sent As Paper Document



Exhibit 3 Sent As Paper Document

**Description**

Provide a brief description of the action (limit 250 characters, required when Initial is checked \*).

Proposed Amendments to the Codes of Arbitration Procedure Relating to Requests to Expunge Customer Dispute  
Information, Including Creating a Special Arbitrator Roster to Decide Certain Expungement Requests**Contact Information**Provide the name, telephone number, and e-mail address of the person on the staff of the self-regulatory organization  
prepared to respond to questions and comments on the action.First Name \* Mignon Last Name \* McLemore  
Title \* Assistant General Counsel  
E-mail \* mignon.mclemore@finra.org  
Telephone \* (202) 728-8151 Fax (202) 728-8264**Signature**

Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

(Title \*)

Date 09/22/2020

Senior Vice President and Deputy General Counsel

By Patrice Gliniecki

(Name \*)

Patrice Gliniecki,

NOTE: Clicking the button at right will digitally sign and lock  
this form. A digital signature is as legally binding as a physical  
signature, and once signed, this form cannot be changed.

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EDFS website.

**Form 19b-4 Information \***

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The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

**Exhibit 1 - Notice of Proposed Rule Change \***

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The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies \***

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The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change, security-based swap submission, or advance notice being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications**

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Exhibit Sent As Paper Document

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Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

**Exhibit 3 - Form, Report, or Questionnaire**

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Exhibit Sent As Paper Document

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Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

**Exhibit 4 - Marked Copies**

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The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

**Exhibit 5 - Proposed Rule Text**

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The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

**Partial Amendment**

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If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

**1. Text of the Proposed Rule Change**

(a) Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 (“Exchange Act” or “Act”),<sup>1</sup> the Financial Industry Regulatory Authority, Inc. (“FINRA”) is filing with the Securities and Exchange Commission (“SEC” or “Commission”) a proposed rule change to amend the Code of Arbitration Procedure for Customer Disputes (“Customer Code”) and the Code of Arbitration Procedure for Industry Disputes (“Industry Code”) (together, “Codes”) to modify the current process relating to the expungement of customer dispute information.

Specifically, the proposed rule change would amend the Codes to: (1) impose requirements on expungement requests (a) filed during an investment-related, customer initiated arbitration (“customer arbitration”) by an associated person, or by a party to the customer arbitration on-behalf-of an associated person (“on-behalf-of request”), or (b) filed by an associated person separate from a customer arbitration (“straight-in request”); (2) establish a roster of arbitrators with enhanced training and experience from which a three-person panel would be randomly selected to decide straight-in requests; (3) establish procedural requirements for expungement hearings; and (4) codify and update the best practices of the Notice to Arbitrators and Parties on Expanded Expungement Guidance (“Guidance”) that arbitrators and parties must follow.<sup>2</sup> In addition, the proposed rule change would amend the Customer Code to specify procedures for requesting expungement of customer dispute information arising from simplified

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> See Guidance, available at <https://www.finra.org/arbitration-and-mediation/notice-arbitrators-and-parties-expanded-expungement-guidance>.

arbitrations. The proposed rule change would also amend the Codes to establish requirements for notifying state securities regulators and customers of expungement requests.

The text of the proposed rule change is attached as Exhibit 5.

(b) Not applicable.

(c) Not applicable.

## **2. Procedures of the Self-Regulatory Organization**

The FINRA Board of Governors authorized the filing of the proposed rule change with the SEC. No other action by FINRA is necessary for the filing of the proposed rule change.

If the Commission approves the proposed rule change, FINRA will announce the effective date of the proposed rule change in a Regulatory Notice to be published no later than 60 days following Commission approval. The effective date will be no later than 120 days following publication of the Regulatory Notice announcing Commission approval of the proposed rule change.

## **3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change**

(a) Purpose

I. Background and Discussion

A. Customer Dispute Information in the Central Registration  
Depository

Information regarding customer disputes involving associated persons is maintained in the Central Registration Depository ("CRD<sup>®</sup>"), the central licensing and

registration system used by the U.S. securities industry and its regulators.<sup>3</sup> FINRA operates the CRD system pursuant to policies developed jointly with NASAA. FINRA works with the SEC, NASAA and other members of the regulatory community to ensure that information submitted and maintained in the CRD system is accurate and complete.

In general, the information in the CRD system is submitted by registered securities firms, brokers and regulatory authorities in response to questions on the uniform registration forms.<sup>4</sup> These forms are used to collect registration information, which includes, among other things, administrative, regulatory, criminal history, financial and other information about brokers, such as customer complaints, arbitration claims and court filings made by customers (i.e., “customer dispute information”). FINRA, state and other regulators use this information in connection with their licensing and regulatory activities, and member firms use this information to help them make informed employment decisions.

Pursuant to rules approved by the SEC, FINRA makes specific CRD information publicly available through BrokerCheck®.<sup>5</sup> BrokerCheck is part of FINRA's ongoing

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<sup>3</sup> The concept for the CRD system was developed by FINRA jointly with the North American Securities Administrators Association (“NASAA”). The CRD system fulfills FINRA’s statutory obligation to establish and maintain a system to collect and retain registration information. NASAA and state regulators play a critical role in the ongoing development and implementation of the CRD system.

<sup>4</sup> The uniform registration forms are Form BD (Uniform Application for Broker-Dealer Registration), Form BDW (Uniform Request for Broker-Dealer Withdrawal), Form BR (Uniform Branch Office Registration Form), Form U4 (Uniform Application for Securities Industry Registration or Transfer), Form U5 (Uniform Termination Notice for Securities Industry Registration) and Form U6 (Uniform Disciplinary Action Reporting Form).

<sup>5</sup> Section 15A of the Exchange Act requires FINRA to provide registration information to the public. BrokerCheck is one of the tools through which FINRA

effort to help investors make informed choices about the brokers and broker-dealer firms with which they may conduct business. BrokerCheck maintains information on the approximately 3,600 registered broker-dealer firms and 624,000 registered brokers. BrokerCheck also provides the public with access to information about formerly registered broker-dealer firms and brokers.<sup>6</sup> In 2019 alone, BrokerCheck helped users conduct more than 40 million searches of firms and brokers.

The regulatory framework governing the CRD system and BrokerCheck has long contemplated the possibility of expunging certain customer dispute information from these systems in limited circumstances, such as where the allegations made about the broker are factually impossible or clearly erroneous. The expungement framework seeks to balance the competing interests of providing regulators broad access to information about customer disputes to fulfill their regulatory obligations, providing a fair process that recognizes a broker's interest in protecting their reputation and ensuring investors have access to accurate information about brokers.

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disseminates this information to the public. There is a limited amount of information in the CRD system that FINRA does not display through BrokerCheck, including personal or confidential information. A detailed description of the information made available through BrokerCheck is available at <http://www.finra.org/investors/about-brokercheck>.

<sup>6</sup> Formerly registered brokers, although no longer in the securities industry in a registered capacity, may work in other investment-related industries or may seek to attain other positions of trust with potential investors. BrokerCheck provides information on more than 17,000 formerly registered broker-dealer firms and nearly 567,000 formerly registered brokers. Broker records are available in BrokerCheck for 10 years after a broker leaves the industry, and brokers who are the subject of disciplinary actions and certain other events remain on BrokerCheck permanently.

B. FINRA Rules 2080, 12805 and 13805 Governing Expungement of Customer Dispute Information

A broker can seek expungement of customer dispute information by obtaining a court expungement order (1) by going through the FINRA arbitration process (and then obtaining a court order confirming an arbitration award containing expungement) or (2) by going directly to court (without first going to arbitration).

FINRA rules require arbitrators to perform fact-finding before recommending expungement of customer dispute information and to provide information about the basis for the expungement. Specifically, FINRA Rules 12805 and 13805 require arbitrators to hold a recorded hearing regarding the appropriateness of expungement of customer dispute information and to review settlement documents, the amount of payments made to any party and any other terms and conditions of the settlement.<sup>7</sup>

In addition, these rules require arbitrators to indicate whether they have awarded expungement because: (1) the claim, allegation or information is factually impossible or clearly erroneous; (2) the associated person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation or conversion of funds; or (3) the claim, allegation or information is false.<sup>8</sup> The arbitrators are further required to

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<sup>7</sup> In almost every proceeding, all or a majority of the arbitrators considering an expungement request are public arbitrators. Among other requirements, public arbitrators have never been employed by the securities industry; do not devote 20 percent or more of their professional work to the securities industry or to parties in disputes concerning investment accounts or transactions or employment relationships within the financial industry; and do not have immediate family members or co-workers who do so. See FINRA Rule 12100(aa).

<sup>8</sup> See FINRA Rules 2080, 12805 and 13805.

provide a brief written explanation of the reasons for recommending expungement.<sup>9</sup>

These requirements are supplemented with extensive guidance and training, including the Guidance, first published in 2013 and expanded further periodically thereafter.<sup>10</sup> The Guidance provides arbitrators with best practices and recommendations to follow, in addition to the requirements of FINRA Rules 12805 and 13805, when deciding expungement requests.

Regardless of whether expungement of customer dispute information is sought directly through a court or in arbitration, FINRA Rule 2080, which was developed in close consultation with representatives of NASAA and state regulators, requires a broker-dealer firm or broker seeking expungement to obtain an order of a court of competent jurisdiction directing such expungement or confirming an award containing expungement. FINRA will expunge customer dispute information only after the court orders it to execute the expungement.<sup>11</sup>

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<sup>9</sup> Although FINRA Rules 12805 and 13805 state that the panel may “grant” expungement of customer dispute information under FINRA Rule 2080, the panel’s decision regarding an expungement request is not the final step in the process. A person seeking expungement must obtain a court order confirming an arbitration award for FINRA to expunge the customer dispute information from the CRD system. Accordingly, FINRA believes the word “recommend” more accurately describes the panel’s role in the expungement process. It has been FINRA’s longstanding practice to state in expungement awards that the arbitrators “recommend,” rather than “grant,” expungement. See also infra note 131, and accompanying text (stating that the proposed amendments to FINRA Rules 12805(c) and 13805(c) would also provide that the panel would “recommend” rather than “grant” expungement).

<sup>10</sup> See supra note 2.

<sup>11</sup> FINRA Rule 2080 also requires that firms and brokers seeking a court order or confirmation of the arbitration award containing expungement name FINRA as a party, and provides that FINRA will challenge the request in court in appropriate circumstances. FINRA may, however, waive the requirement to name it as a

### C. Concerns Regarding Expungement

Some stakeholders of the forum have raised concerns about expungement hearings held after the parties settle the customer arbitration that gave rise to the customer dispute information.<sup>12</sup> In many of these instances, the panel from the customer arbitration has not heard the full merits of that case and, therefore, may not have any special insights in determining whether to recommend a request for expungement of customer dispute information. Further, customers and their representatives typically do not participate in an expungement hearing after the customer arbitration settles, especially

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party if a firm or broker requests a waiver and FINRA determines that the award containing expungement is based on affirmative judicial or arbitral findings that: (1) the claim, allegation or information is factually impossible or clearly erroneous; (2) the associated person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation or conversion of funds; or (3) the claim, allegation, or information is false. In addition, FINRA has sole discretion “under extraordinary circumstances” to waive the requirement that it be named in a court proceeding if it determines that the request for expungement and accompanying award are meritorious and expungement would not have a material adverse effect on investor protection, the integrity of the CRD system, or regulatory requirements. See FINRA Rule 2080(b).

<sup>12</sup> In its Final Report and Recommendations, the FINRA Dispute Resolution Task Force (“Task Force”) included a recommendation to create a special arbitration panel consisting of specially trained arbitrators to decide expungement requests in settled cases and in cases when a claimant did not name the associated person as a respondent in the case. See <http://www.finra.org/sites/default/files/Final-DR-task-force-report.pdf>; see also letter from Barbara Black, Professor of Law, University of Cincinnati College of Law (Retired), to Marcia Asquith, Office of the Corporate Secretary, FINRA, dated February 5, 2018 (“Black”) (discussing the Task Force’s recommendation) and letter from Joseph Borg, President, NASAA, to Marcia Asquith, Office of the Corporate Secretary, FINRA, dated February 5, 2018 (“NASAA”) (commenting that post-settlement expungement hearings often consist of one-sided presentations of the facts). These and other letters responding to Regulatory Notice 17-42 (December 2017) (“Notice 17-42”) are discussed in Item 5 below.

if the expungement hearing occurs a number of years later.<sup>13</sup> In addition, a broker may file a straight-in request against a member firm for the sole purpose of requesting expungement.<sup>14</sup> In most of these straight-in requests, the customer dispute information arises from a customer arbitration or customer complaint that was disclosed on the broker's CRD record a number of years prior to the request.<sup>15</sup> Thus, during these

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<sup>13</sup> The Codes provide that no claim shall be eligible for submission to arbitration under the Codes where six years have elapsed from the occurrence or event giving rise to the claim. The panel resolves any questions regarding the eligibility of a claim under this rule. See FINRA Rules 12206(a) and 13206(a) (Time Limitation on Submission of Claims). This six-year eligibility rule applies to all arbitration claims, including those requesting expungement. Thus, if an associated person requests expungement of a CRD disclosure where six years have elapsed since the customer complaint, arbitration or civil litigation was initially reported, the arbitrator or panel should consider whether the claim is eligible for arbitration. In addition, FINRA Rules 12409 and 13413 (Jurisdiction of Panel and Authority to Interpret the Code) provide that the panel has the authority to interpret and determine the applicability of all provisions under the Codes. Such interpretations are final and binding upon the parties. Together, the rules grant arbitrators the authority to decide whether a claim is eligible for arbitration under the Codes. See *Howsam v. Dean Witter Reynolds*, 537 U.S. 79, 85-86 (2002) (finding that an arbitrator properly decides issues of eligibility).

Arbitrators should ensure that an expungement claim is eligible under the Codes and arbitrators may decide the eligibility issue on their own, rather than only in response to a party's motion. See *Horst v. FINRA*, No. A-18-777960-C (Dist. Ct. Nevada Oct. 25, 2018) (Order Denying Motion to Vacate Arbitration Award) (ruling that an arbitrator may raise sua sponte the eligibility issue, not only when a party to the arbitration raises it in a motion).

<sup>14</sup> Currently, on rare occasions, straight-in requests are filed against a customer. As discussed below, the proposed amendments would prohibit these filings. See *infra* Item 3.(a)II.A.2., "No Straight-in Requests Against Customers."

<sup>15</sup> Several questions on Forms U4 and U5 require associated persons to disclose certain investment-related, consumer-initiated (i) complaints and (ii) arbitrations and civil litigations, alleging sales practice violations. See Form U4, Question 14I, available at <https://www.finra.org/sites/default/files/form-u4.pdf> and Form U5, Question 7E, available at <https://www.finra.org/sites/default/files/form-u5.pdf>. These disclosures become part of the associated person's CRD record and are made available on BrokerCheck.

expungement hearings, the panel may receive information only from the associated person requesting expungement.

Further, FINRA is concerned that an increasing number of straight-in requests are being heard by a single arbitrator instead of a three-person panel.<sup>16</sup> FINRA believes that most expungement requests should be decided by a three-person panel. Expungement requests may be complex to resolve, particularly straight-in requests where customers typically do not participate in the expungement hearing. Thus, having three arbitrators available to ask questions, request evidence and to serve generally as fact-finders in the absence of customer input would help ensure that a complete factual record is created to support the arbitrators' decision in such expungement hearings.

In addition, FINRA is concerned that some associated persons are making second requests to expunge the same customer dispute information that they previously requested be expunged by a court or another arbitration panel. For example, an associated person may have a CRD disclosure that resulted from a customer's arbitration

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<sup>16</sup> An expungement request is a non-monetary or not specified claim. The Codes require that such claims are heard by a panel of three arbitrators, unless the parties agree in writing to one arbitrator. In addition, if a party requesting expungement adds a small monetary claim (of less than \$100,000) to the expungement request, the Codes require that such claims are heard by one arbitrator. See FINRA Rules 12401 and 13401. FINRA has amended the Codes to apply minimum fees to expungement requests, whether the request is made as part of the customer arbitration or the associated person files an expungement request in a separate arbitration. The amendments also apply a minimum process fee and member surcharge to straight-in requests, as well as a minimum hearing session fee to expungement-only hearings. See Securities Exchange Act Release No. 88945 (May 26, 2020), 85 FR 33212 (June 1, 2020) (Order Approving File No. SR-FINRA-2020-005). See also Regulatory Notice 20-25 (July 2020) (announcing a September 14, 2020 effective date) at <https://www.finra.org/rules-guidance/notices/20-25>.

claim, but because the associated person is not named as a party to the customer arbitration (“unnamed person”),<sup>17</sup> the associated person is not able to request expungement in the customer arbitration.<sup>18</sup> When a firm asks, on-behalf-of the unnamed person, that the arbitrators recommend expungement, the unnamed person, as a non-party in the customer arbitration, may subsequently argue that he or she did not receive adequate notice of the expungement request or an opportunity to participate in the earlier proceeding. The unnamed person may then file a new claim to expunge the same disclosure that the firm requested on the unnamed person’s behalf, despite the fact that the panel denied the expungement request in the prior matter.

FINRA believes that re-filing an expungement request that has been denied by an arbitration panel undermines the integrity of the arbitration process and the information in the CRD system. Arbitration awards are final and binding on the parties. If an associated

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<sup>17</sup> In 2009, the SEC approved amendments to Forms U4 and U5 to require, among other things, the reporting of allegations of sales practice violations made against unnamed persons. See Securities Exchange Act Release No. 59916 (May 13, 2009), 74 FR 23750 (May 20, 2009) (Order Approving File No. SR-FINRA-2009-008). Specifically, Forms U4 and U5 were amended to add questions to elicit whether the applicant or registered person, though not named as a respondent or defendant in a customer-initiated arbitration, was either mentioned in or could be reasonably identified from the body of the arbitration claim as a registered person who was involved in one or more of the alleged sales practice violations.

<sup>18</sup> If a broker is not named as a party in the customer arbitration, brokers may seek to expunge customer dispute information by: (1) asking a party to the arbitration, usually the firm, to request expungement on his or her behalf; (2) seeking to intervene in the customer arbitration; (3) initiating a new arbitration in which the unnamed person requests expungement and names the customer or firm as the respondent; or (4) going directly to court (without first going to arbitration).

person seeks to challenge an arbitration award, the associated person can do so by filing a motion to vacate in court.

In addition, some associated persons make second requests for expungement after withdrawing or deciding not to pursue an expungement request made in a customer arbitration, believing that another panel who has not heard the merits of the claim may be more likely to recommend expungement. FINRA is concerned about this practice of “arbitrator shopping,” particularly when associated persons withdraw an original expungement request after the arbitration panel has been made aware of evidence that could result in the denial of the expungement request.

On December 6, 2017, FINRA published Notice 17-42<sup>19</sup> to seek comment on a variety of changes to the process of arbitrating expungement requests, including establishing a roster of arbitrators with additional training and specific backgrounds or experience from which a panel would be selected to decide an associated person’s request for expungement of customer dispute information. The arbitrators from this roster would decide straight-in requests. As discussed below in Item 5, FINRA received 70 comment letters on Notice 17-42 that reflected a variety of perspectives and different suggestions regarding how to proceed. The proposed rule change is responsive to concerns raised by commenters and would include the following primary changes:

- Expungement Requests in Customer Arbitrations
  - An associated person named in a customer arbitration would be required to request expungement during the customer arbitration or forfeit the

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<sup>19</sup> See <http://www.finra.org/industry/notices/17-42>.

ability to request expungement of that same disclosure in any subsequent proceeding.

- A named party from a customer arbitration would be permitted to request expungement during the customer arbitration on-behalf-of an unnamed person pursuant to specified conditions and limitations.
  - If a named associated person or party on-behalf-of an unnamed person requests expungement during the customer arbitration and the arbitration closes by award after a hearing,<sup>20</sup> the panel from the customer arbitration would be required to decide the expungement request during the customer arbitration and issue a decision on the request in the award.
  - If a named associated person or party on-behalf-of an unnamed person requests expungement during the customer arbitration and the arbitration closes other than by award or by award without a hearing, an associated person may only pursue an expungement request by filing a straight-in request under the Industry Code against the member firm at which the associated person was associated at the time the dispute arose.
- Expungement Requests under the Industry Code
- All straight-in requests<sup>21</sup> would be required to be filed under the Industry Code against the member firm at which the associated person was

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<sup>20</sup> Under the Codes, a “hearing” means the hearing on the merits of the arbitration. See FINRA Rules 12100(o) and 13100(o).

<sup>21</sup> A straight-in request would include a request to expunge customer dispute information filed under the Industry Code: (1) by an associated person named in a customer arbitration after the customer arbitration closes other than by award or by award without a hearing; (2) arising from a customer complaint or civil

associated at the time the dispute arose and decided by a panel selected from a roster of arbitrators with enhanced experience and training (“Special Arbitrator Roster”).

- If an associated person withdraws a straight-in request after a panel from the Special Arbitrator Roster is appointed, the case would be closed with prejudice.

➤ Special Arbitrator Roster

- A three-person panel selected from the Special Arbitrator Roster would decide straight-in requests.
- The parties would not be permitted to agree to fewer than three arbitrators from the Special Arbitrator Roster to decide straight-in requests.
- Arbitrators on the Special Arbitrator Roster would be required to be public arbitrators who are eligible for the chairperson roster and who have fully met the following additional qualifications: (1) evidenced successful completion of, and agreement with, enhanced expungement training provided by FINRA; and (2) service as an arbitrator through award on at least four customer-initiated arbitrations administered by FINRA or by another self-regulatory organization (“SRO”) in which a hearing was held.

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litigation rather than a customer arbitration; or (3) by an associated person who was the subject of a customer arbitration, but unnamed, and where a named party in the customer arbitration did not request expungement on-behalf-of the unnamed associated person, or where a named party made an on-behalf-of request, but the customer arbitration closed other than by award or by award without a hearing.

- The Neutral List Selection System (“NLSS”) would randomly select the three public chairpersons from the Special Arbitrator Roster to decide straight-in requests. The first arbitrator selected would be the chair of the panel. The parties would not be permitted to stipulate to the use of pre-selected arbitrators.
  - An associated person who files a straight-in request would not be permitted to strike any arbitrators selected by NLSS or stipulate to the arbitrator’s removal, but would be permitted to challenge any arbitrator selected for cause. If an arbitrator is removed, NLSS would randomly select a replacement.
- Time Limitations on Requests for Expungement
- For customer dispute information reported to the CRD system after the effective date of the proposed rule change, the proposal would provide that an associated person would be barred from requesting expungement if: (1) more than two years have elapsed since the close of the customer arbitration or civil litigation that gave rise to the customer dispute information; or (2) there was no customer arbitration or civil litigation involving the customer dispute information, and more than six years have elapsed since the date that the customer complaint was initially reported to the CRD system.
  - For customer dispute information reported to the CRD system before the effective date of the proposed rule change, the proposal would require an associated person to request expungement as a straight-in request under

the Industry Code: (1) within two years of the effective date of the proposed rule change for disclosures that arose from a customer arbitration or civil litigation that closed on or prior to the effective date; and (2) within six years of the effective date of the proposed rule change for customer complaints initially reported to the CRD system on or prior to the effective date.

➤ Expungement Requests During a Simplified Arbitration

- If a party requests expungement during a simplified arbitration, the single arbitrator in the simplified arbitration would be required to decide the expungement request, regardless of how the simplified arbitration case closes (e.g., even if the case settles).
- If an associated person does not request expungement during the simplified arbitration, the request may be filed as a straight-in request under the Industry Code against the member firm at which the associated person was associated at the time the dispute arose, and be decided by a three-person panel randomly selected from the Special Arbitrator Roster.

➤ Expungement Hearings

- Establish procedural requirements that arbitrators and parties must follow for expungement hearings.

➤ State and Customer Notifications

- Establish requirements for notifying state securities regulators and customers of expungement requests.

Under the proposed rule change, an associated person would only be permitted to seek expungement of customer dispute information in the arbitration forum administered by FINRA by complying with the requirements of proposed Rules 12805 (expungement requests in a customer arbitration), 13805 (straight-in requests under the Industry Code) or 12800(d) (expungement requests in a simplified customer arbitration).

The proposed rule change, as revised in response to comments on Notice 17-42, is set forth in further detail below.<sup>22</sup>

## II. Proposed Rule Change

The discussion below of the proposed rule change is divided into six areas: (A) requests for expungement under the Customer Code; (B) straight-in requests under the Industry Code and the Special Arbitrator Roster; (C) limitations on expungement requests; (D) procedural requirements related to all expungement hearings; (E) notifications to customers and states regarding expungement requests; and (F) expungement requests during simplified customer arbitrations.

### A. Requests for Expungement under the Customer Code

FINRA Rule 12805 provides a list of requirements that arbitrators must meet before they may recommend expungement.<sup>23</sup> The rule does not, however, provide

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<sup>22</sup> The proposed rule change would apply to all members, including members that are funding portals or have elected to be treated as capital acquisition brokers (“CABs”), given that the funding portal and CAB rule sets incorporate the impacted FINRA rules by reference.

<sup>23</sup> FINRA Rule 12805 provides that a panel must comply with the following criteria before recommending expungement: (1) hold a recorded hearing to decide the issue of expungement; (2) review settlement documents, and consider the amount of payments made to any party and any other terms and conditions of the settlement; (3) indicate in the award which of the grounds in FINRA Rule 2080 is the basis for expungement and provide a brief written explanation of the reasons

guidance for associated persons on how and when they may request expungement during the customer arbitration, or on when arbitrators must make expungement determinations. The proposed rule change would amend FINRA Rule 12805 to set forth requirements for expungement requests filed by an associated person during a customer arbitration.

1. Expungement Requests During the Customer Arbitration

a. By a Respondent Named in a Customer Arbitration

Under current practice, an associated person who is named as a respondent in a customer arbitration (“named associated person”) may request expungement at any time during the customer arbitration or separately from the customer arbitration in a straight-in request.<sup>24</sup> If a named associated person requests expungement during the customer arbitration, does not withdraw the request and the case goes to hearing and closes by award, the panel in the customer arbitration will also decide the expungement request and

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for recommending expungement; and (4) assess all forum fees for hearing sessions in which the sole topic is the determination of the appropriateness of expungement against the parties requesting expungement. See also FINRA Rule 13805.

<sup>24</sup> There are several ways in which a named associated person may request expungement during a customer arbitration. The request may be included in the answer to the statement of claim that must be submitted within 45 days of receipt of the statement of claim, and may include other claims and remedies requested. See FINRA Rules 12303(a) and (b); see also FINRA Rules 13303(a) and (b). The expungement request may also be included in other pleadings (e.g., a counterclaim, a cross claim, or a third party claim) and must be filed with the Director of the Office of Dispute Resolution (“Director”) through the Party Portal. See FINRA Rules 12100(x) and 12300(b). The associated person may also request at any time during the case (outside of a pleading) that the panel consider the person’s expungement request during the hearing. Under FINRA Rule 12503, such a request is treated like a motion, which gives the other parties an opportunity to object. If there is an objection, the panel must decide the motion pursuant to FINRA Rule 12503(d)(5). See also FINRA Rules 13503 and 13503(d)(5).

include the decision as part of the customer's award.<sup>25</sup> If the customer arbitration does not close by award after a hearing (e.g., settles), and the associated person continues to pursue the expungement request, the panel from the customer arbitration may hold an expungement-only hearing as required by FINRA Rule 12805 to decide the expungement request.

Under the proposed rule change, if a named associated person seeks to request expungement of customer dispute information arising from the customer's statement of claim, the named associated person must make the expungement request during the customer arbitration.<sup>26</sup> As discussed below, the request would be subject to limitations on how and when the request may be made.<sup>27</sup> In addition, the Director would be authorized to deny the forum to expungement requests during a customer arbitration that do not arise out of the customer arbitration.<sup>28</sup> If the associated person does not request expungement during the customer arbitration, he or she would forfeit the opportunity to seek expungement of the same customer dispute information in any subsequent proceeding.<sup>29</sup>

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<sup>25</sup> Under the Codes, a customer's or claimant's damage request determines whether a single arbitrator or a three-person panel will consider and decide an arbitration case. See FINRA Rules 12401 and 13401. For ease of reference, when discussing expungement requests during customer arbitrations under proposed Rule 12805, unless otherwise specified, the rule filing uses the term "panel" to mean either a panel or single arbitrator.

<sup>26</sup> See proposed Rule 12805(a)(1)(A).

<sup>27</sup> See also infra Item 3.(a)II.C., "Limitations on Expungement Requests."

<sup>28</sup> See proposed Rules 12203(b) and 12805(a).

<sup>29</sup> See proposed Rule 12805(a).

FINRA is proposing to require that a named associated person request expungement during the customer arbitration because, if the arbitration closes by award after a hearing, the panel from the customer arbitration will be best situated to decide the related issue of expungement. Requiring the named associated person to request expungement in the customer arbitration increases the likelihood that a panel will have input from all parties and access to all of the evidence, testimony and other documents to make an informed decision on the expungement request.

FINRA recognizes that this requirement could result in some named associated persons filing expungement requests to preserve their right to make a request, regardless of the potential outcome. FINRA believes that the potential costs that would be incurred by associated persons, arbitrators and the forum if named associated persons file expungement requests to preserve the ability to request expungement are appropriate given the potential benefit of having customer input and a complete factual record for the panel to decide an expungement request. In addition, certain aspects of the proposed rule change may limit the filing of requests without regard to the potential outcome. For example, under the proposed rule change, named associated persons would be permitted to request expungement no later than 30 days before the first scheduled hearing.<sup>30</sup> This proposed amendment would provide the named associated person with a reasonable amount of time to consider, likely after receiving any discovery from the claimant,

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<sup>30</sup> See proposed Rule 12805(a)(1)(C); see also infra Item 3.(a)II.A.1.a.i., “Method of Requesting Expungement.”

whether to file the request because it could meet one or more of the FINRA Rule 2080(b)(1) grounds for expungement.<sup>31</sup>

i. Method of Requesting Expungement

The proposed rule change would limit how and when expungement requests may be made during the customer arbitration. Under the proposed rule change, if a named associated person requests expungement during the customer arbitration, the request must be included in the answer or a pleading requesting expungement.<sup>32</sup> If the request is included in the answer, it must be filed within 45 days of receipt of the customer's statement of claim in accordance with existing requirements under the Codes.<sup>33</sup> If the named associated person requests expungement in a pleading requesting expungement, the request must be filed no later than 30 days before the first scheduled hearing begins.<sup>34</sup>

FINRA believes the proposed rule change would provide a reasonable amount of time for the requesting party to make an informed decision about whether to request expungement while also providing the parties with reasonable case-preparation time, since the expungement issues will overlap with the issues raised by the customer's claim.

In addition, the proposed filing deadline would provide the Director a reasonable amount of time to notify state securities regulators of the expungement request.<sup>35</sup> If a

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<sup>31</sup> In addition, FINRA notes that the SEC has approved changes to FINRA rules to apply minimum fees to expungement requests. See supra note 16.

<sup>32</sup> See proposed Rule 12805(a)(1)(C)(i).

<sup>33</sup> See supra note 24.

<sup>34</sup> See proposed Rule 12805(a)(1)(C)(i).

<sup>35</sup> See proposed Rule 12805(b); see also infra Item 3.(a)II.E.3., "State Notification of Expungement Requests."

named associated person seeks to request expungement after the 30-day filing deadline, the panel would be required to decide whether to grant an extension and permit the request or whether to deny the request for expungement.<sup>36</sup>

ii. Required Contents of an Expungement Request

Under the proposed rule change, a request for expungement by a named associated person in a customer arbitration must include the applicable filing fee under the Codes.<sup>37</sup> In addition, a named associated person would be required to provide the CRD number of the party requesting expungement, each CRD occurrence number that is the subject of the request and the case name and docket number that gave rise to the disclosure, if applicable.<sup>38</sup>

The proposed rule change would also require the party requesting expungement to explain whether expungement of the same customer dispute information was (i) previously requested and, if so (ii) how it was decided.<sup>39</sup> This requirement would assist with implementation of the proposed prohibition on parties making second requests for

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<sup>36</sup> See proposed Rule 12805(a)(1)(C). The proposed amendments would provide that if the expungement request is not filed in a pleading no later than 30 days before the first scheduled hearing, then FINRA Rule 12309(b) would require the associated person to file a motion pursuant to FINRA Rule 12503, seeking an extension of the 30-day deadline to file the expungement request.

<sup>37</sup> See proposed Rule 12805(a)(1)(C)(ii)a.; see also supra note 16.

<sup>38</sup> See proposed Rule 12805(a)(1)(C)(ii)b.-d. An occurrence is a disclosure event that is reported to the CRD system via one or more Disclosure Reporting Pages. Each occurrence contains details regarding a specific disclosure event. An occurrence can have as many as three sources reporting the same event: Forms U4, U5 and U6.

<sup>39</sup> See proposed Rule 12805(a)(1)(C)(ii)e.

expungement, discussed in more detail below.<sup>40</sup> This proposed requirement is also consistent with language in the existing Guidance stating that arbitrators should ask a party requesting expungement whether an arbitration panel or a court previously denied expungement of the customer dispute information at issue and, if there was a prior denial, to deny the expungement request.<sup>41</sup>

Under the proposed rule change, if an expungement request fails to include any of the proposed requirements for requesting expungement, the request would be considered deficient and would not be served unless the deficiency is corrected.<sup>42</sup> These requirements would help ensure that FINRA, the panel and the parties understand who is requesting expungement and which disclosure is the subject of the request. Further, if the disclosure arose from a customer arbitration, the case name and docket number would provide the panel that is considering the expungement request with information about the dispute that gave rise to the disclosure that the party is seeking to expunge.

FINRA believes these proposed requirements for parties requesting expungement are necessary for the timely and orderly consideration of expungement requests as well as to maintain the integrity of the data in the CRD system.

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<sup>40</sup> See infra Item 3.(a)II.A.1.b.i., “Method of Requesting Expungement On-Behalf-Of an Unnamed Person.”

<sup>41</sup> See supra note 2.

<sup>42</sup> See proposed Rule 12307(a)(8)-(11) (setting forth reasons a claim may be deficient).

b. Expungement Requests by a Party Named in the Customer  
Arbitration On-Behalf-Of an Unnamed Person

The Codes do not specifically address expungement requests by a party named in a customer arbitration on-behalf-of an unnamed person.<sup>43</sup> Under current practice, a party to a customer arbitration may file an on-behalf-of request for expungement during the customer arbitration. If the party (typically, a firm) files the request and the customer arbitration closes by award after a hearing, the panel will decide the expungement request and include the decision in the award. If the customer arbitration does not close by award after a hearing (e.g., settles), either the requesting party or the unnamed person could ask the panel to consider and decide the expungement request before it disbands. In this circumstance, the panel from the customer arbitration will hold a separate expungement-only hearing to decide the expungement request.

The proposed rule change would codify the ability of a party in the customer arbitration to file an on-behalf-of request during a customer arbitration.<sup>44</sup> Under the proposed rule change, a party to a customer arbitration may file an on-behalf-of request that seeks to expunge customer dispute information arising from the customer's statement of claim, provided the request is eligible for arbitration under proposed Rule 12805.<sup>45</sup>

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<sup>43</sup> The proposed rule change would define an unnamed person as “an associated person, including a formerly associated person, who is identified in a Form U4, Form U5, or Form U6, as having been the subject of an investment-related, customer-initiated arbitration claim that alleged that the associated person or formerly associated person was involved in one or more sales practice violations, but who was not named as a respondent in the arbitration claim.” See proposed Rule 12100(ff).

<sup>44</sup> See proposed Rule 12805(a)(2).

<sup>45</sup> See proposed Rule 12805(a)(2)(B).

Filing an on-behalf-of request would be permissive, not mandatory.<sup>46</sup> However, as discussed below, if the named party and the unnamed person agree to such a request, FINRA would require them to sign a form consenting to the on-behalf-of request which would help ensure that the unnamed person is fully aware of the request and that the firm is agreeing to represent the unnamed person for the purpose of requesting expungement during the customer arbitration.<sup>47</sup>

i. Method of Requesting Expungement On-Behalf-Of an  
Unnamed Person

The unnamed person would be required to consent to the on-behalf-of request in writing.<sup>48</sup> In particular, the party filing an on-behalf-of request would be required to submit a signed Form Requesting Expungement on Behalf of an Unnamed Person (“Form”) and a statement requesting expungement with the Director.<sup>49</sup> The proposed rule change would not require that an on-behalf-of request be included in an answer or pleading requesting expungement (although it could be), since the request seeks relief on-

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<sup>46</sup> See proposed Rule 12805(a)(2)(A).

<sup>47</sup> A customer complaint can be reported to the CRD system via a Form U4 or Form U5. Pursuant to FINRA Rule 1010, an associated person should be made aware of the filing of a Form U4 and any amendments thereto by the associated person’s member firm. In addition, Article V, Section 3 of the FINRA By-Laws of the Corporation requires that a member firm provide an associated person a copy of an amended Form U5, including one reporting a customer complaint involving the associated person. FINRA also provides several methods for associated persons and former associated persons to check their records (e.g., by requesting an Individual CRD Snapshot or online through BrokerCheck).

<sup>48</sup> See proposed Rule 12805(a)(2)(A).

<sup>49</sup> See proposed Rule 12805(a)(2)(C)(ii). The unnamed person whose CRD record would be expunged and the party requesting expungement on the unnamed person’s behalf must sign the Form.

behalf-of a person who is not a party to the arbitration. However, the party making the request would be required to serve the request, which would include the Form, on all parties no later than 30 days before the first scheduled hearing.<sup>50</sup>

FINRA believes that requiring submission of the Form would help address the issue of an unnamed person not being notified of the on-behalf-of request. As discussed above, FINRA is concerned that some associated persons are filing arbitration claims seeking expungement of the same customer dispute information that was the subject of a previous denial by a panel of an on-behalf-of request. By signing the Form, the unnamed person would be consenting to the on-behalf-of request and agreeing to be bound by the panel's decision on the request.<sup>51</sup> In addition, the Form would provide that, if the customer arbitration closes by award after a hearing, the unnamed person would be barred from filing a request for expungement for the same customer dispute information in a subsequent proceeding, and the unnamed person's signature would serve as acknowledgement of this consequence.

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<sup>50</sup> See proposed Rule 12805(a)(2)(C)(iii). The 30-day deadline is the same as the proposed deadline for a named associated person to request expungement in a customer arbitration.

<sup>51</sup> By signing the Form, the unnamed person would also be agreeing to maintain the confidentiality of documents and information from the customer arbitration to which the unnamed person is given access and to adhere to any confidentiality agreements or orders associated with the customer arbitration. See proposed Rule 12805(a)(2)(D). Failure of the unnamed person to comply with this provision could subject the unnamed person to a claim for damages by an aggrieved party.

ii. Required Contents of an On-Behalf-Of Expungement Request

Under the proposed rule change, an on-behalf-of request would be required to include the same elements as a request for expungement by a named associated person during a customer arbitration.<sup>52</sup> Thus, the party requesting expungement on-behalf-of an unnamed person (typically, the firm) would be required to provide the applicable filing fee, the CRD number of the unnamed person, each CRD occurrence number that is the subject of the request and the case name and docket number that gave rise to the disclosure, if applicable. In addition, as discussed above, the party requesting expungement would be required to include the Form, signed by the unnamed person whose CRD record would be expunged and the party filing the request.

c. Deciding Expungement Requests during Customer Arbitrations

The proposed amendments would require that if there is a request for expungement by a named associated person or on-behalf-of an unnamed person during a customer arbitration, the panel from the customer arbitration must decide the expungement request if the customer arbitration closes by award after a hearing.<sup>53</sup> If the customer arbitration closes other than by award (e.g., settles) or by award without a hearing, the panel would not consider the expungement request.<sup>54</sup> Instead, the associated person would have the option of filing a request to expunge the same customer dispute

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<sup>52</sup> See proposed Rule 12805(a)(1)(C)(ii); see also supra Item 3.(a)II.A.1.a.ii., “Required Contents of an Expungement Request.”

<sup>53</sup> See proposed Rule 12805(a)(1)(D)(i) and (a)(2)(E)(i).

<sup>54</sup> See proposed Rules 12805(a)(1)(D)(ii) and (a)(2)(E)(ii).

information as a new claim under proposed Rule 13805 against the member firm at which he or she was associated at the time the customer dispute arose.<sup>55</sup> A panel from the Special Arbitrator Roster would decide such an expungement request, as discussed in more detail below.<sup>56</sup>

i. Panel Decides the Expungement Request if the Customer's Claim Closes by Award after a Hearing

Currently, if a named associated person requests expungement, or a party files an on-behalf-of request, and the customer's claim closes by award after a hearing, the panel may consider and decide the expungement request during the customer arbitration and issue its decision in the award. If, however, the party requesting expungement does not raise the issue of expungement during the hearing, the panel will not decide the request and may deem it withdrawn without prejudice.<sup>57</sup> In this instance, the associated person has the option to file the request again at a later date.

Under the proposed rule change, if, during the customer arbitration, a named associated person requests expungement or a party files an on-behalf-of request, and the customer's claim closes by award after a hearing, the panel in the customer arbitration

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<sup>55</sup> See supra note 54. Under the Codes, a "member" includes any broker or dealer admitted to membership in FINRA, whether or not the membership has been terminated, suspended, cancelled, revoked, the member has been expelled or barred from FINRA or the member is otherwise defunct. See FINRA Rules 12100(s) and 13100(q); see also Securities Exchange Act Release No. 88254 (February 20, 2020), 85 FR 11157 (February 26, 2020) (Order Approving File No. SR-FINRA-2019-027).

<sup>56</sup> See infra Item 3.(a)II.B.2., "Panel from the Special Arbitrator Roster Decides Requests Filed Under the Industry Code."

<sup>57</sup> See FINRA Rules 12702 and 13702.

would be required to consider and decide the request for expungement during the customer arbitration and issue a decision on the expungement request in the award.<sup>58</sup>

The panel would be required to decide the request even if the requesting party withdraws the request or fails to present a case in support of the request. In this instance, the panel must deny the expungement request with prejudice.<sup>59</sup> This requirement would foreclose the ability of associated persons to withdraw expungement requests to avoid having their requests decided by the panel who heard the evidence on the customer's arbitration claim, and then seeking to re-file the request and receive a new list of arbitrators and a potentially more favorable decision.

ii. Panel Does Not Decide Expungement if the Customer's  
Claim Closes Other than by Award or by Award without a  
Hearing

Currently, if a named associated person requests expungement or a party files an on-behalf-of request and the customer arbitration does not close by award after a hearing (e.g., settles) and the associated person or requesting party, if it is an on-behalf-of request, continues to pursue the expungement request, the panel from the customer arbitration will hold a separate expungement-only hearing to consider and decide the expungement request. If the named associated person or party requesting expungement

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<sup>58</sup> See proposed Rules 12805(a)(1)(D)(i) and 12805(a)(2)(E)(i).

<sup>59</sup> See proposed Rules 12805(a)(1)(D)(i) and 12805(a)(2)(E)(i). A party requesting expungement on-behalf-of an unnamed person may withdraw or not pursue an expungement request only with the written consent of the unnamed person. Under such circumstances, the panel would deny the expungement request with prejudice. See proposed Rule 12805(a)(2)(E)(i).

does not request that the panel hold a separate, expungement-only hearing, the panel may deem the request withdrawn without prejudice, and the associated person has the option to file the request again at a later date.

The proposed rule change would provide that if, during a customer arbitration, a named associated person requests expungement or a party files an on-behalf-of request and the customer arbitration closes other than by award or by award without a hearing, the panel from the customer arbitration would not be permitted to decide the expungement request.<sup>60</sup> Instead, the associated person would be required to seek expungement by filing a request to expunge the same customer dispute information as a straight-in request under proposed Rule 13805, where a panel from the Special Arbitrator Roster would decide the request.<sup>61</sup>

As discussed above, expungement requests may be complex to resolve, particularly straight-in requests where customers typically do not participate in the expungement hearing. Thus, having three arbitrators available to ask questions, request evidence and to serve generally as fact-finders in the absence of customer input would help ensure that a complete factual record is created to support the arbitrators' decision in such expungement hearings.

FINRA believes this is the right approach because the panel selected by the parties in the customer arbitration has not heard the full merits of the case and, therefore, may not bring to bear any special insights in determining whether to recommend

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<sup>60</sup> See proposed Rules 12805(a)(1)(D)(ii)a. and 12805(a)(2)(E)(ii)a.

<sup>61</sup> See infra Item 3.(a)II.B.2., "Panel from the Special Arbitrator Roster Decides Requests Filed Under the Industry Code."

expungement. In addition, customers or their representative have little incentive to participate in an expungement hearing once their case has settled. Requiring that an associated person file the expungement request as a straight-in request under the Industry Code to be heard and decided by a three-person panel selected from the Special Arbitrator Roster would strengthen the expungement framework. As discussed in more detail below, this corps of specially trained arbitrators would follow the procedures set forth in proposed Rule 13805 and make a decision about whether FINRA Rule 2080(b)(1) grounds exist to recommend expungement, keeping in mind the importance of maintaining the integrity of information in the CRD system.

## 2. No Straight-in Requests Against Customers

The proposed amendments would prohibit an associated person from filing a straight-in request against a customer.<sup>62</sup> Currently, straight-in requests are rarely filed against a customer.<sup>63</sup> FINRA does not believe that customers should be compelled to participate in a separate proceeding to decide an expungement request after the customer has resolved his or her arbitration claim or civil litigation, or submitted his or her customer complaint. Accordingly, the proposed amendments would prohibit an associated person from filing a straight-in request against a customer.

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<sup>62</sup> See proposed Rules 12805(a)(1)(D)(ii)c. and 12805(a)(2)(E)(ii)c.

<sup>63</sup> From January 2016 through June 2019, FINRA is able to identify 5,718 requests to expunge customer dispute information. Of those, 3,114 were filed as straight-in requests; 66 of the straight-in requests were filed solely against a customer. See infra Item 4.B., “Economic Baseline.”

### 3. No Intervening in Customer Arbitrations to Request Expungement

The proposed amendments would also prohibit unnamed persons from intervening in a customer arbitration and requesting expungement.<sup>64</sup> If the associated person is neither a party to the arbitration nor the subject of an on-behalf-of request by another party to the arbitration, the associated person should not be able to intervene in the customers' arbitration to request expungement. In these circumstances, the associated person's conduct is unlikely to be fully addressed by the parties during the customer arbitration, and FINRA does not believe that the customer should have the presentation of their case interrupted by an associated person's intervention to request expungement. In addition, there have been instances in customer arbitrations in which the unnamed person learns that the customer's arbitration case is nearing conclusion. The associated person (or his or her representative) then files a motion to intervene in the case to ask the panel to consider recommending expungement. As an unnamed person, the individual is not a party to the case and, therefore, has not made any arguments in support of the expungement request. Further, if the motion is granted, the parties to the case will be required to wait for a decision on the expungement request (which may necessitate another hearing) before their dispute is resolved, causing delay and additional cost to the parties.

Accordingly, under the proposed rule change, associated persons would be prohibited from intervening in a customer arbitration and requesting expungement. Instead, the unnamed person would have the option to file the request as a new claim

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<sup>64</sup> See proposed Rule 12805(a)(2)(E)(iii).

under proposed Rule 13805, where a panel from the Special Arbitrator Roster would decide the request.<sup>65</sup>

B. Straight-in Requests and the Special Arbitrator Roster

Under the proposed rule change, all requests to expunge disclosures arising from customer complaints or civil litigations would be required to be made as straight-in requests under proposed Rule 13805.<sup>66</sup> In addition, an associated person could request expungement of customer dispute information arising from a customer arbitration under proposed Rule 13805 if: (1) the associated person is named in the arbitration or is the subject of an on-behalf-of request and the customer arbitration closes other than by award or by award without a hearing; or (2) the associated person is the subject of a customer arbitration, but is neither named in the arbitration nor the subject of an on-behalf-of request, and the customer arbitration closes for any reason. If an associated person requests expungement under proposed Rule 13805, a three-person panel selected from the Special Arbitrator Roster in accordance with proposed Rule 13806, would decide the expungement request.<sup>67</sup>

1. Filing a Straight-in Request Under the Industry Code

a. Applicability

Under the proposed rule change, an associated person requesting expungement of customer dispute information under the Industry Code must make a straight-in request by

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<sup>65</sup> See infra Item 3.(a)II.B.2., “Panel from the Special Arbitrator Roster Decides Requests Filed Under the Industry Code.”

<sup>66</sup> See proposed Rule 13805(a)(1).

<sup>67</sup> See infra Item 3.(a)II.B.2.a. and b. (discussing eligibility requirements for and composition of the Special Arbitrator Roster).

filing a statement of claim in accordance with FINRA Rule 13302 against a member firm at which he or she was associated at the time the customer dispute arose, unless the request is ineligible for arbitration under proposed Rule 13805(a)(2).<sup>68</sup> Thus, the only way to request expungement of customer dispute information under the Industry Code would be to file the request under proposed Rule 13805.

The requirement that the associated person file the straight-in request against the member firm at which he or she was associated at the time the customer dispute arose would help ensure that there is a connection between the respondent firm and the subject of the expungement request. For example, the firm at which the person requesting expungement was associated at the time the dispute arose should have knowledge of the dispute and access to documents or other evidence relating to the dispute. In addition, the proposed requirement would help ensure that the panel from the Special Arbitrator Roster would be able to request evidence from a member firm with information that is relevant to the expungement request. If the requisite connection is not present, the Director would be authorized to deny the forum to the request.<sup>69</sup>

b. Required Contents of Straight-in Requests

The required contents of a straight-in request would be the same as those required for expungement requests filed under proposed Rule 12805.<sup>70</sup> Thus, the associated

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<sup>68</sup> See proposed Rule 13805(a)(1). FINRA Rule 13302 provides, in relevant part, that to initiate an arbitration, a claimant must file with the Director a signed and dated Submission Agreement, and a statement of claim specifying the relevant facts and remedies requested through the Party Portal.

<sup>69</sup> See proposed Rule 13203(b).

<sup>70</sup> See supra Item 3.(a)II.A.1.a.ii., “Required Contents of an Expungement Request.”

person's straight-in request would be required to contain the applicable filing fee;<sup>71</sup> the CRD number of the party requesting expungement; each CRD occurrence number that is the subject of the request; the case name and docket number that gave rise to the disclosure, if applicable; and an explanation of whether expungement of the same customer dispute information was previously requested and, if so, how it was decided.<sup>72</sup> In addition, as discussed below, the proposed rule change would impose limitations on when such requests may be made.<sup>73</sup>

2. Panel from the Special Arbitrator Roster Decides Requests Filed Under the Industry Code

If a straight-in request is filed in accordance with proposed Rule 13805, a three-person panel selected from the Special Arbitrator Roster pursuant to proposed Rule 13806 would be required to hold an expungement hearing, decide the expungement

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<sup>71</sup> FINRA would not assess a second filing fee when an associated person files a straight-in request if the associated person or the requesting party in the case of an on-behalf-of request, had previously paid the filing fee to request expungement of the same customer dispute information during a customer arbitration.

<sup>72</sup> See proposed Rule 13805(a)(3).

<sup>73</sup> See infra Item 3.(a)II.C., "Limitations on Expungement Requests." As discussed in more detail below in Item 3.(a)II.C., the straight-in request would be ineligible for arbitration under the Industry Code if: (1) a panel held a hearing to consider the merits of the associated person's request for expungement of the same customer dispute information; (2) a court previously denied the associated person's request to expunge the same customer dispute information; (3) the customer arbitration, civil litigation or customer complaint that gave rise to the customer dispute information is not concluded; (4) more than two years has elapsed since the customer arbitration or civil litigation that gave rise to the customer dispute information has closed; or (5) there was no customer arbitration or civil litigation that gave rise to the customer dispute information and more than six years has elapsed since the date that the customer complaint was initially reported to the CRD system. See proposed Rule 13805(a)(2).

request and issue an award.<sup>74</sup> The proposed amendments would also provide that if the associated person withdraws or does not pursue the request, the panel would be required to deny the expungement request with prejudice.<sup>75</sup> This requirement would foreclose the ability of associated persons to withdraw expungement requests to avoid having their requests decided by the panel, and then seeking to re-file the request with the hope of obtaining a potentially more favorable panel.

The proposed rule change would include several requirements to help ensure that arbitrators on the Special Arbitrator Roster have the qualifications and training to decide straight-in requests.

a. Eligibility Requirements for the Special Arbitrator Roster

Arbitrators on the Special Arbitrator Roster would be public arbitrators who are eligible for the chairperson roster.<sup>76</sup> Public arbitrators are not employed in the securities industry and do not devote 20 percent or more of their professional work to the securities industry or to parties in disputes concerning investment accounts or transactions or employment relationships within the financial industry.<sup>77</sup> Arbitrators are eligible for the chairperson roster if they have completed chairperson training provided by FINRA and: (1) have a law degree and are a member of a bar of at least one jurisdiction and have served as an arbitrator through award on at least one arbitration administered by an SRO in which hearings were held; or (2) have served as an arbitrator through award on at least

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<sup>74</sup> See proposed Rule 13805(a)(4).

<sup>75</sup> See supra note 74.

<sup>76</sup> See proposed Rule 13806(b); see also FINRA Rule 12400(c).

<sup>77</sup> See supra note 7.

three arbitrations administered by an SRO in which hearings were held.<sup>78</sup> These requirements would help ensure that the persons conducting the expungement hearing are impartial and experienced in managing and conducting arbitration hearings in the forum.<sup>79</sup>

Further, the public chairpersons must have evidenced successful completion of, and agreement with, enhanced expungement training provided by FINRA.<sup>80</sup> FINRA currently provides an Expungement Training module for arbitrators.<sup>81</sup> This training, however, would be expanded for arbitrators seeking to qualify for the Special Arbitrator Roster. This would allow FINRA to further emphasize, with the subset of arbitrators on

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<sup>78</sup> See FINRA Rule 12400(c). For purposes of this proposed rule change, public arbitrators who are eligible for the chairperson roster would include those arbitrators who have met the chairperson eligibility requirements of FINRA Rule 12400(c), regardless of whether they have already served as a chair on an arbitration case.

<sup>79</sup> The Task Force suggested that the arbitrators on its recommended special arbitration panel be chair-qualified, in part because of the training that arbitrators must complete before they can be added to the chairperson roster. See FINRA's "Advanced Arbitrator Training," available at <https://www.finra.org/arbitration-mediation/advanced-arbitrator-training>. See also supra note 12.

<sup>80</sup> See proposed Rule 13806(b)(2)(A).

<sup>81</sup> See supra note 79. FINRA requires arbitrators to take mandatory online training that focuses on the Guidance. In addition, among other tools, FINRA provides Neutral Workshops (an online discussion on specific arbitration topics) and articles in The Neutral Corner (a quarterly publication that provides arbitrators and mediators with updates on important rules and procedures within the FINRA arbitration forum) to keep arbitrators informed about the expungement process and to emphasize the critical role that arbitrators play in maintaining the relevancy and integrity of disclosure information in the CRD system and BrokerCheck. See Neutral Workshop Audio and Video Files, Spring 2019 Neutral Workshop: Expungement of Customer Dispute Information, <https://www.finra.org/arbitration-mediation/neutral-workshop-audio-and-video-files>; The Neutral Corner, <https://www.finra.org/arbitration-mediation/neutral-corner-view>.

the Special Arbitrator Roster, the unique, distinct role they play in deciding whether to recommend a request to expunge customer dispute information from a broker's CRD record, and that expungement should be granted in limited circumstances and only if one or more of the grounds in FINRA Rule 2080(b)(1) is met.

Under the proposed amendments, arbitrators on the Special Arbitrator Roster would also be required to have served as an arbitrator through award on at least four customer-initiated arbitrations administered by FINRA or by another SRO in which a hearing was held.<sup>82</sup> FINRA believes that if an arbitrator has served on four arbitrations through to award, it would indicate that the arbitrator has gained the knowledge and experience in the forum to conduct hearings.<sup>83</sup>

b. Composition of the Panel

The proposed amendments would require that three randomly-selected members of the Special Arbitrator Roster decide all expungement requests filed under proposed Rule 13805.<sup>84</sup> As discussed above, expungement requests may be complex to resolve, particularly straight-in requests where customers typically do not participate in the expungement hearing. Thus, having three arbitrators available to ask questions, request evidence and generally to serve as fact-finders in the absence of customer input would

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<sup>82</sup> See proposed Rule 13806(b)(2)(B). The hearing requirement would exclude hearings conducted under the special proceeding option of the simplified arbitration rules. See FINRA Rule 12800(c)(3)(B).

<sup>83</sup> In 2019, 85 percent of FINRA customer arbitrations closed other than by award. See Dispute Resolution Statistics, "How Arbitration Cases Close," available at <https://www.finra.org/arbitration-mediation/dispute-resolution-statistics>.

<sup>84</sup> See proposed Rule 13806(b)(1).

help ensure that a complete factual record is created to support the arbitrators' decision in such expungement hearings.<sup>85</sup>

To minimize the potential for party influence in the arbitrator selection process, the proposed rule change would require NLSS randomly to select the three public chairpersons from the Special Arbitrator Roster to decide an expungement request filed by an associated person.<sup>86</sup> The parties would not be permitted to agree to fewer than three arbitrators. The associated person would not be permitted to strike any arbitrators selected by NLSS nor stipulate to their removal,<sup>87</sup> but would be permitted to challenge any arbitrator selected for cause.<sup>88</sup> If an arbitrator is removed, NLSS would randomly select a replacement.<sup>89</sup>

FINRA believes that the current process for selecting arbitrators—striking and combining ranked lists—would not be appropriate to use to select arbitrators to decide straight-in requests.<sup>90</sup> In arbitrations outside of the expungement context, the parties are

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<sup>85</sup> See supra Item 3.(a)I.C., “Concerns Regarding Expungement” (discussing the importance of having a three-person panel decide straight-in requests).

<sup>86</sup> See proposed Rule 13806(b)(1). The first arbitrator selected would be the chair of the panel. See proposed Rule 13806(b)(3).

<sup>87</sup> The parties also would not be permitted to stipulate to the use of pre-selected arbitrators (i.e., arbitrators that the parties find on their own to use in their cases). See proposed Rule 13806(b)(1).

<sup>88</sup> See proposed Rule 13806(b)(4). In addition, before the first hearing session begins, the Director may remove an arbitrator for conflict of interest or bias, either upon request of a party or on the Director's own initiative. See FINRA Rule 12407(a).

<sup>89</sup> See proposed Rule 13806(b)(4); see also FINRA Rules 12402(g) and 12403(g).

<sup>90</sup> See generally FINRA Rules 12402 and 12403.

typically adverse, which means that during arbitrator selection, each side may rank arbitrators on the lists whom they believe may be favorable to their case.<sup>91</sup> The adversarial nature of the proceedings serves to minimize the impact of each party's influence in arbitrator selection.<sup>92</sup> In contrast, a straight-in request filed by an associated person against a firm may not be adversarial in nature. In addition, typically the customer or customer's representative will not appear at the expungement hearing.

FINRA recognizes that the proposed arbitrator selection process for straight-in requests would limit the associated person and member firm's input on arbitration selection. However, the arbitrators on the Special Arbitrator Roster would have the experience, qualifications and training necessary to conduct a fair and impartial expungement hearing in accordance with the proposed rules, and to render a recommendation based on a complete factual record developed during the expungement hearing. FINRA believes that the higher standards that the arbitrators must meet to serve on the Special Arbitrator Roster should mitigate the impact of the absence of party input on the selection of arbitrators. In addition, associated persons and member firms would still be permitted to challenge any arbitrator for cause.<sup>93</sup>

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<sup>91</sup> See infra note 188.

<sup>92</sup> Once the parties have ranked the arbitrators, the Director creates a combined ranked list of arbitrators based on the parties' numerical rankings. The Director appoints the highest-ranked available arbitrator from the combined list. See FINRA Rules 12402(e) and (f) and 12403(d) and (e).

<sup>93</sup> See proposed Rule 13806(b)(4).

C. Limitations on Expungement Requests

Currently, Rules 12805 and 13805 do not address when a party would not be permitted to file an expungement request in the forum.<sup>94</sup> The Guidance, however, describes several circumstances in which an expungement request should be ineligible for arbitration. The proposed rule change would incorporate the limitations contained in the Guidance as well as add time limits to when an associated person may file a straight-in request.

1. Limitations Applicable to Both Straight-in Requests and Expungement Requests During a Customer Arbitration

The Guidance provides that if a panel or a court has issued an award or decision denying an associated person's expungement request, the associated person may not request expungement of the same customer dispute information in another arbitration. In particular, the Guidance states that arbitrators should ask a party requesting expungement whether an arbitration panel or a court previously denied expungement of the customer dispute information at issue and, if there has been a prior denial, the arbitration panel must deny the expungement request.<sup>95</sup>

The proposed rule change would codify the Guidance by providing that an associated person may not file a request for expungement of customer dispute information if (1) a panel held a hearing to consider the merits of the associated person's expungement request for the same customer dispute information or (2) a court of

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<sup>94</sup> But see supra note 13 (describing time limits that apply to all arbitration claims, including expungement requests).

<sup>95</sup> See supra note 2.

competent jurisdiction previously denied the associated person's request to expunge the same customer dispute information.<sup>96</sup> These proposed amendments would prevent an associated person from forum shopping, or seeking to return to the arbitration forum administered by FINRA, to garner a favorable outcome on his or her expungement request.<sup>97</sup>

## 2. Limitations Applicable to Straight-in Requests Only

As discussed below, under the proposed amendments, three additional limitations would apply to straight-in requests.

### i. No Straight-In Request If a Customer Arbitration Has Not Concluded

The Guidance provides that an associated person may not file a separate request for expungement of customer dispute information arising from a customer arbitration until the customer arbitration has concluded. The proposed rule change would codify and expand upon the Guidance by providing that an associated person may not file a straight-in request under proposed Rule 13805 if the customer arbitration, civil litigation or customer complaint that gave rise to the customer dispute information has not closed.<sup>98</sup>

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<sup>96</sup> See proposed Rules 12805(a)(1)(B) and 13805(a)(2)(A). The proposed rule change would require that the requesting party provide information about previous expungement requests and how such requests were decided. See, e.g., proposed Rule 12805(a)(1)(C)(ii)e.

<sup>97</sup> FINRA notes that if a panel holds a hearing that addresses the merits of an associated person's request for expungement, the Director may deny the forum to any subsequent request by the associated person or another party on behalf of the associated person to expunge the same customer dispute information. See FINRA Rules 12203(a) and 13203(a); see also proposed Rules 12203(b) and 13203(b).

<sup>98</sup> See proposed Rule 13805(a)(2)(A)(iii).

The proposed rule change would prevent an associated person from obtaining a decision on an expungement request while the customer arbitration is still ongoing. This change would help ensure that a decision in the customer arbitration is issued before the decision on the expungement request and avoid the possibility of inconsistent awards. The proposed amendment would also help ensure that the arbitrators who will decide the straight-in request are able to consider the final factual record from the customer arbitration.

ii. Time Limits Applicable to Disclosures Arising After the Effective Date of the Proposed Rule Change

FINRA is aware that a number of expungement requests are filed many years after a customer arbitration closes or the reporting of a customer complaint in the CRD system.<sup>99</sup> To encourage timelier filing of expungement requests, the proposed amendments would establish time limits for expungement requests that are specifically tied to the closure of customer arbitrations and civil litigations, or the reporting of customer complaints in the CRD system, as applicable.<sup>100</sup> The proposed time limits should help encourage customer participation in expungement proceedings and help

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<sup>99</sup> See infra Item 4.C.4., “Time Limits for Straight-in Requests – Quantitative Description.”

<sup>100</sup> FINRA Rules 12206 and 13206 provide that no claim shall be eligible for submission to arbitration where six years have elapsed from the occurrence or event giving rise to the claim. Under these Rules, the panel has discretion to determine if the claim, including an expungement request, is eligible for arbitration. See supra note 13. As discussed below, if the proposed rule change is approved by the Commission, this six-year eligibility rule would continue to apply to requests to expunge customer dispute information that arose prior to the effective date of the proposed rule change.

ensure that straight-in requests are brought before relevant evidence and testimony becomes stale or unavailable.<sup>101</sup>

a. Two Years from the Close of a Customer Arbitration or  
Civil Litigation

Under the proposed rule change, an associated person would be required to file a straight-in request within two years of the close of the customer arbitration or civil litigation that gave rise to the customer dispute information.<sup>102</sup> A two-year period would provide a reasonable amount of time for associated persons and their firms to gather the documents, information and other resources required to file the expungement request. In addition, the two-year period would help ensure that the expungement hearing is held close enough in time to the customer arbitration, when information regarding the customer arbitration is available and in a timeframe that could increase the likelihood for the customer to participate if he or she chooses to do so. The shorter timeframe, therefore, could provide panels with more complete factual records on which to base their expungement decisions. At the same time, it would allow the associated person time to determine whether to seek expungement by filing a straight-in request.

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<sup>101</sup> All customers from a customer arbitration or civil litigation, and all customers who initiated a customer complaint, would be notified of the expungement request and encouraged to attend and provide their input. See proposed Rule 13805(b)(1)(A).

<sup>102</sup> See proposed Rule 13805(a)(2)(A)(iv).

b. Six Years from the Date a Customer Complaint Is Reported  
to the CRD System

Under the proposed rule change, an associated person would be prohibited from filing a straight-in request to expunge a customer complaint where more than six years has elapsed since the customer complaint was initially reported to the CRD system and there was no customer arbitration or civil litigation that gave rise to the customer dispute information.<sup>103</sup>

Consistent with FINRA's current eligibility rules,<sup>104</sup> FINRA believes that six years from the date a customer complaint is initially reported to the CRD system should provide a reasonable amount of time for the associated person to bring an expungement claim. The six-year period would allow firms to complete their investigation of the customer complaint and close it in the CRD system; for the complaint to evolve, or not evolve, into an arbitration; and for the associated person to determine whether to proceed with a request to expunge the complaint. The proposed six-year time limit would also provide a reasonable time limit to encourage customer participation and help ensure the availability of evidence related to customer complaints.

iii. Time Limits Applicable to Disclosures Arising on or Prior to the  
Effective Date of the Proposed Rule Change

If the Commission approves the proposed rule change, the proposal would also establish time limits for requests to expunge customer dispute information arising from

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<sup>103</sup> See proposed Rule 13805(a)(2)(A)(v).

<sup>104</sup> See supra note 13.

customer arbitrations and civil litigations that close, and for customer complaints that were initially reported to the CRD system, on or prior to the effective date of the proposed rule change.

Specifically, the proposed amendments would provide that if an expungement request is otherwise eligible under the six-year limitation period of FINRA Rule 13206(a), an associated person would be permitted to file a straight-in request under the Industry Code if: (1) the request for expungement is made within two years of the effective date of proposed rule change, and the disclosure to be expunged arises from a customer arbitration or civil litigation that closed on or prior to the effective date;<sup>105</sup> or (2) the request for expungement is made within six years of the effective date of the proposed rule change, and the disclosure to be expunged arises from a customer complaint initially reported to the CRD system on or prior to its effective date.<sup>106</sup>

### 3. Director's Authority to Deny the Forum

If an associated person files an expungement request that is ineligible for arbitration under proposed Rules 12805 and 13805, the proposed rule change would give the Director the express authority to deny the use of FINRA's arbitration forum to decide the request.<sup>107</sup> If the expungement request is ineligible for arbitration because a court or panel has decided previously an expungement request related to the same customer

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<sup>105</sup> See proposed Rule 13805(a)(2)(B)(i).

<sup>106</sup> See proposed Rule 13805(a)(2)(B)(ii).

<sup>107</sup> See proposed Rules 12203(b) and 13203(b). The panel would continue to have the authority to resolve any questions regarding eligibility of such claims under Rules 12206 and 13206, as applicable. See supra note 13.

dispute information, the Director would deny the forum with prejudice as the request would be an attempt to receive a second decision on a request that had been decided previously on the merits. The Director would also deny the forum with prejudice if an expungement request is ineligible under the proposed time limitations.

If the request is ineligible because a customer arbitration that involves the same customer dispute information is not concluded, the Director would deny the forum without prejudice so that the associated person could file the request (or a party could file an on-behalf-of request) in the customer arbitration or as a straight-in request after the customer arbitration concludes.

D. Procedural Requirements Relating to All Expungement Hearings

The Codes currently provide a list of requirements panels must follow in order to decide an expungement request.<sup>108</sup> In addition, the Guidance provides best practices that arbitrators should follow when deciding expungement requests. To guide further the arbitrators' decision-making, the proposed rule change would expand the expungement hearing requirements currently in FINRA Rules 12805 and 13805 to incorporate the relevant provisions from the Guidance. The proposed amendments would apply to all expungement hearings.<sup>109</sup>

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<sup>108</sup> See supra note 23.

<sup>109</sup> See proposed Rules 12805(c) and 13805(c). The proposed procedural requirements for expungement hearings would apply to all expungement hearings, including hearings held during a customer arbitration or simplified arbitration (see infra Item 3.(a)II.F., "Expungement Requests During Simplified Customer Arbitrations") that consider an expungement request, and expungement hearings conducted by a panel from the Special Arbitrator Roster.

1. Recorded Hearing Sessions

The Codes require a panel that is deciding an expungement request to hold a recorded hearing session (by telephone or in person) regarding the appropriateness of expungement.<sup>110</sup> Consistent with current practice, the proposed rule change would add the ability to hold a recorded hearing session by video conference.<sup>111</sup> Further, the proposed rule change would clarify that a panel would not be limited in the number of hearing sessions it should hold to decide the expungement request.<sup>112</sup>

2. Associated Person's Appearance

The proposed rule change would require the associated person who is seeking expungement of the customer dispute information to appear personally at the expungement hearing.<sup>113</sup> A party requesting expungement on behalf of an unnamed person would also be required to appear at the hearing. The panel would determine whether an appearance should be by telephone, in person, or by video conference.

As the associated person is requesting the permanent removal of information from his or her CRD record, FINRA believes the associated person whose CRD record would be expunged must personally participate in the expungement hearing to respond to questions from the panel and those customers who choose to participate. Rather than restrict the method of appearance, FINRA is proposing to provide the panel with the

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<sup>110</sup> See FINRA Rules 12805(a) and 13805(a).

<sup>111</sup> See proposed Rules 12805(c)(1) and 13805(c)(1).

<sup>112</sup> See *supra* note 111.

<sup>113</sup> See proposed Rules 12805(c)(2) and 13805(c)(2). The requirement to appear personally at the expungement hearing would also apply to an unnamed person who seeks to have his or her customer dispute information expunged.

authority to decide which method of appearance would be the most appropriate for the particular case. FINRA believes that providing flexibility as to the method of appearance would encourage appropriate fact-finding by the arbitrators and generally strengthen the process.

### 3. Customer's Participation during the Expungement Hearing

The Guidance states that it is important to allow customers and their representatives to participate in the expungement hearing if they wish to do so.<sup>114</sup>

Specifically, the Guidance provides that arbitrators should:

- Allow the customers and their representatives to appear at the expungement hearing;
- Allow the customer to testify (telephonically, in person, or other method) at the expungement hearing;
- Allow the representative for the customer or a pro se customer to introduce documents and evidence at the expungement hearing;
- Allow the representative for the customer or a pro se customer to cross-examine the broker or other witnesses called by the party seeking expungement; and

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<sup>114</sup> The Guidance directs arbitrators to permit customers and their counsel to participate in the expungement hearing. See supra note 2. FINRA Rules 12208 and 13208 permit a party to be represented pro se, by an attorney or by a person who is not an attorney. The proposed amendments would replace the term “counsel” with “representative.” See also Securities Arbitration—Should You Hire an Attorney? (Jan. 3, 2019), <https://www.finra.org/investors/insights/securities-arbitration>.

- Allow the representative for the customer or a pro se customer to present opening and closing arguments if the panel allows any party to present such arguments.

The proposed rule change would codify these provisions of the Guidance. The proposed rule change would make clear that all customers whose customer arbitrations, civil litigations and customer complaints gave rise to the customer dispute information that is a subject of the expungement request have a right to representation and are entitled to appear at the expungement hearing.<sup>115</sup> The proposed rule change would provide that the customer can appear by telephone, in person, by video conference or other means convenient to the customer and customer's representative.<sup>116</sup> By providing customers with options for how to participate in hearings, FINRA seeks to make it easier for customers to participate and, thereby, encourage customer participation. Customer participation during an expungement hearing provides the panel with important information and perspective that it might not otherwise receive.

In addition, the proposed rule change would provide that customers must be allowed to testify at the expungement hearing and be questioned by the customer's representative.<sup>117</sup> If a customer testifies, the associated person or a party requesting expungement on-behalf-of an unnamed person would be allowed to cross-examine the

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<sup>115</sup> See proposed Rules 12805(c)(3)(A) and 12805(c)(4); see also proposed Rules 13805(c)(3)(A) and 13805(c)(4). The proposed rule change would make clear that customers also have the option to provide their position on the expungement request in writing in lieu of attending the hearing.

<sup>116</sup> See proposed Rules 12805(c)(3)(B) and 13805(c)(3)(B).

<sup>117</sup> See proposed Rules 12805(c)(5)(A) and 13805(c)(5)(A).

customer.<sup>118</sup> Similarly, the customer or customer's representative would be permitted to cross-examine the associated person or party requesting expungement on-behalf-of an unnamed person and any witnesses called by the associated person or party requesting expungement on-behalf-of an unnamed person during the expungement hearing.<sup>119</sup> If the customer introduces any evidence at the expungement hearing, the associated person or party requesting expungement on-behalf-of an unnamed person could object to the introduction of the evidence, and the panel would decide any objections.<sup>120</sup> The customer or customer's representative would also be permitted to present opening and closing arguments if the panel permits any party to present such arguments.<sup>121</sup> FINRA believes the proposal strikes the right balance of allowing the customer to participate fully in the hearing and giving the associated person or party requesting expungement on-behalf-of an unnamed person the opportunity to substantiate arguments in support of the expungement request.

#### 4. Panel Requests for Additional Documents or Evidence

Arbitrators on the panel do not conduct their own research when hearing an arbitration case; instead, they review the materials provided by the parties. If they need more information, they can request it from the parties.<sup>122</sup> In deciding an expungement request, particularly in cases that settle before an evidentiary hearing or in cases where

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<sup>118</sup> See supra note 117.

<sup>119</sup> See proposed Rules 12805(c)(5)(C) and 13805(c)(5)(C).

<sup>120</sup> See proposed Rules 12805(c)(5)(B) and 13805(c)(5)(B).

<sup>121</sup> See proposed Rules 12805(c)(5)(D) and 13805(c)(5)(D).

<sup>122</sup> See proposed Rules 12805(c)(6) and 13805(c)(6).

the customer does not participate in the expungement hearing, the arbitrator's role as fact-finder is critical. Given this significant role, arbitrators must ensure that they have all of the information necessary to make a fully-informed decision on the expungement request on the basis of a complete factual record. Thus, the proposed rule change would codify the ability of arbitrators to request from the associated person, or other party requesting expungement, any documentary, testimonial or other evidence that they deem relevant to the expungement request.<sup>123</sup>

#### 5. Review of Settlement Documents

Current FINRA Rule 12805(b) provides that, in the event the parties from the customer arbitration settle their case, the panel considering the expungement request must review the settlement documents and consider the amount of payments made to any party and any other terms and conditions of the settlement.<sup>124</sup> The proposed rule change would retain this requirement.<sup>125</sup>

In addition, the Guidance encourages arbitrators to inquire and fully consider whether a party conditioned a settlement of the arbitration upon agreement not to oppose the request for expungement in cases in which the customer does not participate in the

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<sup>123</sup> See supra note 122. The Guidance also suggests that arbitrators should ask the associated person seeking expungement or the party seeking expungement on an associated person's behalf to provide a current copy of the BrokerCheck report for the person whose record would be expunged, paying particular attention to the "Disclosure Events" section of the report. See supra note 2. FINRA continues to encourage arbitrators to request a current copy of the associated person's BrokerCheck report.

<sup>124</sup> The panel should review all settlement documents related to the customer dispute information the associated person is seeking to be expunged, regardless of whether the associated person was a party to the settlement.

<sup>125</sup> See proposed Rules 12805(c)(7) and 13805(c)(7).

expungement hearing or the requesting party states that a customer has indicated that he or she will not oppose the expungement request. The proposed rule change would codify this language in the Guidance.<sup>126</sup> Conditioned settlements violate FINRA Rule 2081 and may be grounds to deny an expungement request.<sup>127</sup>

## 6. Awards

Current FINRA Rules 12805(c) and 13805(c) require that the panel indicate in the arbitration award which of the FINRA Rule 2080 grounds for expungement serves as the basis for its expungement recommendation and provide a brief written explanation of the reasons for its finding that one or more FINRA Rule 2080 grounds for expungement applies to the facts of the case. The proposed rule change would retain this requirement, but would remove the word “brief” to indicate to the panel that it must provide enough detail in the award to explain its rationale for recommending expungement.<sup>128</sup> As the Guidance suggests, the explanation must be complete and not solely a recitation of one of the FINRA Rule 2080 grounds or language provided in the expungement request.

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<sup>126</sup> See proposed Rules 12805(c)(7) and 13805(c)(7).

<sup>127</sup> FINRA Rule 2081 provides that no member firm or associated person shall condition or seek to condition settlement of a dispute with a customer on, or to otherwise compensate the customer for, the customer's agreement to consent to, or not to oppose, the member's or associated person's request to expunge such customer dispute information from the CRD system. See also Prohibited Conditions Relating to Expungement of Customer Dispute Information FAQ, <https://www.finra.org/arbitration-mediation/faq/prohibited-conditions-relating-expungement-customer-dispute-information>.

<sup>128</sup> In addition, all awards rendered under the Codes, including awards recommending expungement, must comply with the requirements of FINRA Rules 12904 or 13904.

In addition, the proposed rule change would incorporate language from the Guidance that the panel’s explanation should identify any specific documentary, testimonial or other evidence relied on in recommending expungement.<sup>129</sup>

The proposed rule change would also make clarifying revisions to FINRA Rules 12805(c) and 13805(c). The proposed amendments would indicate that the FINRA Rule 2080 grounds that the panel must indicate serve as the basis for the expungement order are the grounds found in paragraph (b)(1) of FINRA Rule 2080.<sup>130</sup> The proposed amendments would also provide that the panel would “recommend” rather than “grant” expungement.<sup>131</sup>

#### 7. Forum Fees

The proposed rule change would retain the current requirements in FINRA Rules 12805(d) and 13805(d) that addresses how forum fees are assessed in expungement hearings.<sup>132</sup> Specifically, the panel must assess against the parties requesting expungement all forum fees for each hearing in which the sole topic is the determination of the appropriateness of expungement.

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<sup>129</sup> See proposed Rules 12805(c)(8) and 13805(c)(8).

<sup>130</sup> See infra note 237, and accompanying text.

<sup>131</sup> The word “recommend” more accurately describes the panel’s role in the expungement process, consistent with FINRA’s longstanding practice to state in expungement awards that the arbitrators “recommend,” rather than “grant,” expungement. See supra note 9.

<sup>132</sup> See proposed Rules 12805(c)(9) and 13805(c)(9).

E. Notifications to Customers and States Regarding Expungement Requests

1. Associated Person Serves Customer with Statement of Claim

The Guidance suggests that when a straight-in request is filed against a firm, arbitrators order the associated person to provide a copy of the statement of claim to the customers involved in the customer arbitration that gave rise to the customer dispute information. This helps ensure that the customers know about the expungement request and have an opportunity to participate in the expungement hearing or provide a position in writing on the associated person's request. The proposed rule change would codify this practice in the Industry Code by requiring that the associated person provide all customers whose customer arbitrations, civil litigations and customer complaints gave rise to the customer dispute information that is a subject of the expungement request with notice of the expungement request by serving a copy of the statement of claim requesting expungement.<sup>133</sup> The panel would be authorized to decide whether extraordinary circumstances exist that make service on the customers impracticable.<sup>134</sup>

Given the associated person's personal interest in obtaining expungement, FINRA believes that the panel should review all documents that the associated person used to inform the customers about the expungement request as well as any customer responses

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<sup>133</sup> See proposed Rule 13805(b)(1)(A). The associated person would be required to notify the customer before the first scheduled hearing session is held so that the customer would be aware of the expungement request in advance and could plan to participate once he or she is notified of the time and place of the hearing. See FINRA Rule 13100(p) (providing that a hearing session could be a hearing or prehearing conference).

<sup>134</sup> See proposed Rule 13805(b)(1)(A).

received. Accordingly, the proposed amendments would require the associated person to file with the panel all documents provided by the associated person to the customers, including proof of service, and any responses received by the associated person from a customer.<sup>135</sup> The proposed requirement would help ensure that the associated person does not attempt to dissuade a customer from participating in the expungement hearing.

## 2. Notification to Customers of Expungement Hearing

To help ensure that the customer is notified about the expungement hearing, the proposed rule change would provide that the Director shall notify all customers whose customer arbitrations, civil litigations and customer complaints gave rise to the customer dispute information that is a subject of the expungement request, of the time, date and place of the expungement hearing using the customer's current address provided by the party seeking expungement.<sup>136</sup> The associated person would be required to provide a current address for the customer, or the expungement request would be considered deficient and would not be served.

## 3. State Notification of Expungement Requests

The proposed rule change would require FINRA to notify state securities regulators, in the manner determined by FINRA, of an expungement request within 30 days after receiving a complete request for expungement.<sup>137</sup> The proposed amendments

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<sup>135</sup> See proposed Rule 13805(b)(1)(C).

<sup>136</sup> See proposed Rule 13805(b)(2). This requirement would apply to straight-in requests filed under the Industry Code; notice to customers would not be necessary for requests filed under proposed Rule 12805 of the Customer Code as the customer would be a named party.

<sup>137</sup> See proposed Rules 12805(b) and 13805(b)(3).

would help ensure that state securities regulators are timely notified of the expungement requests.<sup>138</sup>

F. Expungement Requests During Simplified Customer Arbitrations

Customer arbitrations involving \$50,000 or less, called simplified arbitrations, are governed by FINRA Rule 12800. FINRA Rule 12800 provides customers with expedited procedures to make the FINRA forum economically feasible for these smaller claims. Simplified arbitrations are decided on the pleadings and other materials submitted by the parties, unless the customer requests a hearing.<sup>139</sup> Further, a single arbitrator from the chairperson roster is appointed to consider and decide simplified arbitrations, unless the parties agree in writing otherwise.<sup>140</sup>

The customer who files a simplified arbitration determines how the claim will be decided. In particular, the customer has the option of having the case decided in one of three ways: (1) without a hearing (referred to as “on the papers”), where the arbitrator decides the case on the pleadings or other materials; (2) in an “Option One” full hearing, in which prehearings and hearings on the merits take place pursuant to the regular provisions of the Code; or (3) in an “Option Two” special proceeding, whereby the

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<sup>138</sup> FINRA would make this notification in connection with expungement requests under the Customer and Industry Codes. Such notification could be achieved by notifying NASAA of the expungement requests.

<sup>139</sup> See FINRA Rule 12800(a).

<sup>140</sup> See FINRA Rule 12800(b). The parties could agree to have a three-person panel decide the simplified case. For ease of reference, when discussing expungement requests in simplified arbitrations under the proposed rule change, the rule filing uses the term “arbitrator,” unless otherwise specified, to mean either a panel or single arbitrator.

parties present their case in a hearing to the arbitrator in a compressed timeframe, so that the hearings last no longer than one day.<sup>141</sup>

Currently, named associated persons and parties requesting expungement on-behalf-of unnamed persons request expungement during simplified arbitrations. FINRA Rule 12800 does not, however, expressly address how an expungement request should be filed or considered during a simplified arbitration. The proposed amendments would codify an associated person's ability to request expungement when named as a respondent in a simplified arbitration, and for other parties to request expungement on-behalf-of an unnamed person. The proposed rule change would also establish procedures for requesting and considering expungement requests in simplified arbitrations that are consistent with the expedited nature of these proceedings.<sup>142</sup>

#### 1. Requesting Expungement

The proposed rule change would permit a named associated person to request expungement, or a party to file an on-behalf-of request, during a simplified arbitration. Unlike in a non-simplified arbitration, if expungement is not requested during the simplified arbitration, the associated person would be permitted to request it as a straight-in request filed under the Industry Code.<sup>143</sup>

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<sup>141</sup> See FINRA Rule 12800(c).

<sup>142</sup> Under the proposed rule change, an associated person would not be permitted to request expungement in a simplified arbitration administered under the Industry Code, FINRA Rule 13800. All expungement requests under the Industry Code must be filed in accordance with proposed Rule 13805.

<sup>143</sup> See infra Item 3.(a)II.F.1.c., "When No Expungement Request is Made in a Simplified Arbitration."

a. By a Named Associated Person During the Simplified Arbitration

Under the proposed rule change, an associated person named as a respondent in a simplified arbitration could request expungement during the arbitration of the customer dispute information arising from the customer's statement of claim, provided the request is eligible for arbitration.<sup>144</sup>

If a named associated person requests expungement during a simplified arbitration, the proposed rule change would require the request to be filed in an answer or pleading requesting expungement and include the same information required as a request filed in a non-simplified arbitration.<sup>145</sup> Because of the expedited nature of simplified arbitrations, if the named associated person requests expungement in a pleading other than answer, the request must be filed within 30 days after the date that FINRA notifies the associated person of arbitrator appointment,<sup>146</sup> which is the last deadline provided to

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<sup>144</sup> See proposed Rule 12800(d)(1)(A). The limitations that apply to expungement requests filed by a named associated person under proposed Rule 12805(a)(1)(B) would apply to these requests. See supra Item 3.(a)II.C., "Limitations on Expungement Requests."

<sup>145</sup> See proposed Rules 12800(d)(1)(B)(i) and 12805(a)(1)(C)(ii). Thus, the associated person's expungement request would be required to contain the applicable filing fee; the CRD number of the party requesting expungement; each CRD occurrence number that is the subject of the request; the case name and docket number that gave rise to the disclosure, if applicable; and an explanation of whether expungement of the same customer dispute information was previously requested and, if so, how it was decided.

<sup>146</sup> FINRA would notify state securities regulators, in the manner determined by FINRA, of an expungement request within 30 days after receiving a complete expungement request. See proposed Rule 12800(f)(1).

the parties in a simplified arbitration to submit any additional documents before the case is submitted to the arbitrator.<sup>147</sup>

To limit arbitrator shopping, the arbitrator would be required to decide an expungement request once it is filed by the associated person.<sup>148</sup> If an associated person withdraws or does not pursue the request after filing, the arbitrator would be required to deny the request with prejudice so that it could not be re-filed.<sup>149</sup>

b. By a Party On-Behalf-Of an Unnamed Person

Under the proposed amendments, the requirements for a party to file an on-behalf-of request during a simplified arbitration would be the same as the requirements for a named associated person filing an expungement request during a simplified arbitration, with one distinction. A named party would only be able to file an on-behalf-of request during a simplified arbitration with the consent of the unnamed person. As with on-behalf-of requests filed in customer arbitrations under proposed Rule 12805(a)(2), the unnamed person who would benefit from the expungement request must consent to such filing by signing the Form.<sup>150</sup>

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<sup>147</sup> FINRA notifies the parties when an arbitrator has been appointed. FINRA informs the parties that they have 30 days from the date of notification to submit additional documents or other information before the case is submitted to the arbitrator.

<sup>148</sup> See proposed Rule 12800(e)(1).

<sup>149</sup> See proposed Rule 12800(d)(1)(C).

<sup>150</sup> See proposed Rule 12800(d)(2). The request must also meet the same requirements as an on-behalf-of request filed under proposed Rule 12805(a)(2). See proposed Rules 12805(a)(1)(C)(ii), 12805(a)(2)(C)(ii) and 12805(a)(2)(D); see also supra Items 3.(a)II.A.1.b., “Expungement Requests By a Party Named in the Customer Arbitration On-Behalf-Of an Unnamed Person.”

c. When No Expungement Request is Made in a Simplified Arbitration

If expungement is not requested during the simplified arbitration under proposed Rule 12800(d), the associated person would be able to file a straight-in request under proposed Rule 13805 and have the request decided by a three-person panel randomly selected from the Special Arbitrator Roster.<sup>151</sup> The request would be subject to the limitations on whether and when such requests may be filed under the Industry Code.<sup>152</sup>

Due to the expedited nature of simplified proceedings, FINRA believes that the associated person should be able to seek expungement separately under the Industry Code and have his or her expungement request decided by a panel randomly selected from the Special Arbitrator Roster. In simplified arbitrations, there may be less discovery, and the customer may dictate the extent of the evidence presented to the arbitrator. The customer may, for example, determine to have the arbitration decided on the papers. Because there may be less information available for the arbitrator to evaluate an expungement request during a simplified arbitration—even when the simplified arbitration results in an award—the associated person would retain the ability to choose to file the request as a straight-in request under the Industry Code.

2. Deciding Expungement Requests during Simplified Arbitrations

If a named associated person or party on-behalf-of an unnamed person requests expungement during a simplified arbitration, the arbitrator would be required to decide

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<sup>151</sup> See proposed Rules 12800(e)(2), 13805 and 13806.

<sup>152</sup> See proposed Rule 13805(a)(2); see also supra Item 3.(a)II.C., “Limitations on Expungement Requests.”

the expungement request, regardless of how the simplified arbitration case closes (e.g., even if the case settles).<sup>153</sup>

Under the proposed rule change, how and when the expungement request is decided would depend on which option the customer selects to decide the simplified arbitration.

a. No Hearing or Option Two Special Proceeding

If the customer opts not to have a hearing or chooses an Option Two special proceeding, the arbitrator would decide the customer's dispute first and issue an award.<sup>154</sup> After the customer's dispute is decided, the arbitrator must hold a separate expungement-only hearing to consider and decide the expungement request and issue a separate award.<sup>155</sup>

The arbitrator would decide the customer's dispute first and issue an award to minimize any delays in resolving the customer arbitration and any delays in potential recovery that a customer may be awarded. Further, because the customer arbitration may not be as fully developed when an "on the papers" or special proceeding is requested, the arbitrator must hold a separate expungement-only hearing to ensure that he or she has access to sufficient evidence to make a fully-informed decision on the expungement request. The Director would notify all customers whose simplified customer arbitrations

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<sup>153</sup> See proposed Rule 12800(e)(1).

<sup>154</sup> See proposed FINRA Rule 12800(e)(1)(A).

<sup>155</sup> See supra note 154. The arbitrator must conduct the expungement hearing pursuant to proposed Rule 12805(c). The expungement award must meet the requirements of proposed Rule 12805(c)(8), and forum fees would be assessed pursuant to proposed Rule 12805(c)(9).

and customer complaints gave rise to the customer dispute information that is a subject of the expungement request, of the time, date and place of the expungement hearing.<sup>156</sup>

b. Option One Hearing

If the customer chooses to have a full “Option One” hearing on his or her claim and it closes by award, the arbitrator would be required to consider and decide the expungement request during the customer arbitration and include the decision in the award.<sup>157</sup> This process would be the same as deciding an expungement request during a non-simplified customer arbitration that closes by award after a hearing, where the customer’s claim and expungement request are addressed during the customer arbitration. As there would be a more complete factual record from the full hearing on the merits of the customer case, the arbitrator could decide the customer dispute and the expungement request after the hearing concludes.

If the customer arbitration closes other than by award or by award without a hearing, the arbitrator would be required to hold a separate expungement-only hearing to consider and decide the expungement request and issue the decision in an award.<sup>158</sup> The arbitrator would need to conduct a separate expungement hearing to develop a complete factual record in order to make a fully-informed decision on the expungement request.<sup>159</sup>

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<sup>156</sup> See proposed Rule 12800(f)(2). The Director would also notify these customers of the expungement hearing, if the associated person opts to file the request under the Industry Code after the simplified case closes.

<sup>157</sup> See proposed Rule 12800(e)(1)(B)(i).

<sup>158</sup> See proposed Rule 12800(e)(1)(B)(ii).

<sup>159</sup> See supra note 155.

Given the generally less complex nature of simplified arbitrations, FINRA does not believe that it is necessary for a panel from the Special Arbitrator Roster to decide an expungement request if a simplified customer arbitration closes other than by award or by award without a hearing. However, if the Commission approves the proposed rule change, FINRA will continue to monitor expungement requests and decisions in simplified arbitrations to determine if such requests should be decided by the Special Arbitrator Roster, particularly if the customer chooses to have his or her case decided on the papers or in a special proceeding.

G. Non-substantive changes

FINRA is also proposing to amend the Codes to make non-substantive, technical changes to the rules impacted by the proposed rule change. For example, the proposed rule change would require the renumbering of paragraphs and the updating of cross-references in the rules impacted by the proposed rule change. In addition, the title of Part VIII of the Customer Code would be amended to add a reference to “Expungement” proceedings. Similarly, the title of Part VIII of the Industry Code would be amended to add a reference to “Expungement Proceedings” and “Promissory Note Proceedings.” FINRA believes the proposed changes to the titles would more accurately reflect the contents of Part VIII of the Customer and Industry Codes. FINRA is also proposing to re-number current FINRA Rule 13806 (Promissory Note Proceedings) as new FINRA Rule 13807, without substantive change to the current rule language.

As noted in Item 2 of this filing, if the Commission approves the proposed rule change, FINRA will announce the effective date of the proposed rule change in a Regulatory Notice to be published no later than 60 days following Commission approval.

The effective date will be no later than 120 days following publication of the Regulatory Notice announcing Commission approval of the proposed rule change.

(b) Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>160</sup> which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest.

The proposed rule change seeks to balance the important investor protection objectives of maintaining the integrity and accuracy of the information in the CRD system and BrokerCheck with the interest of brokers and firms in the fairness and accuracy of the disclosures contained in the systems.

The proposed rule change will enhance the current expungement framework and improve the efficiency of the FINRA arbitration forum by codifying the Guidance as rules that arbitrators and parties must follow. In addition, when an associated person files a claim against a firm for the sole purpose of requesting expungement, these cases can be complex to resolve, particularly if the customer or customer's representative does not participate in the hearing. Having three arbitrators available to ask questions, request evidence and generally to serve as fact-finders in the absence of customer input will help ensure that a complete factual record is created to support the arbitrators' decision in such expungement hearings. In addition, the proposed rule change will help ensure that

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<sup>160</sup> 15 U.S.C. 78o-3(b)(6).

arbitrators who will decide these requests meet heightened qualifications and have completed enhanced expungement training. FINRA believes that by requiring a three-person panel from the Special Arbitrator Roster to decide expungement requests filed under the Industry Code, the proposed rule change will help ensure expungement is recommended in limited circumstances.

The proposed rule change will foreclose a practice that has emerged in the existing expungement process where parties seek expungement after a prior denial by a court or panel of a request to expunge the same customer dispute information, or where parties withdraw or do not pursue an expungement request and then make another request for expungement of the same customer dispute information. The proposed rule change imposes procedures and requirements around when and how a party may request expungement, and expressly provides that omission of certain of the requirements will make the expungement request deficient. Further, the proposed rule change provides the Director with express authority to deny the forum if an expungement request is ineligible for arbitration under the proposed rules. Thus, FINRA believes the proposed rule change will add more transparency to the expungement process.

Moreover, the proposed rule change seeks to protect investors and the public interest by notifying customers of expungement requests filed under the Industry Code. Although a straight-in request will be filed against a firm, customers whose disputes are a subject of the request will be notified and encouraged to participate in the expungement hearing. Such notifications will make clear to arbitrators and parties the rights of customers who choose to participate in these hearings. The customers' input will provide the panel with additional insight on the customer dispute and help create a complete

factual record, which will result in more informed decisions on expungement requests. FINRA believes this enhancement, which will encourage and facilitate customer participation in expungement hearings, will help to maintain the integrity of the information in the CRD system.

Further, the process of requesting expungement during a simplified arbitration will be codified to help ensure that customers are aware of their rights under the process and how an expungement request will affect (and not affect) their arbitration claims. By expressly incorporating the practice of requesting expungement during simplified proceedings, the proposed amendments add consistency to the rules and provide more guidance to the arbitrators and the parties requesting expungement.

The proposed rule change will also help ensure that state securities regulators have knowledge of expungement requests by requiring notification to the states, in the manner determined by FINRA, after FINRA receives a complete expungement request.

For these reasons, the proposed rule change represents a significant step towards addressing concerns with the current expungement framework. FINRA believes the proposed rule change will improve the expungement framework by incorporating the Guidance, establishing a Special Arbitrator Roster and addressing gaps that have emerged in the existing expungement framework. In addition, FINRA believes these changes will help to maintain the accuracy and integrity of the information in the CRD system and BrokerCheck, while also protecting brokers from the publication of false allegations against them.

**4. Self-Regulatory Organization's Statement on Burden on Competition**

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

**Economic Impact Assessment**

FINRA has undertaken an economic impact assessment to analyze the regulatory need for the proposed rule change, its potential economic impacts, including anticipated costs, benefits and distributional and competitive effects, relative to the current baseline, and the alternatives FINRA considered in assessing how best to meet FINRA's regulatory objectives.

**A. Regulatory Need**

The proposed rule change would address concerns relating to the expungement process that are not consistent with the regulatory intent to permit expungement in limited circumstances. The concerns include the potential impact of the absence of customers and their representatives from an expungement hearing which may result in the arbitrator or panel receiving information only from the associated person. The concerns also include associated persons having their straight-in requests heard by a single arbitrator instead of a three-person panel, and the selection of arbitrators to hear these requests. Lastly, the concerns include requests to expunge the same customer dispute information in multiple proceedings. The proposed rule change would also codify and expand upon the provisions of the Guidance to help ensure that arbitrators and parties are adhering to these procedures for all expungement requests, and to encourage and facilitate customer participation in expungement hearings.

B. Economic Baseline

The economic baseline for the proposed rule change includes the current provisions under the Codes that address the process for parties to seek expungement relief. In addition, because arbitrators are generally believed to be adhering to the best practices and recommendations that are a part of the Guidance, the economic baseline also includes the Guidance.<sup>161</sup> The proposed rule change is expected to affect associated persons and other parties to expungement requests including member firms, customers and arbitrators. The proposed rule change may also affect users of customer dispute information contained in the CRD system and displayed through BrokerCheck.<sup>162</sup>

The customer dispute information contained in the CRD system is submitted by registered securities firms and regulatory authorities in response to questions on the uniform registration forms.<sup>163</sup> The information can be valuable to current and prospective customers to learn about the conduct of associated persons.<sup>164</sup> Current and

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<sup>161</sup> See supra note 2.

<sup>162</sup> Users of customer dispute information include investors; member firms and other companies in the financial services industry; individuals registered as brokers or seeking employment in the brokerage industry; and FINRA, states and other regulators.

<sup>163</sup> See supra note 4 and accompanying text for additional discussion of the uniform registration forms and the information contained in the CRD system. Some of the information may involve pending actions or allegations that have not been resolved or proven.

<sup>164</sup> Recent academic studies provide evidence that the past disciplinary and other regulatory events associated with a firm or individual can be predictive of similar future events. See Hammad Qureshi & Jonathan Sokobin, Do Investors Have Valuable Information About Brokers? FINRA Office of the Chief Economist Working Paper, Aug. 2015; see also Mark Egan, Gregor Matvos, & Amit Seru,

prospective customers may not select or remain with an associated person or a member firm that employs an associated person with a record of customer disputes. Similarly, member firms and other companies in the financial services industry may use the information when making employment decisions.<sup>165</sup> In this manner, the customer dispute information contained in the CRD system (and displayed through BrokerCheck) may positively or negatively affect the business and professional opportunities of associated persons. Where the information is reliable, it also provides for customer protections and information useful for member firms.

Any negative impact on the business and professional opportunities of associated persons may be appropriate and consistent with investor protection, such as when the customer dispute information has merit. Any such negative impact may be inappropriate, however, if, for example, the customer dispute information is factually impossible, clearly erroneous, or false. Regardless of the merit, associated persons have an incentive to remove customer dispute information from the CRD system and its public display through BrokerCheck.

An associated person, or a party on-behalf-of an unnamed person, typically begins the process to remove customer dispute information from the CRD system by filing an expungement request in FINRA arbitration. FINRA is able to identify 6,928 requests to

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The Market for Financial Adviser Misconduct, *Journal of Political Economy* 127, no. 1 (February 2019): 233-295.

<sup>165</sup> Customer dispute information submitted to the CRD system and displayed through BrokerCheck may have other uses. For example, investors may use the information when deciding with whom to do business. FINRA, states and other regulators also use the information to regulate brokers.

expunge customer dispute information in FINRA arbitration from January 2016 through December 2019 (the “sample period”). More than one expungement request can be made in a single arbitration, and multiple expungement requests may relate to the same arbitration, civil litigation or complaint if the dispute relates to more than one associated person.

Among the 6,928 expungement requests, 3,203 requests (46 percent) were made during a customer arbitration, and 3,725 requests (54 percent) were filed as a straight-in request.<sup>166</sup> The 3,203 expungement requests made during a customer arbitration include 2,936 requests made during a non-simplified customer arbitration and 267 requests made during a simplified customer arbitration. The 3,725 requests to expunge customer dispute information disclosures filed as a straight-in request include 3,657 requests in arbitrations filed solely against a member firm or against a member firm and a customer, and 68 requests in arbitrations filed solely against a customer. In the 3,203 expungement requests made during a customer arbitration, the associated person was a named party in 1,504 of the requests (47 percent), and an unnamed party in 1,699 of the requests (53 percent).

Among the expungement requests during the sample period, FINRA is able to identify 82 requests to expunge the same customer dispute information in a subsequent arbitration.<sup>167</sup> For purposes of this analysis, FINRA limited the identification of

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<sup>166</sup> Sixteen requests to expunge customer dispute information were made during industry arbitrations that were not straight-in requests. To simplify the analysis, we exclude these 16 requests from the sample.

<sup>167</sup> Eighty of the 82 subsequent expungement requests relate to previous requests in another arbitration that were withdrawn or otherwise not pursued by the

additional expungement requests to those requests where both the initial request and the subsequent request were made during the sample period. Additional subsequent expungement requests may have been filed during the sample period if the initial expungement request was made prior to the sample period (i.e., before January 2016). The 82 requests to expunge the same customer dispute information in a subsequent arbitration can, therefore, be considered a lower bound for the number of these requests during the sample period. The proposed rule change would foreclose associated persons from filing additional requests.

As of December 2019, 5,159 of the 6,928 expungement requests were made in an arbitration that closed. Among the 5,159 expungement requests, 2,255 requests (44 percent) were made during a customer arbitration and 2,904 requests (56 percent) were filed as a straight-in request. The 2,255 expungement requests made during a customer arbitration include 2,015 requests made during a non-simplified customer arbitration and 240 requests made during a simplified customer arbitration. The 2,904 requests filed as a straight-in request include 2,838 requests in arbitrations filed solely against a member firm or a member firm and a customer, and 66 requests in arbitrations filed solely against

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associated person or party that filed the request. For the two remaining subsequent expungement requests, one relates to a previous request on behalf of an unnamed person that was denied, and the other to a previous request that was determined by the panel to be ineligible for arbitration. An arbitrator or panel recommended expungement in 60 of the 82 subsequent expungement requests and denied eight. One of the granted requests relates to the previous request that was denied. Another of the granted requests relates to the previous request that was deficient and therefore not decided. Seven subsequent expungement requests were withdrawn or deficient and, therefore, not decided. In addition, seven subsequent expungement requests were still pending as of the end of the sample period. In 42 of the 82 subsequent expungement requests, the associated person was an unnamed party in the first arbitration.

a customer. Under the proposed rule change, an associated person would be prohibited from filing a straight-in request against a customer.

An arbitrator or panel made a decision in arbitrations relating to 3,722 of the 5,159 requests in arbitrations that closed, and made no decision in arbitrations relating to the remaining 1,437 requests. A single arbitrator made a decision in arbitrations relating to 2,692 of the 3,722 requests, and a two- or three-person panel made a decision in arbitrations relating to the remaining 1,030 requests. For the customer arbitrations, the decision by an arbitrator or panel may relate to the arbitration, an expungement request, or both. For the straight-in requests, the decision would relate to the expungement request only. In arbitrations where no decision on the merits of the customer case or an expungement request was made, the requests were either not eligible (as determined by the arbitrator or panel), withdrawn, or otherwise not pursued by the associated person or party that filed the request.

As detailed in the next paragraph, the percentage of expungement requests that are recommended is higher when the arbitrator or panel receives information only from the associated person or other party requesting expungement. The arbitrator or panel is likely to receive information only from the party requesting expungement when (1) the customer arbitration does not close by award after a hearing (e.g., settles), or (2) an associated person files a straight-in request against a member firm. In both circumstances, the customer and his or her representative have little incentive to participate in an expungement hearing.

Among the 3,722 expungement requests in arbitrations where an arbitrator or panel made a decision, 2,874 resulted in an arbitrator or panel recommending

expungement (77 percent). Among the 3,722 expungement requests, 976 requests were made during a non-simplified or simplified customer arbitration, and 2,746 requests were filed as a straight-in request. An arbitrator or panel recommended expungement in response to 595 of the 976 requests (61 percent) made during a customer arbitration. This includes 168 of the 369 requests (46 percent) made during a customer arbitration that closed by award after a hearing, and 427 of the 607 expungement requests (70 percent) made during a customer arbitration that closed by award without a hearing or other than by award. An arbitrator or panel recommended expungement in 2,279 of the 2,746 requests filed as a straight-in request (83 percent).<sup>168</sup>

A recommendation for expungement in FINRA arbitration is not the final step in the expungement process. If the arbitrator or panel recommends expungement, then the firm or associated person must confirm the arbitration award in a court of competent jurisdiction and serve the confirmed award on FINRA.<sup>169</sup> As of July 2020, FINRA had removed 2,641 customer dispute information disclosures from the CRD system from the possible 2,874 requests (92 percent) in which an arbitrator or panel recommended expungement. Firms or associated persons may have not yet sought or obtained a court order for the remaining disputes.

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<sup>168</sup> Among the 976 expungement requests during a non-simplified or simplified customer arbitration, a single arbitrator made a decision in arbitrations relating to 306 requests, and a two- or three-person panel made a decision in arbitrations relating to 670 requests. In addition, among the 2,746 straight-in requests, a single arbitrator made a decision in arbitrations relating to 2,386 requests and a two- or three-person panel made a decision in arbitrations relating to 360 requests. See infra note 189 for a discussion of the percentage of expungement requests recommended between two- or three-person panels and one-person panels.

<sup>169</sup> See supra note 9.

Approximately one-third of the 2,641 customer dispute information disclosures (965, or 37 percent) that were expunged were submitted to the CRD system from 2014 to 2019. The 965 customer dispute information disclosures reflect three percent of the total number of customer dispute information disclosures submitted to the CRD system during this period of time (approximately 37,000). The remaining 1,676 customer dispute information disclosures were submitted to the CRD system prior to 2014. The number of customer dispute information disclosures expunged during the sample period that were submitted to the CRD system prior to 2014 suggests that associated persons may yet still expunge customer dispute information disclosures submitted to the CRD system during or prior to the sample period. The three percent of expunged customer dispute information disclosures should therefore be considered a lower bound for the rate at which customer dispute information disclosures are expunged.

A firm or associated person can also initiate a proceeding directly in a court of competent jurisdiction without first going through any arbitration proceeding. From January 2016 through December 2019, the expungement of 138 customer dispute information disclosures were sought directly in court. As of July 2020, court proceedings had concluded for 118 of those disclosures and proceedings remained ongoing for 20 disclosures. Among the 118 disclosures for which the court proceeding had concluded, 86 disclosures were ordered expunged by a court and 32 disclosures were not ordered to be expunged. FINRA will challenge these requests in court in appropriate circumstances.

C. Economic Impact

1. Overview

The proposed rule change would codify the best practices described in the Guidance.<sup>170</sup> The best practices include the prohibition on the filing of an expungement request if (1) an arbitration panel or court of competent jurisdiction previously denied a request to expunge the same customer dispute information, or (2) the customer dispute information arises from a customer's arbitration that has not concluded. Based on FINRA staff observations, arbitrators are generally believed to be adhering to these best practices and, therefore, codifying them should not result in new material economic impacts. Codifying the best practices in the Guidance should, however, clarify among parties how the practices should be applied, including what is permitted during the expungement hearing and the responsibilities of the parties and the arbitrator or panel when expungement is requested. Codifying the Guidance may also help inform customers more generally of the practices that the forum has implemented to encourage and facilitate customer participation in expungement hearings. In addition, parties may incur fewer costs from the codification of the practices, including the costs from actions or decisions (e.g., requesting expungement of customer dispute information that was previously denied in another arbitration or court) that would be denied by an arbitration panel pursuant to the Guidance.

The proposed rule change would also introduce other changes to the Codes that expand upon or that are not a part of the Guidance. In particular, the proposed rule

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<sup>170</sup> See supra note 2.

change would restrict when an associated person is permitted to request expungement in FINRA arbitration. The proposed rule change would also require an arbitrator or panel from a customer arbitration that closes by award after a hearing, from a simplified customer arbitration, or a panel from the Special Arbitrator Roster to decide an expungement request. Finally, the proposed rule change would address the participation by associated persons and customers in expungement hearings. These changes may result in new material economic benefits and costs. These economic effects are discussed in further detail below.

## 2. Expungement Requests during Customer Arbitrations

The proposed rule change would set forth requirements for expungement requests during customer arbitrations. The proposed rule change would establish different requirements for non-simplified customer arbitrations and simplified customer arbitrations, and for an associated person named or unnamed to a (non-simplified or simplified) customer arbitration.

### a. Expungement Requests by Named Associated Persons during Non-Simplified Customer Arbitrations

The proposed rule change would require an associated person named in a non-simplified customer arbitration to request expungement during the customer arbitration regarding the conduct that gave rise to the arbitration. Otherwise, the associated person would forfeit the opportunity to seek expungement of the same customer dispute information in any subsequent proceeding. The arbitrator or panel from a non-simplified

customer arbitration would decide an expungement request if the arbitration closes by award after a hearing.<sup>171</sup>

The proposed rule change would help ensure that, if possible, the arbitrator or panel from a non-simplified customer arbitration, with input from all parties and access to all evidence, testimony and other documents, would decide an expungement request. These arbitrators or panels would be best situated to decide the related issue of expungement, and thereby help ensure that expungement recommendations and the customer dispute information contained in the CRD system and displayed through BrokerCheck reflect the conduct of associated persons.

An associated person named in a non-simplified customer arbitration may lose the ability to request expungement of the customer dispute information arising from the arbitration. A named associated person who does not request expungement during a non-simplified customer arbitration (or within the required time) would lose the ability to seek expungement relief.<sup>172</sup> Because the named associated person may lose the ability to assess information that arises as a part of arbitration before they are required to request expungement, associated persons may incur costs to preserve their right to request expungement by filing a request with or without the expectation that the arbitrator or panel would recommend expungement. FINRA believes, however, that the proposed rule

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<sup>171</sup> See supra Item 3.(a)II.A.1.a., “Expungement Requests During the Customer Arbitration, By a Respondent Named in a Customer Arbitration.”

<sup>172</sup> Under the proposed rule change, a party that does not file or serve an expungement request at least 30 days before the first scheduled hearing begins could file a motion seeking an extension. The motion, however, may be opposed by another party and denied.

change would mitigate these potential costs by providing associated persons a reasonable amount of time (i.e., within 45 days of receipt of the customer's statement of claim if the request is included in an answer, or 30 days before the first scheduled hearing begins if the request is included in a pleading) during the arbitration to consider whether to file a request. Parties may also incur other, indirect costs if, for example, the deadline to request expungement during a non-simplified customer arbitration causes them to incur costs to expedite the filing of the expungement request or constrains their ability to engage in other activities (i.e., incur opportunity costs).

b. Expungement Requests during a Non-Simplified Customer Arbitration that Close other than by Award or by Award without a Hearing

Associated persons who request expungement during a non-simplified customer arbitration (either as a named party or as an unnamed party that consents to an on-behalf-of request) that closes other than by award or by award without a hearing (and would have otherwise had their expungement request decided as part of the customer arbitration) would incur additional costs to file a straight-in request.<sup>173</sup> Associated persons may incur delays in receiving a decision on the request, and may incur additional legal fees and forum fees to resolve the straight-in request. The member firms with which the associated persons were associated at the time the customer dispute arose

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<sup>173</sup> Associated persons who would otherwise request expungement as a counterclaim during an industry arbitration, which is rare, or who would otherwise intervene in a customer arbitration and have an expungement request decided during the arbitration, would instead be required to file a straight-in request under proposed Rule 13805. These associated persons and member firms with which the associated persons were associated would incur similar costs.

would also incur additional legal and forum fees. These costs would be imposed by the proposed rule change if the expungement requests would have otherwise been decided as part of the non-simplified customer arbitration. These costs would not be imposed by the proposed rule change, however, if regardless of the proposed rule change associated persons would have filed a straight-in request after the close of the non-simplified customer arbitration.

The additional costs for an associated person to resolve a straight-in request after the close of a non-simplified customer arbitration (that closes other than by award or by award without a hearing) may reduce the likelihood that the parties settle a customer arbitration.<sup>174</sup> In particular, the associated person may factor the cost to resolve a separate straight-in request into the decision regarding whether to settle the arbitration or have the case decided by the arbitrator or panel to the arbitration. In addition, even if the parties continue to settle the dispute, the associated person may subtract the cost to resolve a separate straight-in request from the potential settlement amount.

An associated person (or a party on behalf of an associated person) who files a straight-in request would incur the minimum hearing session fee of \$1,125 for each

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<sup>174</sup> FINRA notes, however, that the determination regarding whether to settle a customer arbitration can depend on a number of factors, including the parties' respective estimates of the additional costs they would incur to continue the customer arbitration, the value that the associated person places on expungement, the associated person's estimate of the likelihood that he or she could obtain expungement in the customer case compared to in a straight-in request and the cost that they estimate the associated person would incur to pursue the straight-in request.

session the panel conducts to decide the expungement request.<sup>175</sup> The member firm at which the broker was associated at the time the customer dispute arose would also be assessed a minimum surcharge fee of \$1,900 and a minimum process fee of \$3,750. The fees associated with non-monetary claims would help ensure that costs to the forum for administering expungement requests are allocated as intended to the party or parties requesting expungement and, as applicable, the member firms at which the broker was associated at the time the customer dispute arose.

c. Expungement Requests by Unnamed Persons in Non-Simplified Customer Arbitrations and by Named and Unnamed Persons in Simplified Customer Arbitrations

The proposed rule change would not require an unnamed person in a non-simplified customer arbitration, an associated person named in a simplified customer arbitration, or an unnamed person in a simplified customer arbitration to request expungement of the customer dispute information during the customer arbitration. Instead, similar to today, these associated persons may wait until after the customer arbitration has concluded to request expungement as a straight-in request.<sup>176</sup>

The option to wait until after the customer arbitration has concluded to request expungement is not a benefit created by the proposed rule change, but is instead currently permitted under the Codes. FINRA believes that an associated person who is not named

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<sup>175</sup> The associated person would not, however, incur an additional filing fee to file the straight-in expungement request. See infra Item 5(H).

<sup>176</sup> This requirement would help ensure that the panel from the Special Arbitrator Roster is aware of the outcome of the arbitration when deciding the request.

in a non-simplified customer arbitration, or an associated person who is either named or not named in a simplified customer arbitration, should be able to seek expungement as a straight-in request and have their request decided by a panel from the Special Arbitrator Roster.

Associated persons who are not required and choose not to request expungement during the customer arbitration may also incur additional costs. Any incremental costs from not filing an expungement request during a customer arbitration, however, are not imposed by the proposed rule change. Instead, they are borne at the discretion of the parties who make the determination of when to request expungement, and are similar to the costs they would incur under the Codes today.

d. Time Limit for Requesting Expungement in Simplified and  
Non-Simplified Customer Arbitrations

A named associated person or a party on-behalf-of an unnamed person would be required to request expungement in a simplified customer arbitration within 30 days of the date that FINRA provides notice of arbitrator appointment.<sup>177</sup> A named associated person or a party requesting expungement on-behalf-of an unnamed person in a non-

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<sup>177</sup> The proposed rule change would require that if the named associated person or party on-behalf-of an unnamed person requests expungement in a pleading other than an answer, the request must be filed within 30 days after the date FINRA provides the associated person with notice of arbitrator appointment, which is the last deadline provided to the parties in a simplified arbitration to submit additional documents before the case is submitted to the arbitrator. See proposed Rules 12800(d)(1)(B)(i) and 12800(d)(2)(B)(i).

simplified customer arbitration would be required to request expungement no later than 30 days before the first scheduled hearing.<sup>178</sup>

Associated persons who do not request expungement within these time limits may incur additional costs that may include costs arising from delays in receiving a decision on the request and legal and forum fees. The member firms with which the brokers were associated at the time the customer dispute arose would also incur additional legal and forum fees. These costs would be imposed by the proposed rule change.

### 3. Time Limits for Filing Straight-in Requests

The proposed rule change would also set forth requirements for an associated person to file a straight-in request. For customer dispute information reported to the CRD system after the effective date of the proposed rule change, the proposed rule change would require an associated person to file a straight-in request within two years of a customer arbitration or civil litigation closing, or, if no customer arbitration or civil litigation, within six years from the initial reporting of the customer complaint to the CRD system.<sup>179</sup>

The proposed rule change would also require a two-year time limit for requests to expunge customer dispute information that arose from a customer arbitration or civil

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<sup>178</sup> See proposed Rules 12805(a)(1)(C)(i) and 12805(a)(2)(C)(iii). The proposed rule change also provides that FINRA would notify state securities regulators, in the manner determined by FINRA, of an expungement request within 30 days of receiving a complete request for expungement. See proposed Rule 12805(b). State securities regulators would, therefore, have additional time to review the request and decide whether to oppose expungement if confirmation of an expungement recommendation is later sought in court.

<sup>179</sup> See proposed Rules 13805(a)(2)(A)(iv) and 13805(a)(2)(A)(v).

litigation that closed on or prior to the effective date of the proposed rule change or a six-year time limit to request expungement of customer dispute information arising from a customer complaint initially reported to the CRD system on or prior to the effective date of the proposed rule change.<sup>180</sup> These time limits would begin from the effective date of the proposed rule change.

Arbitrators on the Special Arbitrator Roster would have the experience, qualifications and training necessary to decide straight-in requests. These time limits may increase customer participation in the proceedings and the likelihood that the panel from the Special Arbitrator Roster receives the relevant evidence and testimony to decide an expungement request. The time limits would help ensure that the expungement hearing is held close in time to the customer arbitration or civil litigation, or the events that led to the customer dispute information disclosure, and foreclose the option of an associated person to choose the timing of a straight-in request to potentially reduce the likelihood of customer participation. Similar to other amendments proposed herein, an increase in customer participation may provide a panel from the Special Arbitrator Roster with additional information to decide an expungement request and help ensure the accuracy of the customer dispute information contained in the CRD system and displayed through BrokerCheck.

These time limits, however, may constrain an associated person from filing a straight-in request.<sup>181</sup> Associated persons who would otherwise delay the filing of a

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<sup>180</sup> See proposed Rules 13805(a)(2)(B)(i) and 13805(a)(2)(B)(ii).

<sup>181</sup> If the Commission approves the proposed rule change, FINRA expects that a number of associated persons would file a straight-in request to expunge customer

straight-in request may incur additional costs to file a straight-in request within the required time limits (e.g., opportunity costs, as described above). These time limits may also constrain an associated person from filing more than one expungement request in the same straight-in request. For example, associated persons may lose the ability to delay the filing of a straight-in request to expunge a complaint from a particular customer until other customers make additional complaints, if the filing of the straight-in request to expunge the complaint of the first customer would be time barred. Instead, an associated person may be required (as a result of the time limits) to file more than one straight-in request.

Associated persons who are restricted from including more than one request to expunge customer dispute information in the same straight-in request would incur additional legal and forum fees for each straight-in request or not seek expungement for all of the disclosures. The member firm at which the associated person was associated at the time the customer disputes arose would incur additional legal and forum fees if the associated person were to file multiple, separate straight-in requests.

#### 4. Time Limits for Straight-in Requests – Quantitative Description

As discussed as part of the Economic Baseline, 3,725 expungement requests were filed as straight-in requests during the sample period. The following estimates demonstrate that the majority of these straight-in requests would not have been permitted under the proposed time limits, and associated persons may not have been able to include more than one expungement request in the same straight-in request. The estimates,

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dispute information reported to the CRD system prior to or soon after the effective date of the proposed rule change to help ensure that they are not constrained from seeking expungement because of the proposed time limitations.

however, do not take into account the potential change in the behavior of associated persons; associated persons would have incentive under the proposed amendments to file the straight-in requests within the time limits or otherwise lose the ability to make or file a request.<sup>182</sup>

Among the 3,725 expungement requests filed as a straight-in request, 1,140 requests followed a (non-simplified or simplified) customer arbitration (of the same underlying dispute). Two-hundred ninety of the 1,140 requests (25 percent) were filed as a straight-in request within the two-year time limit and would have been permitted under the proposed rule change. The remaining 850 requests (75 percent) were filed as a straight-in request after the two-year time limit and would not have been permitted. The median time from the close of the customer arbitration to the filing of the straight-in request was six years.

The 3,725 expungement requests filed as a straight-in request also include 2,585 requests that did not follow a (non-simplified or simplified) customer arbitration (of the same underlying dispute). Among the 2,585 requests, 813 requests (31 percent) were filed as a straight-in request within six years from the initial reporting of the disclosure to the CRD system and would have been permitted under the proposed rule change. The remaining 1,772 requests (69 percent) were filed as a straight-in request after the six-year time limit and would not have been permitted.

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<sup>182</sup> The following estimates also do not take into account the number of straight-in requests of customer dispute information arising from a previous (non-simplified or simplified) customer arbitration which, under the proposed rule change, may have been decided as part of the customer arbitration.

As discussed above, more than one expungement request can be made in a single arbitration, and the time limits may limit the ability of an associated person to include multiple expungement requests in the same straight-in request. The 3,725 expungement requests filed as a straight-in request relate to 1,778 arbitrations. Associated persons included more than one request to expunge customer dispute information in 810 of the 1,778 arbitrations. Under the proposed time limits, associated persons would not have been able to include all expungement requests in at least 225 of the 810 arbitrations.

#### 5. Arbitrators or Panels Deciding Expungement Requests

The proposed rule change would require that the arbitrator or panel from a non-simplified customer arbitration decide expungement requests during the arbitration if the arbitration closes by award after a hearing.<sup>183</sup> In addition, the proposed rule change would require the arbitrator from a simplified customer arbitration to decide expungement requests if there is a full hearing, or in a separate expungement-only hearing after the simplified arbitration closes if the arbitration is decided “on the papers” or in a special proceeding.<sup>184</sup> The proposed rule change would also require a randomly selected panel from the Special Arbitrator Roster to decide straight-in requests.<sup>185</sup>

The proposed rule change is not structured to increase or decrease the likelihood that an arbitrator or panel recommends expungement in any individual hearing except as it relates to the merits of the request. The proposed rule change is structured, however, to

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<sup>183</sup> See proposed Rules 12805(a)(1)(D)(i) and 12805(a)(2)(E)(i).

<sup>184</sup> See proposed Rule 12800(e)(1).

<sup>185</sup> See proposed Rule 13806(b)(1).

place an arbitrator or panel in a better position to determine whether to recommend expungement of customer dispute information, and thereby help ensure the accuracy of the customer dispute information contained in the CRD system and displayed through BrokerCheck. Under the proposed rule change and in general, the arbitrator or panel that decides a request would either hear the full merits of the customer case or have additional training and qualifications when they are likely to receive information only from the party requesting expungement. In addition, panels from the Special Arbitrator Roster would be able to request evidence from the member firm at which the associated person was associated at the time the customer dispute arose

The proposed rule change is also structured to reduce the potential influence of associated persons and member firms on the selection of the arbitrator or panel that decides an expungement request. First, a panel from the Special Arbitrator Roster would be randomly selected to decide a straight-in request, thereby decreasing the extent to which an associated person and member firm with which the associated person was associated at the time the customer dispute arose may together select arbitrators who are more likely to recommend expungement.<sup>186</sup>

Second, the proposed rule change would foreclose the option for an associated person to withdraw a request and seek expungement of the same customer dispute information in a subsequent arbitration.<sup>187</sup> Associated persons may exercise this option if

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<sup>186</sup> See supra Item 3.(a)II.B.2.b., “Straight-in Requests and the Special Arbitrator Roster, Composition of the Panel.”

<sup>187</sup> This includes the requirement for an unnamed person to provide written consent to an on-behalf-of request for it to proceed, thereby preventing an unnamed person from subsequently arguing that they were unaware of an expungement

they believe that they have a higher probability of obtaining an expungement recommendation with a different arbitrator or panel in another arbitration, and in particular if the associated person files a straight-in request against the member firm with which the broker was associated at the time the customer dispute arose. To the extent that the associated person and his or her employer's interests are aligned and both seek to increase the likelihood that expungement is recommended, they would together be expected to select arbitrators who may be more likely to recommend expungement.<sup>188</sup> Though these proposed amendments are consistent with the regulatory intent to permit expungement in limited circumstances, it may decrease the likelihood that associated persons are able to obtain an award recommending expungement.

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request on their behalf. See proposed Rule 12805(a)(2)(A). This also includes the requirement that a case be closed with prejudice if an associated person withdraws a straight-in request after a panel from the Special Arbitrator Roster is appointed (unless the panel decides otherwise). See proposed Rule 13805(a)(4). In the sample period, an associated person withdrew 155 of the 2,904 straight-in requests (five percent) filed in cases that closed. The 155 straight-in requests include 118 requests where an arbitrator or panel was appointed.

<sup>188</sup> A recent academic study finds evidence that suggests parties can use previous expungement decisions to predict the potential likelihood that an arbitrator would recommend expungement. See Colleen Honigsberg & Matthew Jacob, "Deleting Misconduct: The Expungement of BrokerCheck Records," November 2018, <https://www-cdn.law.stanford.edu/wp-content/uploads/2018/11/SSRN-id3284738.pdf>. The study also finds evidence that suggests both successful and unsuccessful expungement attempts predict future broker misconduct. An unsuccessful expungement attempt is associated with an approximately four times higher probability of future misconduct. Although expungement decisions are based on the information available at the time of the request, including the facts and circumstances of the arbitration, this finding suggests that the decisions being made by arbitrators are related to the potential future harm posed by the requesting broker.

In general, under the proposed rule change, a three-person panel would consider and decide expungement requests during non-simplified customer arbitrations that close by award after a hearing and straight-in requests. Expungement decisions by a three-person panel may differ from expungement decisions by a single arbitrator. In addition, the decisions may differ depending on the arbitrators selected and the interaction among the arbitrators when deciding an expungement request. The extent to which a three-person panel would decide an expungement request differently than a single arbitrator, however, is not known.<sup>189</sup> As discussed above, expungement requests may be complex to resolve, particularly straight-in requests where customers typically do not participate in the expungement hearing. Thus, having three arbitrators available to ask questions, request evidence and to serve generally as fact-finders in the absence of customer input would help ensure that a complete factual record is created to support the arbitrators' decision in such expungement hearings.

#### 6. Arbitrators or Panels Deciding Expungement Requests – Quantitative Description

As discussed as part of the Economic Baseline, 5,159 of the 6,928 expungement requests sought during the sample period were filed in an arbitration that closed. Among

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<sup>189</sup> Among the 2,746 expungement requests filed as a straight-in request where an arbitrator or panel made a decision, a similar percentage of requests was recommended by a two- or three-person panel (306 of 360 requests, or 85 percent) as was recommended by a one-person panel (1,973 of 2,386 requests, or 83 percent). In addition, among the 976 expungement requests during a non-simplified or simplified customer arbitration where an arbitrator or panel made a decision, a similar percentage of requests was recommended by a two- or three-person panel (422 of 670 requests, or 63 percent) as was recommended by a one-person panel (173 of 306 requests, or 57 percent).

the 5,159 expungement requests, 4,521 requests (88 percent) would have required a panel from the Special Arbitrator Roster. The 4,521 requests include 2,456 expungement requests made during a non-simplified customer arbitration that closed by award without a hearing or other than by award, and 2,065 requests that were filed as a straight-in request but did not relate to a previous (non-simplified or simplified) customer arbitration.

An arbitrator or panel from a (non-simplified or simplified) customer arbitration would have been required to decide 590 of the 5,159 expungement requests (11 percent). The 590 expungement requests include 292 requests made during a non-simplified customer arbitration that closed by award after a hearing, 240 expungement requests made during a simplified customer arbitration, and 58 requests filed as a straight-in request to expunge customer dispute information arising from a previous non-simplified customer arbitration that closed by award after a hearing.

Finally, a panel from the Special Arbitrator Roster, or an arbitrator from a simplified customer arbitration, would have been required to decide the remaining 48 arbitration requests that relate to customer dispute information arising from a previous simplified customer arbitration. The arbitrator or panel that would have decided the request is dependent on whether an associated person, or a party on-behalf-of an associated person, would have requested expungement during the simplified arbitration.

## 7. Participation in Expungement Hearings

The proposed rule change would require an associated person to appear personally at an expungement hearing.<sup>190</sup> This requirement would provide the arbitrator or panel the opportunity to ask questions of an associated person to better assess his or her credibility. An associated person would be permitted to cross-examine and seek information from customers who testify.<sup>191</sup> This may provide associated persons with the opportunity to substantiate their arguments in support of their expungement request.

Associated persons may incur additional costs to appear at an expungement hearing. The additional costs may depend on the method of appearance (i.e., by telephone, videoconference, or in person), which, under the proposed rule change, would be determined by the arbitrator or panel. For example, associated persons who would otherwise not appear in person may incur additional costs under the proposed rule change if they are so required. The additional costs include the time and expense to appear, and other direct and indirect costs (e.g., opportunity costs) associated with the associated person's appearance.

The proposed rule change would also help encourage customer participation in an expungement hearing. As noted above, the proposed rule change would require that a named associated person request expungement during a non-simplified customer arbitration and that the arbitrator or panel decide the expungement request if the arbitration closes by award after a hearing. In addition, an expungement request during a

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<sup>190</sup> See proposed Rules 12805(c)(2) and 13805(c)(2).

<sup>191</sup> See proposed Rules 12805(c)(5)(A) and 13805(c)(5)(A).

non-simplified customer arbitration would be considered and decided by the arbitrator or panel from that arbitration.

Further, the proposed time limits for filing straight-in requests may increase customer participation during these arbitrations. The proposed rule change would also provide customers the option to appear at an expungement hearing using whichever method is convenient for them. The proposed rule change would also codify elements of the Guidance that permit the customer to testify, cross-examine the associated person and other witnesses, present evidence at the hearing and make opening and closing arguments.<sup>192</sup>

#### 8. Impact on Business and Professional Opportunities

As a result of the proposed rule change, associated persons may determine that the additional costs to seek expungement relief are higher than the anticipated benefits. In addition, although the proposed rule change is intended to help ensure arbitrators recommend expungement when appropriate as it relates to the merits of the request, an arbitrator or panel may be less likely to recommend expungement depending on the information that becomes available for the reasons described above. This may cause

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<sup>192</sup> Other amendments to the proposed rule change would also help encourage customer participation. For example, the proposed rule change would allow customers to be represented at an expungement hearing and thereby mitigate any potential concern they may have regarding a direct confrontation with the associated person. In addition, the proposed rule change provides that FINRA would notify the customer of the time and place of the expungement hearing. Customers would still retain the option to participate in the expungement hearing or provide their position on the expungement request in writing. The costs to participate would therefore be borne at the customers' discretion.

associated persons not to seek expungement where expungement is likely (or unlikely) to be recommended.

Associated persons who no longer seek, or are not able to expunge customer dispute information from the CRD system and its display through BrokerCheck, or are delayed in doing so, may experience a loss of business and professional opportunities. The loss of business and professional opportunities by one associated person, however, may be the gain of another. Associated persons who may benefit in this regard include those who still determine that the additional costs to seek expungement relief under the proposed rule change is less than the anticipated benefits and continue to seek expungement of customer dispute information, and other associated persons who do not have similar disclosures.

A firm or associated person can also initiate an expungement proceeding directly in a court of competent jurisdiction without first going through any arbitration proceeding. The proposed rule change may incent firms or associated persons to initiate an expungement proceeding directly in a court of competent jurisdiction without first going through any arbitration proceeding. For some firms and associated persons, the anticipated costs to first go through arbitration may be greater than the similar costs to proceed directly in a court of competent jurisdiction. Firms and associated persons who would otherwise first go through arbitration as a result of the proposed rule change may incur additional costs to seek expungement relief.

The number of firms or associated persons who would instead initiate an expungement proceeding directly in a court of competent jurisdiction is dependent not only on the additional costs under the proposed rule change, but the costs a firm or

associated person would expect to incur in the different forums to initiate an expungement proceeding. This information is generally not available, and accordingly the potential effect of the proposed rule change on direct-to-court expungement requests is uncertain.

#### 9. Other Economic Effects

Finally, the proposed rule change may have other marginal economic effects. First, the prohibition of a subsequent expungement request would decrease the potential inefficient allocation of resources resulting from a subsequent request that would have resulted in the same decision (i.e., denial) as the first. The resources of the forum allocated to the additional expungement request could instead be used for other claims or requests that were not previously adjudicated or for other purposes.<sup>193</sup>

Second, the proposed rule change may increase the efficiency of the forum by requiring that a party provide certain information when filing an expungement request. The information includes identification of the customer dispute information that is the subject of the request, and whether expungement of the same customer dispute information was previously requested and, if so, how it was decided. This would increase the efficiency of the forum by enabling FINRA to identify and track a request through the expungement process, and by alerting arbitrators and FINRA to another expungement request of the same customer dispute information. The efficiency of the forum would also increase by requiring an unnamed person to consent to an on-behalf-of expungement request in writing. This would help ensure that an unnamed person is

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<sup>193</sup> The resources relate to the specific costs to administer the claim, as well as the overall attendant costs to administer the forum.

aware of the request and prevent another expungement request by the unnamed person of the same customer dispute information.

In addition, the proposed rule change may affect the value of the customer dispute information to describe the conduct of associated persons. The change in the value of the information depends on the merit of the disclosures that would have otherwise been expunged. The merit of these disclosures also depends on many factors which are difficult to predict. These factors include the incentive of parties to file an expungement request under the proposed rule change, the decisions by the arbitrator or panel to recommend expungement dependent on the information that is available, and the merit of the customer dispute information that would have otherwise been sought to be expunged.

As stated above, the proposed rule change is not structured to increase or decrease the likelihood that an arbitrator or panel recommends expungement in any individual hearing except as it relates to the merits of the request. The proposed rule change may, however, reduce the incentive for an associated person to request expungement even when warranted. The effect of the proposed rule change on the extent to which the customer dispute information available in the CRD system (and its public display through BrokerCheck) accurately describes the conduct of associated persons is, therefore, uncertain.

D. Alternatives Considered

Alternatives to the proposed rule change include amendments that were proposed in Notice 17-42. Notice 17-42 proposed to restrict when a party can file or serve an expungement request during a customer arbitration to 60 days before the first hearing session begins. Although 60 days would provide a customer with more time to address

an expungement request, 60 days may further restrict a party from seeking expungement during a customer arbitration relative to the 30 days before the first scheduled hearing begins in the proposed rule change. FINRA believes that the proposed 30-day period would provide customers with enough time to address an expungement request, and FINRA with sufficient time to notify the states of the request. FINRA also believes that 30 days would reduce the potential that parties would lose their ability to file an expungement request during an arbitration.

Notice 17-42 also proposed that an arbitrator or panel find that the customer dispute information has “no investor protection or regulatory value,” and that there must be a unanimous rather than a majority decision by a panel to recommend expungement. These proposed amendments may increase the difficulty for an associated person to receive an expungement recommendation, and thereby deter an associated person from seeking expungement. After considering the comments, FINRA has determined not to propose that the panel must find “no investor protection or regulatory value” to recommend expungement. FINRA agrees with some commenters that the standard may, if codified into rule language, create confusion among arbitrators and the potential for inconsistent application among different arbitrators and panels.<sup>194</sup> A majority decision is

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<sup>194</sup> FINRA notes that in its Order approving NASD Rule 2130 (now FINRA Rule 2080), which describes the current findings that arbitrators must make to recommend expungement, the SEC stated that “it believes the proposal strikes the appropriate balance between permitting members and associated persons to remove information from the CRD system that holds no regulatory value, while at the same time preserving information on the CRD system that is valuable to investors and regulators.” See Securities Exchange Act Release No. 48933 (December 16, 2003) 68 FR 74667, 74672 (December 24, 2003) (Order Approving File No. SR-NASD-2002-168).

also consistent with what is required for other decisions in customer and industry arbitrations. FINRA also believes that the overall proposal, coupled with the existing standards in FINRA Rule 2080, would be sufficient to help preserve in the CRD system information that is valuable to investors and regulators, while allowing associated persons to remove information that is inaccurate.

Another alternative to the proposed rule change includes different time limits for an associated person to file a straight-in request. Although shorter (longer) time limits may increase (decrease) customer participation in the proceedings and the likelihood that the panel from the Special Arbitrator Roster receives the relevant evidence and testimony to decide an expungement request, shorter (longer) time limits may further (less) constrain an associated person from filing a straight-in request or including more than one expungement request in the same straight-in request. FINRA believes that the time limits proposed herein would facilitate customer participation but also provide associated persons sufficient opportunity to file a straight-in request.

**5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others**

In December 2017, FINRA published Notice 17-42, requesting comment on proposed amendments to the expungement process including establishing a roster of arbitrators with additional training and specific backgrounds or experience from which a panel would be selected to decide an associated person's request for expungement of customer dispute information. The arbitrators from this roster would decide expungement requests where the customer arbitration is not resolved on the merits or the associated person files a straight-in request to expunge customer dispute information.

FINRA received 70 comments in response to Notice 17-42.<sup>195</sup> A copy of Notice 17-42 is attached as Exhibit 2a. A list of comment letters received in response to Notice 17-42 is attached as Exhibit 2b and copies of the comment letters are attached as Exhibit 2c.

In general, individual commenters supported some aspects of the proposal and raised concerns with others. A summary of the comments and FINRA's responses are discussed below.

A. Requirement to Request Expungement during a Customer Arbitration

In Notice 17-42, FINRA proposed that an associated person who is named as a party in a customer arbitration must request expungement during the arbitration or be prohibited from seeking to expunge the customer dispute information arising from the customer's statement of claim during any subsequent proceeding under the Codes.

NASAA and PIABA supported the proposed limitation. NASAA stated that the limitation would help ensure timelier expungement requests and help avoid requests made years after the underlying customer arbitration has closed. PIABA stated that it did not believe that requiring associated persons to request expungement during the customer arbitration would result in more expungement requests because the rule proposal contained "heightened standards applicable to expungement requests" and a "clear process for requesting expungement following the close of the customer case," which may cause "associated persons [to] be more deliberate in making expungement requests."

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<sup>195</sup> All references to commenters are to the comment letters as listed in Exhibit 2b.

Some commenters opposed the limitation for a variety of reasons.<sup>196</sup> Cornell stated that it “could lead associated persons to request expungement in every dispute in order to preserve the right to request expungement.” Keesal stated that these additional expungement requests could result in increased expenses to associated persons and member firms and “could impede the goals of protecting investors and ensuring that FINRA arbitration remains an expedient and cost-effective forum.” Herskovits expressed a concern that an associated person “may be unaware of the important rights he is waiving by failing to file a request for expungement in the underlying arbitration.” Saretsky, responding to FINRA’s concern that customers and documents may be unavailable when an associated person files a separate expungement request years after the customer arbitration closed, stated that customers can be located through counsel or internet searches, and that securities industry rules mandate the retention of important customer and account records for several years. JonesBell and Behr stated that the requirement to request expungement during the customer arbitration should apply only to named associated persons who have also appeared in the arbitration.

FINRA believes that requiring an associated person who is named in a customer arbitration to request expungement during that arbitration or be prohibited from doing so should help limit expungement requests filed years after the customer arbitration concludes, facilitate customer participation in expungement hearings and help ensure that relevant evidence does not become stale or unavailable.<sup>197</sup> The proposed requirement

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<sup>196</sup> See Behr, Cornell, Herskovits, JonesBell, Keesal and Saretsky.

<sup>197</sup> See supra Item 4.C.4., “Time Limits for Straight-in Requests – Quantitative Description.”

would also help ensure that the panel that has heard the merits of the customer's claim at a hearing would decide the expungement request. Accordingly, FINRA believes that all associated persons who are named in non-simplified arbitrations should be required to request expungement during the arbitration, and that the requirement should not depend on whether the associated person has chosen to enter an appearance in response to the complaint. In addition, FINRA notes that if the named associated person requests expungement, under the proposed rule change, the associated person would be required to appear at the expungement hearing.

The proposed amendments would also provide a detailed framework governing the expungement process, which should help ensure that both associated persons and customers are aware of their rights.

FINRA acknowledges commenters' concerns that the proposed limitation could potentially result in an increase in the number of expungement requests and their associated costs. To address this concern, as well as the related concern that the requirement could result in expungement requests by associated persons simply to preserve their right to request expungement, FINRA has modified the proposed rule to allow the associated person to make the request 30 days before the hearing in the customer arbitration.<sup>198</sup> This should provide sufficient time during the customer arbitration for the associated person to evaluate whether an expungement request is warranted and help avoid unnecessary expungement requests.

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<sup>198</sup> See supra Item 3.(a)II.A.1.a.i., "Method of Requesting Expungement."

B. Deadline to File Expungement Request during a Customer Arbitration

In Notice 17-42, FINRA proposed that an expungement request made in a pleading during a customer arbitration must be made no later than 60 days before the first hearing session begins. Three commenters opposed the proposal, stating that the 60-day filing deadline was an impractical or unnecessary restriction that could cause an associated person to miss the deadline and, therefore, an opportunity to file a request.<sup>199</sup> These commenters suggested that the proposal retain the status quo, which allows an associated person to request expungement up to and during any hearing. One commenter, Keesal, supported a deadline of 60 days before the first scheduled hearing date, provided, however, that the associated person “has appeared in [the] Underlying Customer Case.” Keesal stated that this would “ensure[] that all participants” were “on notice of the issues to be addressed and determined at the evidentiary hearing.” SIFMA stated that the proposed requirement “to file for expungement 60 days prior to the first scheduled hearing date” was impractical and would require the payment of expungement fees even though a large portion of cases settle within 60 days of the hearing.

After considering the comments, FINRA does not believe that it is necessary to require a 60-day filing deadline. Instead, the proposed rule change would require that an expungement request be filed no later than 30 days before the first scheduled hearing.<sup>200</sup> This should provide the parties with sufficient case preparation time, as the expungement issues will overlap with the issues raised by the customer’s claim. If a named associated

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<sup>199</sup> See Behr, JonesBell and SIFMA.

<sup>200</sup> See supra Item 3.(a)II.A.1.a.i., “Method of Requesting Expungement.”

person seeks to request expungement after the 30-day filing deadline, the panel would be required to decide whether to grant an extension and permit the request.<sup>201</sup> The purpose of the deadline is to provide the parties other than the associated person with sufficient notice that expungement will be addressed at the hearing.

In addition, FINRA has determined that requiring the party to request expungement at least 30 days before the first “hearing session,” which is typically the initial pre-hearing conference (“IPHC”) rather than the first hearing on the merits, may not provide the requesting party with sufficient time to make an informed decision about whether to request expungement.<sup>202</sup> Therefore, FINRA has modified the proposal to require that an expungement request must be made 30 days before the first scheduled “hearing” begins to provide time for the requesting party to make a better-informed decision.<sup>203</sup>

C. Panel from the Customer Arbitration Decides Expungement Requests  
Where the Customer Arbitration Closes by Award after a Hearing

In Notice 17-42, FINRA proposed that if the customer arbitration closes by award, the panel from the customer arbitration would consider and decide the expungement request during the customer arbitration.

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<sup>201</sup> See supra note 36.

<sup>202</sup> The term “hearing session” means any meeting between the parties and arbitrator(s) of four hours or less, including a hearing or a prehearing conference. See FINRA Rules 12100(p) and 13100(p). The IPHC is scheduled after the panel is appointed. During the IPHC, the panel will set discovery, briefing, and motions deadlines, schedule subsequent hearing sessions, and address other preliminary matters. The parties may agree, however, to forgo the IPHC. See generally FINRA Rules 12500 and 13500.

<sup>203</sup> Under the Codes, a “hearing” means a hearing on the merits. See supra note 20.

Some commenters disagreed with this aspect of the proposal and suggested that a panel selected from the Special Arbitrator Roster should decide all expungement requests, even if the customer arbitration was decided by an award.<sup>204</sup> For example, PIABA stated that a panel from the Special Arbitrator Roster should decide the expungement request separate from the customer's claim because the "decision a panel is asked to make with respect to expungement is different than deciding whether or not to find liability on a customer claim" and because it is "unfair to require a customer to participate in a potentially lengthy expungement hearing that they did not ask for." Grebenik stated that the expungement request should be evaluated separately by an independent panel because the arbitrator may "have bias" and "has heard comments and issues from the customer [about] the actual claim." AdvisorLaw stated that all expungement requests should receive the "same level of review and consideration by a specially trained arbitration panel."

Cornell expressed a concern that the proposed requirement could "transform hearings designed to determine the merits of a customer dispute into lengthy expungement hearings." Cornell proposed, as an alternative, that the same panel from the customer arbitration make the expungement determination, but do so in a separate proceeding to avoid inconveniencing the customer.

Keesal questioned whether the proposed requirement that the panel from the customer arbitration decide the expungement request if the customer arbitration "closes

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<sup>204</sup> See AdvisorLaw, Georgia State, Grebenik, PIABA, St. John's, Tinklenberg and UNLV. In addition, St. John's "strongly agree[d] with requiring associated or unnamed persons to wait until the conclusion of a customer's case to file an expungement request."

by award” would require the panel to decide an expungement request if the cases closes as a result of an order dismissing the case.

In response to the comments, FINRA is clarifying that the panel from the customer arbitration would be required to decide the expungement request and include its decision in the award if the arbitration “closes by award after a hearing” instead of where the arbitration “closes by award.” FINRA believes that where the panel from the customer arbitration has heard the parties’ presentation of the evidence about the customer’s claim, that same panel is best situated to decide the expungement request. In addition, it would generally be more efficient and less costly for the panel from the customer arbitration to decide the expungement request in these circumstances. Although FINRA Rule 2080(b)(1) requires the panel to make a separate, different determination than its determination on the merits of the customer’s claim, the evidence offered with respect to both determinations should generally overlap. Accordingly, FINRA does not believe that it would overly burden the parties if, when the customer arbitration closes by award after a hearing, the panel must also decide the expungement request in addition to the merits of the customer’s claim.

D. Qualifications of Arbitrators on the Special Arbitrator Roster

In Notice 17-42, FINRA proposed that to qualify for the Special Arbitrator Roster, a public chairperson would be required to: (i) have completed enhanced expungement training; (ii) be admitted to the practice of law in at least one jurisdiction; and (iii) have five years’ experience in litigation, federal or state securities litigation, administrative law, service as a securities regulator or service as a judge. Commenters

generally supported the proposed requirements,<sup>205</sup> but were split on whether the members of the Special Arbitrator Roster should be required to be attorneys.<sup>206</sup> One commenter, Black, did not oppose the proposed qualifications but suggested that they would likely result in fewer eligible arbitrators for straight-in requests. PIABA stated that the Special Arbitrator Roster should be made up of attorneys because it would be difficult for FINRA, in some areas of the country, to alternatively fill the Special Arbitrator Roster with local chair-qualified arbitrators that had served on three arbitrations through award. PIABA also stated that arbitrators with legal training may be better equipped to make the distinction between the FINRA Rule 2080 grounds for expungement and deciding the merits of the underlying claim. Keesal, in contrast, stated that there was no rationale for allowing non-attorneys to decide expungement requests made during the customer arbitration, but not brought as a stand-alone claim.

Some commenters also expressed concerns that the arbitrators on the Special Arbitrator Roster were not required to have securities industry experience.<sup>207</sup> FSI stated

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<sup>205</sup> See, e.g., SIFMA (supporting the proposal, and stating that more highly qualified and trained arbitrators should lead to a more efficient and fair process); NASAA (supporting the proposal, and stating that the extent to which the panels truly appreciate the nuanced regulatory issues related to expungement largely depended on the content and effectiveness of the proposed enhanced expungement training).

<sup>206</sup> See AdvisorLaw, FSI, Gocsek, Keesel, Osiason, Rodriguez and White (all opposing the requirement that members of the Special Arbitrator Roster be attorneys). But cf. Cornell, Georgia State, NASAA, PIABA, Schlein, SIFMA, St. John's and Tinklenberg (all supporting the requirement).

<sup>207</sup> See AdvisorLaw, Behr, FSI and JonesBell. Behr and JonesBell also criticized the proposal as allowing claimants' attorneys "whose business is the ligation of customer complaints" to serve on the Special Arbitrator Roster. FINRA notes, however, that the proposal requires that arbitrators on the Special Arbitrator Roster be public arbitrators, and that FINRA's definition of public arbitrators excludes, among other persons, those who devote 20 percent or more of their

that without this background “it may be difficult to appreciate whether information has regulatory significance or investor protection value.” AdvisorLaw stated that “[r]equiring all expungement arbitrators to have a minimum of five years’ experience with the financial services industry [would be] appropriate considering the complexity of expungement requests in cases involving customer dispute information.” In contrast, Public Citizen suggested that at least one FINRA employee who meets the requirements of the Special Arbitrator Roster be a member of every three-person panel that considers an expungement request.

After considering the comments, FINRA has determined not to propose requiring that the members of the Special Arbitrator Roster be attorneys; instead, they would be required to be public arbitrators who have evidenced successful completion of, and agreement with, enhanced expungement training, and have served as an arbitrator through award on at least four customer-initiated arbitrations.<sup>208</sup> FINRA believes that the non-attorneys on its roster who meet these qualifications and complete enhanced expungement training should be appropriately knowledgeable and experienced to decide straight-in requests. The requirement that the arbitrators on the Special Arbitrator Roster be public arbitrators should help ensure that the arbitrators are free of bias. The requirement that they have served on four cases through to award would help ensure that

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professional time to representing parties in disputes concerning investment accounts or transactions, or employment relationships within the financial industry. See FINRA Rules 12100(aa) and 13100(x); see also supra note 7.

<sup>208</sup> See proposed Rule 13806(b)(2)(B). In addition, to qualify for the Special Arbitrator Roster, the arbitrators must be chairpersons and, therefore, will have completed the training that arbitrators must complete before they can be added to the chairperson roster. See also supra note 79.

the members of the Special Arbitrator Roster have the necessary knowledge and experience to conduct hearings in the forum.

Although FINRA believes that a sufficient number of arbitrators on its roster would meet these additional qualifications, if the Commission approves the proposed rule change, FINRA would engage in efforts to recruit arbitrators for the Special Arbitrator Roster. FINRA notes that its Office of Dispute Resolution has embarked on an aggressive campaign to recruit new arbitrators, with a particular focus on adding arbitrators from diverse backgrounds, professions and geographical locations.<sup>209</sup>

FINRA's commitment and focus on this critical initiative have resulted in increases in under-represented categories of arbitrators.<sup>210</sup> FINRA believes its continued commitment to this important initiative will help the forum improve the quality, depth and diversity of its public chairperson roster.

E. Special Arbitrator Roster Decides Expungement Requests if the Customer Arbitration Closes other than By Award or By Award Without a Hearing

In Notice 17-42, FINRA proposed that if the customer arbitration closes other than by award (e.g., the parties settle the arbitration), the panel in that arbitration would not decide the associated person's expungement request. Instead, the associated person would be permitted to file an expungement request as a new claim under the Industry

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<sup>209</sup> See Our Commitment to Achieving Arbitrator and Mediator Diversity at FINRA, <https://www.finra.org/arbitration-mediation/our-commitment-achieving-arbitrator-and-mediator-diversity-finra>.

<sup>210</sup> See supra note 209.

Code against the member firm at which he or she was associated at the time of the events giving rise to the customer dispute.

The SEC Investor Advocate supported the proposal because FINRA's data showed that where the arbitration case was not decided on the merits, the expungement rate was "simply too high for an extraordinary remedy." (emphasis in original). NASAA also supported the proposal, stating that "post-settlement expungement hearings often consist of a one-sided presentation of the facts" because "investors and their counsel have little incentive to participate after the customer's concerns have been resolved."

Some commenters disagreed with the proposal to require the associated person to file a new arbitration under the Industry Code if the customer arbitration closes other than by award, as inefficient or burdensome on associated persons.<sup>211</sup> As an alternative, SIFMA suggested that the panel from the customer arbitration decide the request; but, to address FINRA's concern for greater training and increased qualifications for those arbitrators determining expungement, SIFMA suggested that the proposed rule change require that at least one arbitrator on every three-person panel be selected from the Special Arbitrator Roster at the inception of each customer arbitration.

Saretsky stated that associated persons should be able to name the customer, and that the "minor inconvenience" to the customer was outweighed by the harm to the

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<sup>211</sup> See Behr, Herskovits, JonesBell, Saretsky and SIFMA. Herskovits also stated that "[financial advisors] will respond to the proposed rule by filing a counterclaim or cross claim for expungement in the customer arbitration, thus preventing the customer arbitration from closing before a hearing is held on expungement or the [financial advisors'] other claims for relief." FINRA notes, however, that under the proposed rule change, a request for expungement relief would not prevent a customer arbitration from closing.

associated person. PIABA stated that it would be “inappropriate” to name customers. St. John’s “support[ed] allowing the proposed expungement process to proceed without the customer having to be named a party to the request.”

Schlein expressed concerns that a former employing member firm may have “little or no economic incentive to cooperate in an expungement proceeding,” and that it “would also be difficult for the panel to elicit potentially relevant facts” where the “economic and reputational interests of the associated person and the employer are aligned.” Schlein also stated that an “aggrieved customer has no economic incentive to participate in an expungement proceeding that occurs only after the underlying case has concluded.” Schlein also expressed concern that expungement requests would be referred to the Special Arbitrator Roster even if the matter settled on the eve of hearing, when it may be more efficient and promote investor protection to require the existing panel to hear the expungement request. Schlein stated that “FINRA could ameliorate the possibility that a panel might receive one-sided information” by (i) providing the expungement panel with significant filings from the underlying customer dispute, (ii) permitting the panel to review the parties’ settlement papers and (iii) giving the associated person, firm, and the customer the right to provide the panel with transcripts of the underlying customer proceeding.

FINRA believes that where there has not been a hearing on the merits of the customer’s claim, the members of the Special Arbitrator Roster, who would be public chairpersons who have served on at least four customer arbitrations in which a hearing was held and received enhanced expungement training, would be better situated to decide expungement requests than the panel from the customer arbitration. FINRA does not

believe that requiring the associated person to file a new arbitration under the Industry Code would unduly burden the associated person—instead of presenting evidence related to the expungement request to the arbitrators in the customer arbitration in a separate expungement hearing, they would instead present the evidence supporting the expungement request to a panel randomly selected from the Special Arbitrator Roster.

FINRA shares commenters’ concerns that the factual record could be less well-developed where a straight-in request is filed against a member firm and the associated person or member firm’s interests are aligned, or where the customer does not participate. FINRA does not believe, however, that the customer should be named as a respondent or be required to participate in an expungement proceeding after the customer’s claim has been resolved (e.g., after the claim is settled). Instead, the proposed rule change addresses concerns that straight-in requests filed against the member firm may be non-adversarial or lack customer participation by, among other things (i) requiring that straight-in requests be decided by three randomly selected public chairpersons with enhanced training and experience,<sup>212</sup> (ii) requiring the panel to review the settlement documents,<sup>213</sup> (iii) granting the panel the explicit authority to request from the associated person, the member firm at which he or she was associated at the time the customer dispute arose or other party requesting expungement, any documentary, testimonial or

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<sup>212</sup> See supra Item 3.(a)II.B.2.b., “Straight-in Requests and the Special Arbitrator Roster, Composition of the Panel.”

<sup>213</sup> See proposed Rules 12805(c)(7) and 13805(c)(7).

other evidence that it deems relevant to the expungement request,<sup>214</sup> and (iv) including provisions to encourage and facilitate customer participation in expungement hearings.<sup>215</sup>

In response to commenters' concerns, FINRA has modified the language in the proposed rule change to require that a straight-in request be filed against the member firm at which he or she was associated "at the time the customer dispute arose," consistent with the language used in other FINRA rules, instead of "at the time of the events giving rise to the customer dispute."<sup>216</sup>

F. Three Randomly Selected Arbitrators Decide Straight-in Requests

In Notice 17-42, FINRA proposed that the NLSS would randomly select three public chairpersons to serve on the Special Arbitrator Roster who would decide the request for expungement, and that the first arbitrator selected would be the chairperson. The parties would not be permitted to agree to fewer than three arbitrators or to the use of pre-selected arbitrators. The associated person seeking expungement would not be permitted to strike any arbitrators, but would be able to challenge a selected arbitrator for cause.

PIABA and AdvisorLaw supported the proposed random selection of three arbitrators. PIABA stated that the random selection of three arbitrators would "reduce the risk of arbitrators being concerned about ruling against an associated person for fear they may not be selected for another panel."

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<sup>214</sup> See proposed Rules 12805(c)(6) and 13805(c)(6).

<sup>215</sup> See supra Item 3.(a)II.D.3., "Customer's Participation during the Expungement Hearing."

<sup>216</sup> See, e.g., FINRA Rules 12901(a)(1)(C) and 13903(b); see also Kessal.

Other commenters opposed the proposed rule change. SIFMA expressed concerns that not permitting parties to rank and strike arbitrators would remove the parties' involvement and input.<sup>217</sup> SIFMA also stated that there was no compelling need to use three rather than a single arbitrator, and that the proposal would increase the financial burden on registered representatives seeking expungement. Walter stated that a single FINRA-qualified arbitrator with the special qualifications would be "more than qualified to make a determination as to expungement" and that "[h]aving to coordinate the schedules of three arbitrators will delay the processing and will impose unnecessarily high additional costs on all parties involved."<sup>218</sup> Tinklenberg opposed the three-person panel requirement because of the associated costs. Baritz stated that the three-person panel requirement would increase expenses to associated persons and the "time necessary to rank and choose a panel," and "significantly delay the process."

Keesal opposed the random selection of three arbitrators as unfair to associated persons, and suggested that FINRA "randomly select a minimum of 12 proposed arbitrators to serve on an expungement case, from which the associated person and anyone else involved in the case can rank and strike the proposed panelists."

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<sup>217</sup> SIFMA also proposed that "to preserve arbitrator neutrality and foster greater transparency," FINRA make publicly available all training materials, communications with arbitrators regarding expungement, and documents related to the addition, removal or exclusion of any arbitrators from the roster. FINRA notes that making such communications and documents publicly available could have a chilling effect on arbitrator recruitment and communications. FINRA does, however, make expungement training materials publicly available. See supra note 81.

<sup>218</sup> See also Saretsky.

FINRA notes that since straight-in requests may be complex, may not be actively opposed by another party and the customer or customer's representative typically does not appear at the hearing, having three arbitrators from the Special Arbitrator Roster available to ask questions and request evidence would help ensure that a complete factual record is developed to support the arbitrators' decision. In addition, FINRA believes that requiring two out of three randomly selected public chairpersons with enhanced training and qualifications to agree that expungement is appropriate in straight-in requests should help FINRA maintain the integrity of its CRD records and ensure that expungement is recommended in limited circumstances and only when one of the FINRA Rule 2080(b)(1) grounds applies.

FINRA does not believe that selecting three rather than one arbitrator would overly burden the parties during the proceeding or result in undue delay. As the parties would not be permitted to rank or strike these arbitrators, this should shorten the average length of the proceeding.<sup>219</sup> In addition, pursuant to FINRA Rule 13403, FINRA would send the lists generated by the NLSS to all parties at the same time, within approximately 30 days after the last answer is due, regardless of the parties' agreement to extend any answer due date.

FINRA recognizes that the proposed random arbitrator selection process would limit party input on arbitrator selection. However, the arbitrators on the Special Arbitrator Roster would have the experience, qualifications and training necessary to

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<sup>219</sup> Under the Codes, the lists of ranked arbitrators must be completed and returned to the Director no more than 20 days after the date the Director sends the lists to the parties. See, e.g., FINRA Rules 12403(c)(3) and 13404. However, the parties may agree to extend the due date. See FINRA Rules 12105 and 13105.

conduct a fair and impartial expungement hearing in accordance with the proposed rules, and to render a recommendation based on a complete factual record developed during the expungement hearing. FINRA believes that the higher standards that the arbitrators must meet to serve on the Special Arbitrator Roster should mitigate the impact of the absence of party input on the selection of arbitrators. In addition, associated persons and member firms would still be permitted to challenge any arbitrator for cause.<sup>220</sup>

G. Simplified Arbitrations

In Notice 17-42, FINRA proposed to require that an associated person or unnamed person wait until the conclusion of a customer's simplified arbitration case to file an expungement request, which would be filed under the Industry Code against the member firm at which he or she was associated at the time the customer dispute rose and would be heard by a panel selected from the Special Arbitrator Roster.

Some commenters supported the proposal.<sup>221</sup> PIABA stated that it would address a flaw in the current process, whereby a hearing is held to consider expungement even if the customer has not requested a hearing under FINRA Rule 12800, and that it would eliminate delays in securing an award because the arbitrator is considering the request for expungement. PIABA also stated that a single arbitrator should not be permitted to decide an expungement request in a simplified arbitration because the goals of the proposed amendments should not be affected simply because the misconduct involved \$50,000 or less.<sup>222</sup> The SEC Investor Advocate stated that it would be easier for a broker

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<sup>220</sup> See proposed Rule 13806(b)(4).

<sup>221</sup> See NASAA, PIABA, The SEC Investor Advocate, St. John's and UNLV.

<sup>222</sup> See also UNLV.

to convince one arbitrator to recommend expungement. St. John's stated that "separating the expungement request from the underlying customer case" should result in "faster decisions in simplified cases."

Some commenters opposed the proposed change and stated that the arbitrator who heard the evidence in the underlying simplified customer arbitration would be most qualified to determine an expungement request, and that it was unfair to impose the burden of a subsequent arbitration on the associated person in this circumstance.<sup>223</sup>

After considering the comments, FINRA has revised the proposed rule change to provide that if a party requests expungement during a simplified arbitration, the single arbitrator from the simplified arbitration would be required to decide the expungement request, regardless of how the simplified arbitration case closes (e.g., even if the case settles).<sup>224</sup> FINRA believes that it is appropriate for the single arbitrator in a simplified arbitration case to decide expungement requests, regardless of how the underlying case closes, due to the lower monetary requirement and generally less complex nature of these cases. To address concerns that customers should not be required to participate in a hearing addressing expungement requests in simplified arbitrations, the proposed rule change would require arbitrators to hold a separate expungement-only hearing after the customer's dispute is decided to consider the expungement request if the customer elects to have his or her claim decided on the papers or through an Option Two special

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<sup>223</sup> See Behr, JonesBell and Keesal.

<sup>224</sup> See proposed Rule 12800(e)(1).

proceeding. The arbitrator would be required to issue a subsequent, separate award in connection with the expungement-only hearing.<sup>225</sup>

H. Fees that Parties Will Incur to File a New Claim Under the Industry Code to Request Expungement

Some commenters expressed concerns that if an associated person were required to file a separate claim under the Industry Code to request expungement after the customer arbitration closes other than by award, the member firm and associated person would be assessed the filing fee, member surcharge and process fees twice, in both the underlying customer arbitration and the separate straight-in request.<sup>226</sup> SIFMA stated that this could increase the costs of expungement and have the “indirect effect of increasing the costs of settlement, potentially discouraging settlement in smaller cases due to the increased costs associated with expungement.”

FINRA believes that it is appropriate to assess the member surcharge and process fee for straight-in requests because they are separate arbitrations before a separate panel of specially trained arbitrators. The member firm, having not previously paid a member surcharge and process fee for the expungement request, would be assessed these fees when and if a straight-in request is filed. FINRA would not, however, assess a second filing fee when an associated person files a straight-in request if the associated person, or the requesting party if it is an on-behalf-of request, has previously paid the filing fee to

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<sup>225</sup> See proposed Rule 12800(e)(1)(A).

<sup>226</sup> See Janney, Keesal and SIFMA.

request expungement of the same customer dispute information during a customer arbitration.

I. Arbitrators “Recommend” Rather than “Grant” Expungement

In Notice 17-42, FINRA requested comment on whether to revise FINRA Rules 12805 and 13805 to state that the panel may “recommend” rather than “grant” expungement if the FINRA Rule 2080 standards are satisfied. Several commenters supported the revision as a clarifying change that would more accurately reflect the panel’s role in the expungement process.<sup>227</sup> For example, PIABA stated that after the panel recommends expungement, under FINRA Rule 2080 the member or associated person “must obtain an order from a court of competent jurisdiction confirming the arbitration award containing expungement relief.” AdvisorLaw and Tinklenberg opposed the proposed rule change, with AdvisorLaw stating that “grant” should be retained because “[i]t has long been established that the decisions made in arbitration are final and binding upon the parties,” and that “[c]hanging the language of the Rule from the word ‘grant’ to ‘recommend’ may lessen the perceived binding effect of the decision.”<sup>228</sup>

FINRA believes that “recommend” more accurately captures the panel’s authority in the expungement process. Pursuant to FINRA Rule 2080, FINRA will only expunge customer dispute information after a court of competent jurisdiction enters an order requiring it to do so. Accordingly, the proposed rule change would change the word “grant” to “recommend” in proposed Rules 12805 and 13805.<sup>229</sup>

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<sup>227</sup> See Black, Cornell, Georgia State, Gocsek, Keesal and PIABA.

<sup>228</sup> See also Wellington.

<sup>229</sup> See supra note 9.

## J. Unanimity of Decision

In Notice 17-42, FINRA proposed that to recommend expungement, a three-person panel of arbitrators would be required to agree unanimously to recommend expungement. Some commenters opposed the unanimity requirement as making it too difficult to obtain expungement or because it was inconsistent with the ability of a customer to prevail by a majority decision.<sup>230</sup> SIFMA, for example, stated that the unanimity requirement would “impinge upon the fundamental fairness of the expungement process in providing an effective balance to the allegation-based complaint reporting regime and will have a significant impact on registered representatives’ ability to protect their livelihoods and reputations.” JonesBell and Behr stated that “[t]o require a unanimous decision on any expungement request obviously would give a single individual sitting on a three-member panel the power to prevent, for improper reason or no good reason at all, a meritorious request that a false or erroneous claim be removed from a representative’s CRD record.”

Other commenters supported requiring a unanimous decision to recommend expungement.<sup>231</sup> For example, PIABA stated that the unanimity requirement would help ensure that expungement was an extraordinary remedy that is only granted when it has no

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<sup>230</sup> See AdvisorLaw, Behr, Gocsek, Hagenstein, Higgenbotham, Janney, JonesBell, Keesal, Leven, Mahoney, Saretsky, SIFMA, Smart, Speicher, Tinklenberg and White.

<sup>231</sup> See Black, Cornell, Georgia State, Liebrader, NASAA, PIABA, Public Citizen, The SEC Investor Advocate and UNLV. In addition, Wellington stated that if an expungement was endorsed unanimously, the term “grant” should be retained, there should be little or no cost to the requesting party, and the associated person should not have to obtain a court order directing the expungement.

meaningful investor protection or regulatory value. The SEC Investor Advocate stated that the requirement would provide greater “assurance that only meritless complaints are expunged,” and expressed hope “that this requirement will encourage brokers to only seek expungement when the underlying customer dispute information is meritless.” Cornell stated that the “unanimity requirement protects public investors by ensuring that the threshold for expungement is high,” and that, “given the history of abuse of the expungement process,” would “help[] to ensure that when expungement is granted, the expungement is legitimate.”

After considering the comments, FINRA has determined to allow arbitrators to recommend expungement through a majority decision, consistent with what is required for other decisions in customer and industry arbitrations.<sup>232</sup> FINRA believes that requiring a majority of arbitrators to agree that expungement is appropriate should be sufficient to help preserve in the CRD system information that is valuable to investors and regulators, while allowing associated persons a reasonable mechanism to remove information that is inaccurate. FINRA notes, however, that if the SEC approves the proposed rule change, FINRA will continue to monitor the expungement process to determine if additional changes are needed.

K. No Investor Protection or Regulatory Value

In Notice 17-42, FINRA proposed to require that a panel find that customer dispute information has “no investor protection or regulatory value” to recommend

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<sup>232</sup> See FINRA Rules 12904(a) and 13904(a).

expungement. Several commenters opposed the requirement.<sup>233</sup> For example, Herskovits stated that the standard was vague and opened the possibility of inconsistent rulings among different panels. FSI stated that the proposal was “confusing as it is difficult to imagine a scenario where information that is false, clearly erroneous, factually impossible or did not involve the advisor, would have regulatory or investor protection value.” SIFMA stated that the requirement was redundant in light of the current high standards in FINRA Rule 2080(b)(1), may have the effect of discouraging meritorious expungement claims, was already incorporated into the Guidance and would transform the traditional role of arbitrators as fact-finders and require them to make a policy determination in each case. Keesal stated that the change would unnecessarily complicate the expungement process to the detriment of associated persons with no corresponding investor protection value. Saretsky proposed that arbitrators instead be required to find that the customer dispute had no “reasonable” investor protection or regulatory value.

NASAA expressed a concern with the proposal because it would allow arbitrators, rather than regulators, to make the finding. The SEC Investor Advocate expressed the same concern, and suggested that FINRA provide a framework on how the standard should be interpreted and applied to avoid disparate interpretations and outcomes. Schlein stated that arbitrators “should receive supplemental training on the proposed new standard,” and that FINRA should also “offer training or instructional materials to judges” who will be required to confirm an expungement award.

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<sup>233</sup> See Baritz, FSI, Gocek, Herskovits, Janney, Keesal, Saretsky, SIFMA and White.

Other commenters supported the requirement.<sup>234</sup> For example, PIABA suggested that arbitrators should be required to make the finding because in practice arbitration panels “often believe that the Rule 2080 standards are easily met” and “do not grasp the fact that” a claim may not be factually impossible or false even though a customer has not met his or her burden of proof for purposes of establishing liability or rebutting an affirmative defense. St. John’s stated that the proposed requirement would “help strengthen investor protection by improving confidence in the accuracy of the CRD system and BrokerCheck.” Cornell stated that the requirement would allow the panel to look beyond the claim and at the associated person’s record as a whole, including other customer dispute information, which would protect public investors. Liebrader stated that “[t]oo many legitimate claims disappear from public view in the largely uncontested expungement process.”

After considering the comments, FINRA has determined not to propose that the panel must find “no investor protection or regulatory value” to recommend expungement. FINRA agrees with some commenters that the standard may, if codified into rule language, create confusion among arbitrators and the potential for inconsistent application among different arbitrators and panels.<sup>235</sup> FINRA also believes that the

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<sup>234</sup> See Cornell, Liebrader, PIABA, St. John’s and UNLV.

<sup>235</sup> FINRA notes that in its Order approving NASD Rule 2130 (now FINRA Rule 2080), which describes the current findings that arbitrators must make to recommend expungement, the SEC stated that “it believes the proposal strikes the appropriate balance between permitting members and associated persons to remove information from the CRD system that holds no regulatory value, while at the same time preserving information on the CRD system that is valuable to investors and regulators.” See Securities Exchange Act Release No. 48933

overall proposal, coupled with the existing standards in FINRA Rule 2080, would be sufficient to help preserve in the CRD system information that is valuable to investors and regulators, while allowing associated persons to remove information that is inaccurate.

L. Panel Must Identify One of the FINRA Rule 2080(b)(1) Grounds for Expungement

In Notice 17-42, FINRA clarified in proposed Rules 12805 and 13805 that the FINRA Rule 2080 grounds for expungement that the panel must identify to recommend expungement are the grounds stated in paragraph (b)(1) of FINRA Rule 2080. In response to Notice 17-42, PIABA supported clarifying “that an arbitration panel may not recommend expungement on grounds other than those set forth in Rule 2080.” Keesal, however, viewed FINRA’s proposal as “remov[ing] the arbitrator’s ability to grant expungement relief based on judicial or arbitral findings other than those listed in Rule 2080(b)(1).”<sup>236</sup>

FINRA notes that under current FINRA Rule 12805, arbitrators are required to base their expungement recommendations on one of the three grounds listed in FINRA

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(December 16, 2003) 68 FR 74667, 74672 (December 24, 2003) (Order Approving File No. SR-NASD-2002-168).

<sup>236</sup> See also Baritz; compare SIFMA (stating that “FINRA already imposes high standards in order for arbitrators to recommend expungement,” and that “FINRA Rule 2080(b)(1) requires a finding either that: (i) the claim or allegation is factually impossible or clearly erroneous; (ii) the registered person was not involved in the alleged sales practice violation, forgery, theft, misappropriation or conversion of funds, or (iii) the claim, allegation, or information is false”).

Rule 2080(b)(1).<sup>237</sup> Accordingly, the proposed rule change clarifies in proposed Rules 12805 and 13805 that the grounds for expungement that the panel must indicate in its award are the grounds in FINRA Rule 2080(b)(1).<sup>238</sup>

M. Time Limits for Straight-in Requests

In Notice 17-42, FINRA proposed that for customer arbitrations, associated persons must file straight-in requests within one-year from the date the customer arbitration closed. For customer complaints, FINRA proposed that associated persons must file straight-in requests within one-year from the date that a member firm initially reported the complaint to the CRD system. For customer arbitrations that close and customer complaints that are reported prior to the effective date of the proposed rule change, the associated person would have six months from the effective date of the rule, if approved by the Commission, to file the expungement request.

Some commenters opposed the proposed time limitations as unwarranted or too short.<sup>239</sup> For example, SIFMA stated that the one-year time limitation is unnecessary because the general six-year period to file all claims also applies to expungement requests. SIFMA also stated that the one-year time limitation is insufficient for firms to properly investigate and respond to customer complaints, and would create inefficiency

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<sup>237</sup> See Regulatory Notice 08-79 (December 2008) (stating that “[t]he arbitration panel must indicate which of the grounds for expungement under Rule 2130(b)(1)(A)–(C) serve as the basis for their expungement order, and provide a brief written explanation of the reasons for ordering expungement”).

<sup>238</sup> See proposed Rules 12805(c)(8) and 13805(c)(8).

<sup>239</sup> See AdvisorLaw, Barber, Baritz, Behr, Brookes, FSI, Glenn, Grebenik, Herskovits, Higgenbotham, JonesBell, Keesal, Leven, Saretsky, SIFMA, Smart, Speicher, Stephens and Walter.

by requiring the filing of requests to expunge customer complaints that would then be stayed if they evolved into an arbitration. SIFMA also requested “further guidance on the extended time period that will be afforded registered representatives who have eligible claims for expungement that would become ineligible if the rule proposals were implemented.”<sup>240</sup> JonesBell and Behr stated that an associated person may be unaware that a member firm “has reported a customer complaint on his or her CRD.”<sup>241</sup> FSI stated that associated persons should have three years to file expungement requests to provide them with time to assess how the information will impact their business, which may not be immediately apparent. Keesal stated that because customers may wait up to six years to file an arbitration claim under FINRA Rule 12206 after making a customer complaint, the proposed time limits would be unfair and would increase the frequency of requests, as the associated person would have to make a second expungement request if the customer complaint was later the subject of an arbitration claim. Saretksy stated that the time restriction was unnecessary because arbitrators are “free to weigh the evidentiary value (if any) of an associated person’s undue delay.” Herskovits stated that FINRA’s concern about document retention was “misplaced” because SEC and FINRA rules “generally mandate the preservation of most records for 3 to 6 years (and many firms preserve documents for longer periods of time).” Grebenik expressed concerns with the proposed

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<sup>240</sup> See also AdvisorLaw (stating that providing six months where the customer arbitration closes on or prior to the effective date of the proposed rule change was arbitrary and creates an unjustifiable distinction between cases that close prior to the rules and those that close after).

<sup>241</sup> See supra note 47.

time limits because there were “thousands of advisors who have customer disputes and do not know about the expungement process.”

Other commenters supported the time limits.<sup>242</sup> For example, UNLV stated that the proposed time limit would ensure “that relevant evidence is available and increases investors’ ability to participate.” In response to other commenters’ suggestion that brokers may not be aware of a customer complaint, Cornell stated that “public investors should not be penalized for the failure of firms to implement streamlined notification and recordkeeping procedures,” and that “it is not too much to ask that the associated person follow up as to disposition by the firm.”

PIABA “strongly support[ed] a definite cut-off date for requests for expungement,” and stated that a customer is “far more likely to participate in an expungement hearing when it takes place in close proximity to the resolution of the underlying arbitration proceeding.” PIABA also stated that a more stringent time limit would lead to higher quality evidence, which becomes less reliable and available with the passage of time. PIABA stated that when the arbitration results in an award, a shorter timeframe of 90 days is preferable because significant time will already have passed from the filing of the customer’s arbitration claim, and because 90 days matches the deadline to file a motion to vacate an arbitration award under the Federal Arbitration Act. PIABA also stated that, because member firms and associated persons control the date that information is reported in the CRD system, the time limit for customer complaints should

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<sup>242</sup> See Cornell, Georgia State, PIABA, Public Citizen and Schlein.

run from the shorter of the date the firm initially reported the complaint in the CRD system or a month after the associated person receives notice of the complaint.

After considering the comments, FINRA believes that adjustments to the originally proposed time limitations are warranted to provide sufficient time for associated persons to determine whether to seek expungement of customer dispute information. Accordingly, FINRA has revised the proposal to provide for a two-year period to file an expungement request when a customer arbitration or civil litigation that gives rise to customer dispute information closes.<sup>243</sup> The two-year period would help ensure that the expungement hearing is held close in time to the customer arbitration or civil litigation, when information regarding the customer arbitration is available and in a timeframe that would increase the likelihood for the customer to participate if he or she chooses to do so. At the same time, it would allow the associated person time to determine whether to seek expungement.

For customer complaints where no customer arbitration or civil litigation gave rise to the customer dispute information, the proposed rule change would provide for six years from the date that the customer complaint was initially reported to the CRD system for the associated person to file the expungement request.<sup>244</sup> Six years would allow firms time to complete investigations of customer complaints and close them in the CRD system and for the complaints to evolve, or not evolve, into an arbitration. Thus, the revised proposal would help avoid unnecessary duplicative requests to expunge customer

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<sup>243</sup> See proposed Rule 13805(a)(2)(A)(iv).

<sup>244</sup> See proposed Rule 13805(a)(2)(A)(v).

complaints that subsequently evolve into arbitrations or civil litigations, while providing reasonable time limits to encourage customer participation and help ensure the availability of evidence. The proposed six-year time limitation is also consistent with FINRA's general eligibility rule, which provides that no claim shall be eligible for submission to arbitration under the Code where six years have elapsed from the occurrence or event giving rise to the claim.<sup>245</sup>

The proposed rule change makes similar revisions to the time limits described in Notice 17-42 to seek to expunge customer dispute information that arose prior to the effective date of the proposed rule change. For customer dispute information arising from customer arbitrations or civil litigations that closed on or prior to the effective date of the proposed rule change, the expungement request would be required to be made within two years of the effective date of the proposed rule change.<sup>246</sup> For customer complaints initially reported to the CRD system on or prior to the effective date of the proposed rule change, where no customer arbitration or civil litigation gave rise to the customer dispute information, the expungement request would be required to be made within six years of the effective date of the proposed rule change.<sup>247</sup>

N. Effect of Withdrawal of Expungement Request

In Notice 17-42, FINRA proposed that if the associated person withdraws an expungement request after the panel is appointed in a straight-in request, the case would be closed with prejudice, unless the panel decides otherwise. AdvisorLaw supported the

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<sup>245</sup> See supra note 13.

<sup>246</sup> See proposed Rule 13805(a)(2)(B)(i).

<sup>247</sup> See proposed Rule 13805(a)(2)(B)(ii).

proposal, stating that it would “create safeguards, and prevent an associated person from simply withdrawing their case and refile in hopes of drawing a more favorable pool of randomly selected arbitrators.”

Under the proposed rule change, for expungement requests during customer arbitrations and straight-in requests, if the associated person withdraws or does not pursue the expungement request (or the party, with the written consent of the unnamed person, withdraws or does not pursue the request), the panel would be required to deny the expungement request with prejudice.<sup>248</sup> These requirements would foreclose the ability of associated persons withdrawing expungement requests to avoid having their requests decided by the panel, and then seeking to re-file the request and receive a new list of arbitrators and a potentially more favorable panel and decision.

O. Associated Person’s Appearance Required at the Expungement Hearing

In Notice 17-42, FINRA proposed that an associated person seeking to have his or her CRD record expunged would be required to appear at the expungement hearing either in person or by video conference. Five commenters supported the proposal, stating generally that this would allow the arbitrators to better assess the associated person’s demeanor and credibility.<sup>249</sup> UNLV also stated that requiring videoconferencing would carry minimal costs given its widespread availability at FINRA’s regional offices and other venues. NASAA stated that the broker should be required to appear in-person, “given the extraordinary relief the broker is seeking.” Georgia State also supported

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<sup>248</sup> See proposed Rules 12805(a)(1)(D)(i), 12805(a)(2)(E)(i) and 13805(a)(4).

<sup>249</sup> See Black, Caruso, Cornell, PIABA and UNLV.

requiring an associated person to appear in person at the hearing, and stated that appearance by video conference should only “be permitted, if at all, in those simplified cases where a hearing did not take place.”

Six commenters preferred to allow the associated person to appear by telephone.<sup>250</sup> SIFMA, for example, stated that there appeared to be no basis for allowing customers, but not associated persons, to appear by telephone, and that the proposal would “greatly increase the cost of expungement through attendant travel costs and loss of productivity.” Three commenters stated that the arbitrators should decide the method of appearance.<sup>251</sup> White, for example, stated that telephonic testimony “might be acceptable in limited circumstances,” and suggested that “arbitrators can make this determination and the Rule should not limit their flexibility to do so.”

After considering the comments, the proposed rule change would allow the panel to determine the method of appearance by the associated person—by telephone, in person or by video conference.<sup>252</sup> As the associated person is requesting the permanent removal of information from his or her CRD record, FINRA believes the associated person should personally participate in the expungement hearing to respond to questions from the panel and those customers who choose to participate. Rather than restrict the method of appearance, the panel would have the authority to decide which method of appearance would be the most appropriate for the particular case.<sup>253</sup> FINRA believes that providing

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<sup>250</sup> See Baritz, Gocek, Grebenik, Keesal, SIFMA and Tinklenberg.

<sup>251</sup> See AdvisorLaw, Robbins and White.

<sup>252</sup> See proposed Rules 12805(c)(2) and 13805(c)(2).

<sup>253</sup> See supra note 252.

flexibility as to the method of appearance would encourage appropriate fact-finding by the arbitrators and generally strengthen the process.

P. Customer Notification

In Notice 17-42, FINRA proposed that when an expungement request is filed separately from the customer arbitration, FINRA would notify the parties from the customer arbitration or the customer who initiated the complaint that is the subject of the request about the expungement request. PIABA supported the proposed customer notification requirement. Georgia State recommended “additional notifications to the investor about the expungement hearing.”

The proposed rule change modifies the proposal in Notice 17-42 to add an additional notification to help ensure that customers receive timely notice of both the expungement request and the expungement hearing. The associated person would be required to serve all customers whose customer arbitrations, civil litigations and customer complaints gave rise to customer dispute information that is a subject of the expungement request with notice of the request by serving on the customers a copy of the statement of claim requesting expungement before the first scheduled hearing session is held.<sup>254</sup> The Director would then notify the customers of the time, date and place of the expungement hearing using the customers’ current address provided by the party seeking expungement.<sup>255</sup>

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<sup>254</sup> See proposed Rule 13805(b)(1)(A); see also supra note 133.

<sup>255</sup> See proposed Rule 13805(b)(2); see also supra note 136.

Q. Customer Participation during the Expungement Hearing

In Notice 17-42, FINRA proposed that, consistent with the Guidance, all customers in the customer arbitration or who filed a customer complaint would be entitled to appear at the expungement hearing. At the customer's option, the customer could appear by telephone.

In response to Notice 17-42, PIABA and The SEC Investor Advocate stated that FINRA should codify all of the customer rights provided in the Guidance, including, for example, allowing the customer or their counsel to introduce documents and other evidence and to cross-examine the broker or other witnesses called by the broker seeking expungement.<sup>256</sup>

FINRA agrees that the customer rights contained in the Guidance should be codified, as reflected in the proposed rule change.<sup>257</sup> In addition to incorporating the customer rights contained in the Guidance, the proposed rule change also clarifies that the customer may be represented and states that the customer may appear at the expungement hearing by telephone, in person, or by video conference. In addition, if a customer testifies, the associated person or other person requesting expungement would be allowed to cross-examine the customer. If the customer introduces any evidence at the expungement hearing, the associated person or party requesting expungement could object to the introduction of the evidence, and the panel would decide any objections. The proposed rule change would allow and encourage customers to participate fully in

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<sup>256</sup> See also St. John's.

<sup>257</sup> See proposed Rules 12805(c) and 13805(c).

the expungement hearing, while providing the associated person with a reasonable opportunity to rebut evidence introduced by the customer.<sup>258</sup>

R. State Notification

In response to Notice 17-42, NASAA requested “earlier notices to state regulators of an expungement request to better facilitate regulator involvement where appropriate.”<sup>259</sup> The proposed rule change provides that FINRA would notify state securities regulators, in the manner determined by FINRA, of the associated person’s expungement request within 30 days after receiving a complete request for expungement, so that the states are timely notified of the request.<sup>260</sup>

S. Unnamed Persons

In Notice 17-42, FINRA proposed to codify the ability of a party in a customer arbitration to request expungement on behalf of an unnamed person. AdvisorLaw stated that it opposed the practice and suggested that FINRA prohibit it entirely as there would be an “inherent conflict” of interest for the firm’s counsel because the interest of the member (who is the counsel’s client) and the associated person rarely align. AdvisorLaw also suggested that the associated person’s consent may be compromised “in the likely

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<sup>258</sup> In response to the Notice 17-42, White stated that if the customer chooses to object to the expungement request, “it would be helpful if it was mandated that the customer participate in the hearing or file a substantive statement or brief opposing expungement.” Schlein stated that FINRA should consider requiring the associated person to “bear the cost of the customer’s attendance if the customer wishes to participate in person.” FINRA believes that these requirements would be unduly burdensome and, therefore, has determined not to propose them as requirements.

<sup>259</sup> See also The SEC Investor Advocate.

<sup>260</sup> See proposed Rules 12805(b) and 13805(b)(3).

scenario where the member firm is providing financial assistance for the legal representation, as the associated person may agree under financial duress.” NASAA supported codifying the practice, but noted that it would “require cooperation between firms and their associated persons” and that FINRA would have to develop “robust, mandated notification procedures.”<sup>261</sup>

FINRA notes that under the proposed rule change, filing an on-behalf-of request would be permissive, not mandatory. In addition, FINRA would require the party and the unnamed person to sign a form consenting to the on-behalf-of request to help ensure that the unnamed person is fully aware of the request and that the firm is agreeing to represent the unnamed person for the purpose of requesting expungement during the customer arbitration, regardless of how the arbitration closes.<sup>262</sup>

T. No Interventions by Associated Persons to Request Expungement

In Notice 17-42, FINRA proposed to foreclose the option of an unnamed person to intervene in a customer arbitration to request expungement. Keesal opposed this proposal, stating that intervention “often can be economical, given that the evidence on the merits (or lack thereof) of the customer’s complaint will be presented at the evidentiary hearing and that same evidence will provide the basis for expungement relief.”<sup>263</sup>

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<sup>261</sup> See NASAA (noting support for this change along with the proposal in the Notice 17-42 that would prevent an unnamed associated from filing an arbitration claim seeking expungement against an investor).

<sup>262</sup> See proposed Rules 12805(a)(2)(C)(ii) and 12805(a)(2)(D).

<sup>263</sup> See also Behr and JonesBell.

FINRA believes that where no party to the arbitration has filed a claim against the associated person or requested expungement on his or her behalf, the associated person's conduct is less likely to be addressed fully by the parties during the customer arbitration. In those circumstances, FINRA believes that the associated person should not be able to intervene in the customer arbitration, and that any expungement request should be decided separately by the Special Arbitrator Roster.<sup>264</sup>

U. Application of Expungement Framework to Customer Complaints

In Notice 17-42, FINRA proposed to allow an associated person to file an arbitration against a member firm for the sole purpose of seeking expungement of a customer complaint and have the request decided by the Special Arbitrator Roster. In response to Notice 17-42, NASAA stated that it objected to “expanding the scope of Rule 2080 to apply to all information related to [non-arbitrated] customer complaints.” NASAA stated that today, the expungement process is used to expunge customer complaints that are not the subject of arbitration, but believed that this practice was “beyond the scope originally intended with the rules” and that codification would “further embed a flawed process that does not afford regulators the ability to preserve information already considered to have regulatory value and provide investor protection.” The SEC Investor Advocate also indicated that it did not believe that “now is the time to expand the Rule 2080 expungement process to claims that do not result in arbitration,” and that it would “prefer to see the results of the new process before introducing an entirely new class of complaints to the mix.”

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<sup>264</sup> See proposed Rule 12805(a)(1)(E)(iii); see also supra Item 3.(a)II.A.3, “No Intervening in Customer Arbitrations to Request Expungement.”

FINRA notes that customer complaints have always been within the contemplated scope of FINRA Rule 2080. In proposing and adopting predecessor NASD Rule 2130, and in proposing to adopt FINRA Rule 2080 without material change, FINRA defined “customer dispute information” as including “customer complaints, arbitration claims, and court filings made by customers, and the arbitration awards or court judgments that may result from those claims or filings.”<sup>265</sup> The proposed amendments would continue to allow associated persons to file a claim in arbitration against a member firm for the sole purpose of seeking expungement of a customer complaint that is reported in the CRD system.

#### V. Other General Comments in Response to Notice 17-42

##### 1. Personal Experiences with the Expungement Process

Some commenters opposed the proposal as set forth in Notice 17-42 because of their experiences with what they considered to be meritless customer arbitration claims.<sup>266</sup> In addition, a number of commenters described their personal experiences with the customer complaint and expungement process or generally criticized the current process and the proposed rule change as unfair.<sup>267</sup> FINRA acknowledges and appreciates

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<sup>265</sup> See Notice to Members 04-16 (March 2004); Securities Exchange Act Release No. 47435 (March 4, 2003), 68 FR 11435 (March 10, 2003) (Notice of Filing and Amendment No. 1 of File No. SR-NASD-2002-168); Securities Exchange Act Release No. 59771 (April 15, 2009), 74 FR 18411 (April 22, 2009) (Notice of Filing and Amendment No. 1 of File No. SR-FINRA-2009-016).

<sup>266</sup> See Anzaldua, Barber, Braschi, Brookes, Burrill, Christ, Decker, Di Silvio, Gamblin, Glenn, Harmon, Harris, Higgenbotham, Isola, Joyce, Leven, Lindsey, Ram, Rosser, Scrydloff, Skafco, Slaughter, Stephens, Stewart, Tinklenberg, Walter, Weinerf and Zanolli.

<sup>267</sup> See e.g., Higgenbotham (describing CRD disclosures “related to funds offered by my employer [that] crashed during the 2007-2008 Financial Crisis”); see also

the commenters' concerns and has considered them in connection with the proposed rule change as a whole.

## 2. General Perspectives on the Proposed Rule Change

Some commenters also offered more general perspectives on the rule proposal as set forth in Notice 17-42. The SEC Investor Advocate, while generally supporting the proposed rule change, expressed a concern that the proposed amendments may cause brokers to seek to avoid the FINRA Rule 2080 process entirely, and instead request expungement directly in a court of competent jurisdiction. FINRA notes that today, a broker can seek expungement by going through the FINRA arbitration process or by going directly to court.<sup>268</sup>

SIFMA stated that FINRA already has in place a robust set of rules and expanded guidance to safeguard the expungement process, and that there did not appear to be any empirical justification for the additional regulations contained in the proposal, such as that expungements are too numerous or are being improperly granted.

PIABA stated that FINRA should only promulgate rules that facilitate removal of customer dispute information from the CRD system in the most extraordinary of circumstances. NASAA supported the proposal as an "important first step" that "add[ed] beneficial requirements and limitations related to the procedure of expungement."

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AdvisorLaw (providing a hyperlink to an online petition that requested signatures to "support a balanced, cost and time effective, expungement process," and collecting associated comments).

<sup>268</sup> See FINRA Rule 2080; see also supra note 11 (describing the requirement to name FINRA as a party when brokers seek expungement in court).

FINRA appreciates the commenters' differing perspectives. FINRA's review suggests that the percentage of expungement requests that are recommended is higher when the arbitrator or panel receives information only from the associated person or other party requesting expungement.<sup>269</sup> FINRA believes that the expungement process that would be established by the proposed rule change would help ensure that expungement is recommended in limited circumstances, while providing associated persons with a reasonable framework to seek expungement of information on their CRD records by establishing one or more of the grounds set forth in FINRA Rule 2080(b)(1).

### 3. Alternatives to the CRD Disclosure and Expungement Framework

Several commenters suggested alternatives to the current CRD disclosure and expungement framework.<sup>270</sup> For example, Mahoney stated that where an arbitration panel renders an award denying a customer's claims against an associated person, "the associated person should automatically have their CRD record expunged of all references to the complaint." Mahoney also stated that FINRA should not subject associated persons who are not named in a customer complaint, but were determined by member firms to have been involved in the sales practice violation(s), to disclosure and expungement standards that "create an unprecedented rebuttable presumption of liability."<sup>271</sup> In contrast, St. John's suggested that associated persons be prohibited from seeking expungement if there has been a finding of liability in the arbitration.

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<sup>269</sup> See supra Item 4.B., "Economic Baseline."

<sup>270</sup> See Barber, Baumgardner, Burrill, Butt, Chepucavage, Commonwealth, Harmon, Harris, Mahoney, Penzell, PIABA, Stewart, Tinklenberg and Wellington.

<sup>271</sup> See also FSI.

PIABA stated that although it supported the proposed rule change, expungement requests would be best handled separate from the arbitration and determined by FINRA itself rather than arbitrators. NASAA proposed further reform to the expungement process built around several principles including, for example, increased regulatory participation that allows for a regulatory determination regarding the merits of the expungement request.

FINRA appreciates the commenters' suggestions. As indicated by the proposed rule change, FINRA believes that revising the current expungement process as set forth in the proposed rule change, particularly the establishment of a panel of arbitrators randomly selected from the Special Arbitrator Roster to consider and decide straight-in requests, would best help achieve the goal that expungement should be recommended in limited circumstances. However, FINRA welcomes continued engagement to discuss further ways to enhance the expungement process.

#### 4. Other Comments

In response to Notice 17-42, Public Citizen stated that the explanation of expungement decisions that arbitrators write should be made public to ensure transparency. FINRA notes that arbitrators are required to provide a brief written explanation of the reasons for recommending expungement in the arbitration award.<sup>272</sup> The proposed rule change would retain this requirement, but would remove the word "brief" to indicate to the arbitrators that they must provide enough detail in the award to

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<sup>272</sup> See FINRA Rule 12805.

explain their rationale for recommending expungement.<sup>273</sup> As the Guidance suggests, the explanation must be complete and not solely a recitation of one of the FINRA Rule 2080 grounds or language provided in the expungement request.<sup>274</sup>

In addition, FINRA makes arbitration awards publicly available in the FINRA Arbitration Awards Online database (which provides arbitration awards rendered in FINRA's arbitration forum as well as other forums).<sup>275</sup> To provide information to the public, BrokerCheck links directly to the FINRA Arbitration Awards Online database. When a broker's BrokerCheck record includes a reportable arbitration award, the BrokerCheck record provides a hyperlink directly to the relevant document.

PIABA stated that removal of customer dispute information from the CRD system diminishes the ability of reputation to police business misconduct because of "FINRA's embrace of widespread pre-dispute arbitration agreements," and because records from FINRA proceedings are not available to the public on the same terms as public court proceedings. As discussed above, the proposed rule change is intended to help preserve in CRD information that is valuable to investors and regulators, while allowing associated persons a reasonable mechanism to remove information that is inaccurate.

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<sup>273</sup> See proposed Rules 12805(c)(8) and 13805(c)(8).

<sup>274</sup> See supra note 2.

<sup>275</sup> Arbitration Awards Online is available at <http://www.finra.org/arbitration-and-mediation/arbitration-awards>. This database enables users to perform Web-based searches for FINRA and historical NASD arbitration awards. Also available through the database are historical awards for the New York Stock Exchange, the American Stock Exchange, the Philadelphia Stock Exchange, the Chicago Board Options Exchange, the Pacific Exchange/ARCA and the Municipal Securities Rulemaking Board.

Keesal suggested that orders from other respected arbitration forums, such as the American Arbitration Association (“AAA”), should be afforded the same weight as arbitral findings from arbitrators in FINRA-administered arbitration, provided that (1) the arbitrators make written, factual findings as the basis for expungement under FINRA Rule 2080 and (2) the requirements of FINRA Rule 12805 are satisfied. FINRA appreciates the commenter’s suggestion and would consider how to treat arbitration awards recommending expungement in accordance with the proposed rule change from other recognized arbitration forums, such as AAA or JAMS, if the proposed rule change is approved by the Commission.

In addition, Keesal requested that FINRA provide guidance to associated persons and registration personnel regarding the meaning and effect of an expunged claim in the context of licensing and registration questionnaires. Although the impact on licensing and registration questionnaires is outside the scope of the proposed rule change, FINRA will consider whether additional guidance is appropriate.

**6. Extension of Time Period for Commission Action**

FINRA does not consent at this time to an extension of the time period for Commission action specified in Section 19(b)(2) of the Act.<sup>276</sup>

**7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2) or Section 19(b)(7)(D)**

Not applicable.

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<sup>276</sup> 15 U.S.C 78s(b)(2).

**8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission**

Not applicable.

**9. Security-Based Swap Submissions Filed Pursuant to Section 3C of the Act**

Not applicable.

**10. Advance Notices Filed Pursuant to Section 806(e) of the Payment, Clearing and Settlement Supervision Act**

Not applicable.

**11. Exhibits**

Exhibit 1. Completed notice of proposed rule change for publication in the Federal Register.

Exhibit 2a. Regulatory Notice 17-42 (December 2017).

Exhibit 2b. A list of comment letters received in response to Regulatory Notice 17-42 (December 2017).

Exhibit 2c. Copies of the comment letters received in response to Regulatory Notice 17-42 (December 2017).

Exhibit 2d. Form Requesting Expungement of Customer Dispute Information on Behalf of an Unnamed Person.

Exhibit 5. Text of the proposed rule change.

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION

(Release No. 34- ; File No. SR-FINRA-2020-030)

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Proposed Amendments to the Codes of Arbitration Procedure Relating to Requests to Expunge Customer Dispute Information, Including Creating a Special Arbitrator Roster to Decide Certain Expungement Requests

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on , the Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FINRA. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

FINRA is proposing to amend the Code of Arbitration Procedure for Customer Disputes (“Customer Code”) and the Code of Arbitration Procedure for Industry Disputes (“Industry Code”) (together, “Codes”) to modify the current process relating to the expungement of customer dispute information.

Specifically, the proposed rule change would amend the Codes to: (1) impose requirements on expungement requests (a) filed during an investment-related, customer initiated arbitration (“customer arbitration”) by an associated person, or by a party to the

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

customer arbitration on-behalf-of an associated person (“on-behalf-of request”), or (b) filed by an associated person separate from a customer arbitration (“straight-in request”); (2) establish a roster of arbitrators with enhanced training and experience from which a three-person panel would be randomly selected to decide straight-in requests; (3) establish procedural requirements for expungement hearings; and (4) codify and update the best practices of the Notice to Arbitrators and Parties on Expanded Expungement Guidance (“Guidance”) that arbitrators and parties must follow.<sup>3</sup> In addition, the proposed rule change would amend the Customer Code to specify procedures for requesting expungement of customer dispute information arising from simplified arbitrations. The proposed rule change would also amend the Codes to establish requirements for notifying state securities regulators and customers of expungement requests.

The text of the proposed rule change is available on FINRA’s website at <http://www.finra.org>, at the principal office of FINRA and at the Commission’s Public Reference Room.

II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, FINRA included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at

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<sup>3</sup> See Guidance, available at <https://www.finra.org/arbitration-and-mediation/notice-arbitrators-and-parties-expanded-expungement-guidance>.

the places specified in Item IV below. FINRA has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

(I) Background and Discussion

A. Customer Dispute Information in the Central Registration Depository

Information regarding customer disputes involving associated persons is maintained in the Central Registration Depository ("CRD<sup>®</sup>"), the central licensing and registration system used by the U.S. securities industry and its regulators.<sup>4</sup> FINRA operates the CRD system pursuant to policies developed jointly with NASAA. FINRA works with the SEC, NASAA and other members of the regulatory community to ensure that information submitted and maintained in the CRD system is accurate and complete.

In general, the information in the CRD system is submitted by registered securities firms, brokers and regulatory authorities in response to questions on the uniform registration forms.<sup>5</sup> These forms are used to collect registration information,

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<sup>4</sup> The concept for the CRD system was developed by FINRA jointly with the North American Securities Administrators Association ("NASAA"). The CRD system fulfills FINRA's statutory obligation to establish and maintain a system to collect and retain registration information. NASAA and state regulators play a critical role in the ongoing development and implementation of the CRD system.

<sup>5</sup> The uniform registration forms are Form BD (Uniform Application for Broker-Dealer Registration), Form BDW (Uniform Request for Broker-Dealer Withdrawal), Form BR (Uniform Branch Office Registration Form), Form U4 (Uniform Application for Securities Industry Registration or Transfer), Form U5

which includes, among other things, administrative, regulatory, criminal history, financial and other information about brokers, such as customer complaints, arbitration claims and court filings made by customers (i.e., “customer dispute information”). FINRA, state and other regulators use this information in connection with their licensing and regulatory activities, and member firms use this information to help them make informed employment decisions.

Pursuant to rules approved by the SEC, FINRA makes specific CRD information publicly available through BrokerCheck<sup>®</sup>.<sup>6</sup> BrokerCheck is part of FINRA's ongoing effort to help investors make informed choices about the brokers and broker-dealer firms with which they may conduct business. BrokerCheck maintains information on the approximately 3,600 registered broker-dealer firms and 624,000 registered brokers. BrokerCheck also provides the public with access to information about formerly registered broker-dealer firms and brokers.<sup>7</sup> In 2019 alone, BrokerCheck helped users conduct more than 40 million searches of firms and brokers.

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(Uniform Termination Notice for Securities Industry Registration) and Form U6 (Uniform Disciplinary Action Reporting Form).

<sup>6</sup> Section 15A of the Exchange Act requires FINRA to provide registration information to the public. BrokerCheck is one of the tools through which FINRA disseminates this information to the public. There is a limited amount of information in the CRD system that FINRA does not display through BrokerCheck, including personal or confidential information. A detailed description of the information made available through BrokerCheck is available at <http://www.finra.org/investors/about-brokercheck>.

<sup>7</sup> Formerly registered brokers, although no longer in the securities industry in a registered capacity, may work in other investment-related industries or may seek to attain other positions of trust with potential investors. BrokerCheck provides information on more than 17,000 formerly registered broker-dealer firms and nearly 567,000 formerly registered brokers. Broker records are available in BrokerCheck for 10 years after a broker leaves the industry, and brokers who are

The regulatory framework governing the CRD system and BrokerCheck has long contemplated the possibility of expunging certain customer dispute information from these systems in limited circumstances, such as where the allegations made about the broker are factually impossible or clearly erroneous. The expungement framework seeks to balance the competing interests of providing regulators broad access to information about customer disputes to fulfill their regulatory obligations, providing a fair process that recognizes a broker's interest in protecting their reputation and ensuring investors have access to accurate information about brokers.

B. FINRA Rules 2080, 12805 and 13805 Governing Expungement of Customer Dispute Information

A broker can seek expungement of customer dispute information by obtaining a court expungement order (1) by going through the FINRA arbitration process (and then obtaining a court order confirming an arbitration award containing expungement) or (2) by going directly to court (without first going to arbitration).

FINRA rules require arbitrators to perform fact-finding before recommending expungement of customer dispute information and to provide information about the basis for the expungement. Specifically, FINRA Rules 12805 and 13805 require arbitrators to hold a recorded hearing regarding the appropriateness of expungement of customer dispute information and to review settlement documents, the amount of payments made to any party and any other terms and conditions of the settlement.<sup>8</sup>

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the subject of disciplinary actions and certain other events remain on BrokerCheck permanently.

<sup>8</sup> In almost every proceeding, all or a majority of the arbitrators considering an expungement request are public arbitrators. Among other requirements, public arbitrators have never been employed by the securities industry; do not devote 20

In addition, these rules require arbitrators to indicate whether they have awarded expungement because: (1) the claim, allegation or information is factually impossible or clearly erroneous; (2) the associated person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation or conversion of funds; or (3) the claim, allegation or information is false.<sup>9</sup> The arbitrators are further required to provide a brief written explanation of the reasons for recommending expungement.<sup>10</sup> These requirements are supplemented with extensive guidance and training, including the Guidance, first published in 2013 and expanded further periodically thereafter.<sup>11</sup> The Guidance provides arbitrators with best practices and recommendations to follow, in addition to the requirements of FINRA Rules 12805 and 13805, when deciding expungement requests.

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percent or more of their professional work to the securities industry or to parties in disputes concerning investment accounts or transactions or employment relationships within the financial industry; and do not have immediate family members or co-workers who do so. See FINRA Rule 12100(aa).

<sup>9</sup> See FINRA Rules 2080, 12805 and 13805.

<sup>10</sup> Although FINRA Rules 12805 and 13805 state that the panel may “grant” expungement of customer dispute information under FINRA Rule 2080, the panel’s decision regarding an expungement request is not the final step in the process. A person seeking expungement must obtain a court order confirming an arbitration award for FINRA to expunge the customer dispute information from the CRD system. Accordingly, FINRA believes the word “recommend” more accurately describes the panel’s role in the expungement process. It has been FINRA’s longstanding practice to state in expungement awards that the arbitrators “recommend,” rather than “grant,” expungement. See also *infra* note 132, and accompanying text (stating that the proposed amendments to FINRA Rules 12805(c) and 13805(c) would also provide that the panel would “recommend” rather than “grant” expungement).

<sup>11</sup> See *supra* note 3.

Regardless of whether expungement of customer dispute information is sought directly through a court or in arbitration, FINRA Rule 2080, which was developed in close consultation with representatives of NASAA and state regulators, requires a broker-dealer firm or broker seeking expungement to obtain an order of a court of competent jurisdiction directing such expungement or confirming an award containing expungement. FINRA will expunge customer dispute information only after the court orders it to execute the expungement.<sup>12</sup>

### C. Concerns Regarding Expungement

Some stakeholders of the forum have raised concerns about expungement hearings held after the parties settle the customer arbitration that gave rise to the customer dispute information.<sup>13</sup> In many of these instances, the panel from the customer

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<sup>12</sup> FINRA Rule 2080 also requires that firms and brokers seeking a court order or confirmation of the arbitration award containing expungement name FINRA as a party, and provides that FINRA will challenge the request in court in appropriate circumstances. FINRA may, however, waive the requirement to name it as a party if a firm or broker requests a waiver and FINRA determines that the award containing expungement is based on affirmative judicial or arbitral findings that: (1) the claim, allegation or information is factually impossible or clearly erroneous; (2) the associated person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation or conversion of funds; or (3) the claim, allegation, or information is false. In addition, FINRA has sole discretion “under extraordinary circumstances” to waive the requirement that it be named in a court proceeding if it determines that the request for expungement and accompanying award are meritorious and expungement would not have a material adverse effect on investor protection, the integrity of the CRD system, or regulatory requirements. See FINRA Rule 2080(b).

<sup>13</sup> In its Final Report and Recommendations, the FINRA Dispute Resolution Task Force (“Task Force”) included a recommendation to create a special arbitration panel consisting of specially trained arbitrators to decide expungement requests in settled cases and in cases when a claimant did not name the associated person as a respondent in the case. See <http://www.finra.org/sites/default/files/Final-DR-task-force-report.pdf>; see also letter from Barbara Black, Professor of Law, University of Cincinnati College of Law (Retired), to Marcia Asquith, Office of the Corporate Secretary, FINRA, dated February 5, 2018 (“Black”) (discussing

arbitration has not heard the full merits of that case and, therefore, may not have any special insights in determining whether to recommend a request for expungement of customer dispute information. Further, customers and their representatives typically do not participate in an expungement hearing after the customer arbitration settles, especially if the expungement hearing occurs a number of years later.<sup>14</sup> In addition, a broker may file a straight-in request against a member firm for the sole purpose of requesting

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the Task Force’s recommendation) and letter from Joseph Borg, President, NASAA, to Marcia Asquith, Office of the Corporate Secretary, FINRA, dated February 5, 2018 (“NASAA”) (commenting that post-settlement expungement hearings often consist of one-sided presentations of the facts). These and other letters responding to Regulatory Notice 17-42 (December 2017) (“Notice 17-42”) are discussed in Item II.C. below.

<sup>14</sup> The Codes provide that no claim shall be eligible for submission to arbitration under the Codes where six years have elapsed from the occurrence or event giving rise to the claim. The panel resolves any questions regarding the eligibility of a claim under this rule. See FINRA Rules 12206(a) and 13206(a) (Time Limitation on Submission of Claims). This six-year eligibility rule applies to all arbitration claims, including those requesting expungement. Thus, if an associated person requests expungement of a CRD disclosure where six years have elapsed since the customer complaint, arbitration or civil litigation was initially reported, the arbitrator or panel should consider whether the claim is eligible for arbitration. In addition, FINRA Rules 12409 and 13413 (Jurisdiction of Panel and Authority to Interpret the Code) provide that the panel has the authority to interpret and determine the applicability of all provisions under the Codes. Such interpretations are final and binding upon the parties. Together, the rules grant arbitrators the authority to decide whether a claim is eligible for arbitration under the Codes. See Howsam v. Dean Witter Reynolds, 537 U.S. 79, 85-86 (2002) (finding that an arbitrator properly decides issues of eligibility).

Arbitrators should ensure that an expungement claim is eligible under the Codes and arbitrators may decide the eligibility issue on their own, rather than only in response to a party’s motion. See Horst v. FINRA, No. A-18-777960-C (Dist. Ct. Nevada Oct. 25, 2018) (Order Denying Motion to Vacate Arbitration Award) (ruling that an arbitrator may raise sua sponte the eligibility issue, not only when a party to the arbitration raises it in a motion).

expungement.<sup>15</sup> In most of these straight-in requests, the customer dispute information arises from a customer arbitration or customer complaint that was disclosed on the broker's CRD record a number of years prior to the request.<sup>16</sup> Thus, during these expungement hearings, the panel may receive information only from the associated person requesting expungement.

Further, FINRA is concerned that an increasing number of straight-in requests are being heard by a single arbitrator instead of a three-person panel.<sup>17</sup> FINRA believes that most expungement requests should be decided by a three-person panel. Expungement requests may be complex to resolve, particularly straight-in requests where customers

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<sup>15</sup> Currently, on rare occasions, straight-in requests are filed against a customer. As discussed below, the proposed amendments would prohibit these filings. See infra Item II.A.1.(II)A.2., "No Straight-in Requests Against Customers."

<sup>16</sup> Several questions on Forms U4 and U5 require associated persons to disclose certain investment-related, consumer-initiated (i) complaints and (ii) arbitrations and civil litigations, alleging sales practice violations. See Form U4, Question 14I, available at <https://www.finra.org/sites/default/files/form-u4.pdf> and Form U5, Question 7E, available at <https://www.finra.org/sites/default/files/form-u5.pdf>. These disclosures become part of the associated person's CRD record and are made available on BrokerCheck.

<sup>17</sup> An expungement request is a non-monetary or not specified claim. The Codes require that such claims are heard by a panel of three arbitrators, unless the parties agree in writing to one arbitrator. In addition, if a party requesting expungement adds a small monetary claim (of less than \$100,000) to the expungement request, the Codes require that such claims are heard by one arbitrator. See FINRA Rules 12401 and 13401. FINRA has amended the Codes to apply minimum fees to expungement requests, whether the request is made as part of the customer arbitration or the associated person files an expungement request in a separate arbitration. The amendments also apply a minimum process fee and member surcharge to straight-in requests, as well as a minimum hearing session fee to expungement-only hearings. See Securities Exchange Act Release No. 88945 (May 26, 2020), 85 FR 33212 (June 1, 2020) (Order Approving File No. SR-FINRA-2020-005). See also Regulatory Notice 20-25 (July 2020) (announcing a September 14, 2020 effective date) at <https://www.finra.org/rules-guidance/notices/20-25>.

typically do not participate in the expungement hearing. Thus, having three arbitrators available to ask questions, request evidence and to serve generally as fact-finders in the absence of customer input would help ensure that a complete factual record is created to support the arbitrators' decision in such expungement hearings.

In addition, FINRA is concerned that some associated persons are making second requests to expunge the same customer dispute information that they previously requested be expunged by a court or another arbitration panel. For example, an associated person may have a CRD disclosure that resulted from a customer's arbitration claim, but because the associated person is not named as a party to the customer arbitration ("unnamed person"),<sup>18</sup> the associated person is not able to request expungement in the customer arbitration.<sup>19</sup> When a firm asks, on-behalf-of the unnamed person, that the arbitrators recommend expungement, the unnamed person, as a non-party in the customer arbitration, may subsequently argue that he or she did not receive adequate notice of the expungement request or an opportunity to participate in the earlier

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<sup>18</sup> In 2009, the SEC approved amendments to Forms U4 and U5 to require, among other things, the reporting of allegations of sales practice violations made against unnamed persons. See Securities Exchange Act Release No. 59916 (May 13, 2009), 74 FR 23750 (May 20, 2009) (Order Approving File No. SR-FINRA-2009-008). Specifically, Forms U4 and U5 were amended to add questions to elicit whether the applicant or registered person, though not named as a respondent or defendant in a customer-initiated arbitration, was either mentioned in or could be reasonably identified from the body of the arbitration claim as a registered person who was involved in one or more of the alleged sales practice violations.

<sup>19</sup> If a broker is not named as a party in the customer arbitration, brokers may seek to expunge customer dispute information by: (1) asking a party to the arbitration, usually the firm, to request expungement on his or her behalf; (2) seeking to intervene in the customer arbitration; (3) initiating a new arbitration in which the unnamed person requests expungement and names the customer or firm as the respondent; or (4) going directly to court (without first going to arbitration).

proceeding. The unnamed person may then file a new claim to expunge the same disclosure that the firm requested on the unnamed person's behalf, despite the fact that the panel denied the expungement request in the prior matter.

FINRA believes that re-filing an expungement request that has been denied by an arbitration panel undermines the integrity of the arbitration process and the information in the CRD system. Arbitration awards are final and binding on the parties. If an associated person seeks to challenge an arbitration award, the associated person can do so by filing a motion to vacate in court.

In addition, some associated persons make second requests for expungement after withdrawing or deciding not to pursue an expungement request made in a customer arbitration, believing that another panel who has not heard the merits of the claim may be more likely to recommend expungement. FINRA is concerned about this practice of "arbitrator shopping," particularly when associated persons withdraw an original expungement request after the arbitration panel has been made aware of evidence that could result in the denial of the expungement request.

On December 6, 2017, FINRA published Notice 17-42<sup>20</sup> to seek comment on a variety of changes to the process of arbitrating expungement requests, including establishing a roster of arbitrators with additional training and specific backgrounds or experience from which a panel would be selected to decide an associated person's request for expungement of customer dispute information. The arbitrators from this roster would decide straight-in requests. As discussed below in Item II.C., FINRA received 70 comment letters on Notice 17-42 that reflected a variety of perspectives and different

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<sup>20</sup> See <http://www.finra.org/industry/notices/17-42>.

suggestions regarding how to proceed. The proposed rule change is responsive to concerns raised by commenters and would include the following primary changes:

➤ Expungement Requests in Customer Arbitrations

- An associated person named in a customer arbitration would be required to request expungement during the customer arbitration or forfeit the ability to request expungement of that same disclosure in any subsequent proceeding.
- A named party from a customer arbitration would be permitted to request expungement during the customer arbitration on-behalf-of an unnamed person pursuant to specified conditions and limitations.
- If a named associated person or party on-behalf-of an unnamed person requests expungement during the customer arbitration and the arbitration closes by award after a hearing,<sup>21</sup> the panel from the customer arbitration would be required to decide the expungement request during the customer arbitration and issue a decision on the request in the award.
- If a named associated person or party on-behalf-of an unnamed person requests expungement during the customer arbitration and the arbitration closes other than by award or by award without a hearing, an associated person may only pursue an expungement request by filing a straight-in request under the Industry Code against the member firm at which the associated person was associated at the time the dispute arose.

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<sup>21</sup> Under the Codes, a “hearing” means the hearing on the merits of the arbitration. See FINRA Rules 12100(o) and 13100(o).

➤ Expungement Requests under the Industry Code

- All straight-in requests<sup>22</sup> would be required to be filed under the Industry Code against the member firm at which the associated person was associated at the time the dispute arose and decided by a panel selected from a roster of arbitrators with enhanced experience and training (“Special Arbitrator Roster”).
- If an associated person withdraws a straight-in request after a panel from the Special Arbitrator Roster is appointed, the case would be closed with prejudice.

➤ Special Arbitrator Roster

- A three-person panel selected from the Special Arbitrator Roster would decide straight-in requests.
- The parties would not be permitted to agree to fewer than three arbitrators from the Special Arbitrator Roster to decide straight-in requests.
- Arbitrators on the Special Arbitrator Roster would be required to be public arbitrators who are eligible for the chairperson roster and who have fully met the following additional qualifications: (1) evidenced successful

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<sup>22</sup> A straight-in request would include a request to expunge customer dispute information filed under the Industry Code: (1) by an associated person named in a customer arbitration after the customer arbitration closes other than by award or by award without a hearing; (2) arising from a customer complaint or civil litigation rather than a customer arbitration; or (3) by an associated person who was the subject of a customer arbitration, but unnamed, and where a named party in the customer arbitration did not request expungement on-behalf-of the unnamed associated person, or where a named party made an on-behalf-of request, but the customer arbitration closed other than by award or by award without a hearing.

completion of, and agreement with, enhanced expungement training provided by FINRA; and (2) service as an arbitrator through award on at least four customer-initiated arbitrations administered by FINRA or by another self-regulatory organization (“SRO”) in which a hearing was held.

- The Neutral List Selection System (“NLSS”) would randomly select the three public chairpersons from the Special Arbitrator Roster to decide straight-in requests. The first arbitrator selected would be the chair of the panel. The parties would not be permitted to stipulate to the use of pre-selected arbitrators.
  - An associated person who files a straight-in request would not be permitted to strike any arbitrators selected by NLSS or stipulate to the arbitrator’s removal, but would be permitted to challenge any arbitrator selected for cause. If an arbitrator is removed, NLSS would randomly select a replacement.
- Time Limitations on Requests for Expungement
- For customer dispute information reported to the CRD system after the effective date of the proposed rule change, the proposal would provide that an associated person would be barred from requesting expungement if: (1) more than two years have elapsed since the close of the customer arbitration or civil litigation that gave rise to the customer dispute information; or (2) there was no customer arbitration or civil litigation involving the customer dispute information, and more than six years have

elapsed since the date that the customer complaint was initially reported to the CRD system.

- For customer dispute information reported to the CRD system before the effective date of the proposed rule change, the proposal would require an associated person to request expungement as a straight-in request under the Industry Code: (1) within two years of the effective date of the proposed rule change for disclosures that arose from a customer arbitration or civil litigation that closed on or prior to the effective date; and (2) within six years of the effective date of the proposed rule change for customer complaints initially reported to the CRD system on or prior to the effective date.

➤ Expungement Requests During a Simplified Arbitration

- If a party requests expungement during a simplified arbitration, the single arbitrator in the simplified arbitration would be required to decide the expungement request, regardless of how the simplified arbitration case closes (e.g., even if the case settles).
- If an associated person does not request expungement during the simplified arbitration, the request may be filed as a straight-in request under the Industry Code against the member firm at which the associated person was associated at the time the dispute arose, and be decided by a three-person panel randomly selected from the Special Arbitrator Roster.

➤ Expungement Hearings

- Establish procedural requirements that arbitrators and parties must follow for expungement hearings.

➤ State and Customer Notifications

- Establish requirements for notifying state securities regulators and customers of expungement requests.

Under the proposed rule change, an associated person would only be permitted to seek expungement of customer dispute information in the arbitration forum administered by FINRA by complying with the requirements of proposed Rules 12805 (expungement requests in a customer arbitration), 13805 (straight-in requests under the Industry Code) or 12800(d) (expungement requests in a simplified customer arbitration).

The proposed rule change, as revised in response to comments on Notice 17-42, is set forth in further detail below.<sup>23</sup>

(II) Proposed Rule Change

The discussion below of the proposed rule change is divided into six areas: (A) requests for expungement under the Customer Code; (B) straight-in requests under the Industry Code and the Special Arbitrator Roster; (C) limitations on expungement requests; (D) procedural requirements related to all expungement hearings; (E) notifications to customers and states regarding expungement requests; and (F) expungement requests during simplified customer arbitrations.

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<sup>23</sup> The proposed rule change would apply to all members, including members that are funding portals or have elected to be treated as capital acquisition brokers (“CABs”), given that the funding portal and CAB rule sets incorporate the impacted FINRA rules by reference.

A. Requests for Expungement under the Customer Code

FINRA Rule 12805 provides a list of requirements that arbitrators must meet before they may recommend expungement.<sup>24</sup> The rule does not, however, provide guidance for associated persons on how and when they may request expungement during the customer arbitration, or on when arbitrators must make expungement determinations. The proposed rule change would amend FINRA Rule 12805 to set forth requirements for expungement requests filed by an associated person during a customer arbitration.

1. Expungement Requests During the Customer Arbitration

a. By a Respondent Named in a Customer Arbitration

Under current practice, an associated person who is named as a respondent in a customer arbitration (“named associated person”) may request expungement at any time during the customer arbitration or separately from the customer arbitration in a straight-in request.<sup>25</sup> If a named associated person requests expungement during the customer

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<sup>24</sup> FINRA Rule 12805 provides that a panel must comply with the following criteria before recommending expungement: (1) hold a recorded hearing to decide the issue of expungement; (2) review settlement documents, and consider the amount of payments made to any party and any other terms and conditions of the settlement; (3) indicate in the award which of the grounds in FINRA Rule 2080 is the basis for expungement and provide a brief written explanation of the reasons for recommending expungement; and (4) assess all forum fees for hearing sessions in which the sole topic is the determination of the appropriateness of expungement against the parties requesting expungement. See also FINRA Rule 13805.

<sup>25</sup> There are several ways in which a named associated person may request expungement during a customer arbitration. The request may be included in the answer to the statement of claim that must be submitted within 45 days of receipt of the statement of claim, and may include other claims and remedies requested. See FINRA Rules 12303(a) and (b); see also FINRA Rules 13303(a) and (b). The expungement request may also be included in other pleadings (e.g., a counterclaim, a cross claim, or a third party claim) and must be filed with the Director of the Office of Dispute Resolution (“Director”) through the Party Portal. See FINRA Rules 12100(x) and 12300(b). The associated person may also

arbitration, does not withdraw the request and the case goes to hearing and closes by award, the panel in the customer arbitration will also decide the expungement request and include the decision as part of the customer's award.<sup>26</sup> If the customer arbitration does not close by award after a hearing (e.g., settles), and the associated person continues to pursue the expungement request, the panel from the customer arbitration may hold an expungement-only hearing as required by FINRA Rule 12805 to decide the expungement request.

Under the proposed rule change, if a named associated person seeks to request expungement of customer dispute information arising from the customer's statement of claim, the named associated person must make the expungement request during the customer arbitration.<sup>27</sup> As discussed below, the request would be subject to limitations on how and when the request may be made.<sup>28</sup> In addition, the Director would be authorized to deny the forum to expungement requests during a customer arbitration that

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request at any time during the case (outside of a pleading) that the panel consider the person's expungement request during the hearing. Under FINRA Rule 12503, such a request is treated like a motion, which gives the other parties an opportunity to object. If there is an objection, the panel must decide the motion pursuant to FINRA Rule 12503(d)(5). See also FINRA Rules 13503 and 13503(d)(5).

<sup>26</sup> Under the Codes, a customer's or claimant's damage request determines whether a single arbitrator or a three-person panel will consider and decide an arbitration case. See FINRA Rules 12401 and 13401. For ease of reference, when discussing expungement requests during customer arbitrations under proposed Rule 12805, unless otherwise specified, the rule filing uses the term "panel" to mean either a panel or single arbitrator.

<sup>27</sup> See proposed Rule 12805(a)(1)(A).

<sup>28</sup> See also infra Item II.A.1.(II)C., "Limitations on Expungement Requests."

do not arise out of the customer arbitration.<sup>29</sup> If the associated person does not request expungement during the customer arbitration, he or she would forfeit the opportunity to seek expungement of the same customer dispute information in any subsequent proceeding.<sup>30</sup>

FINRA is proposing to require that a named associated person request expungement during the customer arbitration because, if the arbitration closes by award after a hearing, the panel from the customer arbitration will be best situated to decide the related issue of expungement. Requiring the named associated person to request expungement in the customer arbitration increases the likelihood that a panel will have input from all parties and access to all of the evidence, testimony and other documents to make an informed decision on the expungement request.

FINRA recognizes that this requirement could result in some named associated persons filing expungement requests to preserve their right to make a request, regardless of the potential outcome. FINRA believes that the potential costs that would be incurred by associated persons, arbitrators and the forum if named associated persons file expungement requests to preserve the ability to request expungement are appropriate given the potential benefit of having customer input and a complete factual record for the panel to decide an expungement request. In addition, certain aspects of the proposed rule change may limit the filing of requests without regard to the potential outcome. For example, under the proposed rule change, named associated persons would be permitted

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<sup>29</sup> See proposed Rules 12203(b) and 12805(a).

<sup>30</sup> See proposed Rule 12805(a).

to request expungement no later than 30 days before the first scheduled hearing.<sup>31</sup> This proposed amendment would provide the named associated person with a reasonable amount of time to consider, likely after receiving any discovery from the claimant, whether to file the request because it could meet one or more of the FINRA Rule 2080(b)(1) grounds for expungement.<sup>32</sup>

i. Method of Requesting Expungement

The proposed rule change would limit how and when expungement requests may be made during the customer arbitration. Under the proposed rule change, if a named associated person requests expungement during the customer arbitration, the request must be included in the answer or a pleading requesting expungement.<sup>33</sup> If the request is included in the answer, it must be filed within 45 days of receipt of the customer's statement of claim in accordance with existing requirements under the Codes.<sup>34</sup> If the named associated person requests expungement in a pleading requesting expungement, the request must be filed no later than 30 days before the first scheduled hearing begins.<sup>35</sup>

FINRA believes the proposed rule change would provide a reasonable amount of time for the requesting party to make an informed decision about whether to request

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<sup>31</sup> See proposed Rule 12805(a)(1)(C); see also infra Item II.A.1.(II)A.1.a.i., "Method of Requesting Expungement."

<sup>32</sup> In addition, FINRA notes that the SEC has approved changes to FINRA rules to apply minimum fees to expungement requests. See supra note 17.

<sup>33</sup> See proposed Rule 12805(a)(1)(C)(i).

<sup>34</sup> See supra note 25.

<sup>35</sup> See proposed Rule 12805(a)(1)(C)(i).

expungement while also providing the parties with reasonable case-preparation time, since the expungement issues will overlap with the issues raised by the customer's claim.

In addition, the proposed filing deadline would provide the Director a reasonable amount of time to notify state securities regulators of the expungement request.<sup>36</sup> If a named associated person seeks to request expungement after the 30-day filing deadline, the panel would be required to decide whether to grant an extension and permit the request or whether to deny the request for expungement.<sup>37</sup>

ii. Required Contents of an Expungement Request

Under the proposed rule change, a request for expungement by a named associated person in a customer arbitration must include the applicable filing fee under the Codes.<sup>38</sup> In addition, a named associated person would be required to provide the CRD number of the party requesting expungement, each CRD occurrence number that is the subject of the request and the case name and docket number that gave rise to the disclosure, if applicable.<sup>39</sup>

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<sup>36</sup> See proposed Rule 12805(b); see also infra Item II.A.1.(II)E.3., "State Notification of Expungement Requests."

<sup>37</sup> See proposed Rule 12805(a)(1)(C). The proposed amendments would provide that if the expungement request is not filed in a pleading no later than 30 days before the first scheduled hearing, then FINRA Rule 12309(b) would require the associated person to file a motion pursuant to FINRA Rule 12503, seeking an extension of the 30-day deadline to file the expungement request.

<sup>38</sup> See proposed Rule 12805(a)(1)(C)(ii)a.; see also supra note 17.

<sup>39</sup> See proposed Rule 12805(a)(1)(C)(ii)b.-d. An occurrence is a disclosure event that is reported to the CRD system via one or more Disclosure Reporting Pages. Each occurrence contains details regarding a specific disclosure event. An occurrence can have as many as three sources reporting the same event: Forms U4, U5 and U6.

The proposed rule change would also require the party requesting expungement to explain whether expungement of the same customer dispute information was (i) previously requested and, if so (ii) how it was decided.<sup>40</sup> This requirement would assist with implementation of the proposed prohibition on parties making second requests for expungement, discussed in more detail below.<sup>41</sup> This proposed requirement is also consistent with language in the existing Guidance stating that arbitrators should ask a party requesting expungement whether an arbitration panel or a court previously denied expungement of the customer dispute information at issue and, if there was a prior denial, to deny the expungement request.<sup>42</sup>

Under the proposed rule change, if an expungement request fails to include any of the proposed requirements for requesting expungement, the request would be considered deficient and would not be served unless the deficiency is corrected.<sup>43</sup> These requirements would help ensure that FINRA, the panel and the parties understand who is requesting expungement and which disclosure is the subject of the request. Further, if the disclosure arose from a customer arbitration, the case name and docket number would provide the panel that is considering the expungement request with information about the dispute that gave rise to the disclosure that the party is seeking to expunge.

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<sup>40</sup> See proposed Rule 12805(a)(1)(C)(ii)e.

<sup>41</sup> See infra Item II.A.1.(II)A.1.b.i., “Method of Requesting Expungement On-Behalf-Of an Unnamed Person.”

<sup>42</sup> See supra note 3.

<sup>43</sup> See proposed Rule 12307(a)(8)-(11) (setting forth reasons a claim may be deficient).

FINRA believes these proposed requirements for parties requesting expungement are necessary for the timely and orderly consideration of expungement requests as well as to maintain the integrity of the data in the CRD system.

b. Expungement Requests by a Party Named in the Customer  
Arbitration On-Behalf-Of an Unnamed Person

The Codes do not specifically address expungement requests by a party named in a customer arbitration on-behalf-of an unnamed person.<sup>44</sup> Under current practice, a party to a customer arbitration may file an on-behalf-of request for expungement during the customer arbitration. If the party (typically, a firm) files the request and the customer arbitration closes by award after a hearing, the panel will decide the expungement request and include the decision in the award. If the customer arbitration does not close by award after a hearing (e.g., settles), either the requesting party or the unnamed person could ask the panel to consider and decide the expungement request before it disbands. In this circumstance, the panel from the customer arbitration will hold a separate expungement-only hearing to decide the expungement request.

The proposed rule change would codify the ability of a party in the customer arbitration to file an on-behalf-of request during a customer arbitration.<sup>45</sup> Under the proposed rule change, a party to a customer arbitration may file an on-behalf-of request

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<sup>44</sup> The proposed rule change would define an unnamed person as “an associated person, including a formerly associated person, who is identified in a Form U4, Form U5, or Form U6, as having been the subject of an investment-related, customer-initiated arbitration claim that alleged that the associated person or formerly associated person was involved in one or more sales practice violations, but who was not named as a respondent in the arbitration claim.” See proposed Rule 12100(ff).

<sup>45</sup> See proposed Rule 12805(a)(2).

that seeks to expunge customer dispute information arising from the customer's statement of claim, provided the request is eligible for arbitration under proposed Rule 12805.<sup>46</sup> Filing an on-behalf-of request would be permissive, not mandatory.<sup>47</sup> However, as discussed below, if the named party and the unnamed person agree to such a request, FINRA would require them to sign a form consenting to the on-behalf-of request which would help ensure that the unnamed person is fully aware of the request and that the firm is agreeing to represent the unnamed person for the purpose of requesting expungement during the customer arbitration.<sup>48</sup>

i. Method of Requesting Expungement On-Behalf-Of an  
Unnamed Person

The unnamed person would be required to consent to the on-behalf-of request in writing.<sup>49</sup> In particular, the party filing an on-behalf-of request would be required to submit a signed Form Requesting Expungement on Behalf of an Unnamed Person

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<sup>46</sup> See proposed Rule 12805(a)(2)(B).

<sup>47</sup> See proposed Rule 12805(a)(2)(A).

<sup>48</sup> A customer complaint can be reported to the CRD system via a Form U4 or Form U5. Pursuant to FINRA Rule 1010, an associated person should be made aware of the filing of a Form U4 and any amendments thereto by the associated person's member firm. In addition, Article V, Section 3 of the FINRA By-Laws of the Corporation requires that a member firm provide an associated person a copy of an amended Form U5, including one reporting a customer complaint involving the associated person. FINRA also provides several methods for associated persons and former associated persons to check their records (e.g., by requesting an Individual CRD Snapshot or online through BrokerCheck).

<sup>49</sup> See proposed Rule 12805(a)(2)(A).

(“Form”) and a statement requesting expungement with the Director.<sup>50</sup> The proposed rule change would not require that an on-behalf-of request be included in an answer or pleading requesting expungement (although it could be), since the request seeks relief on-behalf-of a person who is not a party to the arbitration. However, the party making the request would be required to serve the request, which would include the Form, on all parties no later than 30 days before the first scheduled hearing.<sup>51</sup>

FINRA believes that requiring submission of the Form would help address the issue of an unnamed person not being notified of the on-behalf-of request. As discussed above, FINRA is concerned that some associated persons are filing arbitration claims seeking expungement of the same customer dispute information that was the subject of a previous denial by a panel of an on-behalf-of request. By signing the Form, the unnamed person would be consenting to the on-behalf-of request and agreeing to be bound by the panel’s decision on the request.<sup>52</sup> In addition, the Form would provide that, if the customer arbitration closes by award after a hearing, the unnamed person would be barred from filing a request for expungement for the same customer dispute information

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<sup>50</sup> See proposed Rule 12805(a)(2)(C)(ii). The unnamed person whose CRD record would be expunged and the party requesting expungement on the unnamed person’s behalf must sign the Form.

<sup>51</sup> See proposed Rule 12805(a)(2)(C)(iii). The 30-day deadline is the same as the proposed deadline for a named associated person to request expungement in a customer arbitration.

<sup>52</sup> By signing the Form, the unnamed person would also be agreeing to maintain the confidentiality of documents and information from the customer arbitration to which the unnamed person is given access and to adhere to any confidentiality agreements or orders associated with the customer arbitration. See proposed Rule 12805(a)(2)(D). Failure of the unnamed person to comply with this provision could subject the unnamed person to a claim for damages by an aggrieved party.

in a subsequent proceeding, and the unnamed person's signature would serve as acknowledgement of this consequence.

ii. Required Contents of an On-Behalf-Of Expungement Request

Under the proposed rule change, an on-behalf-of request would be required to include the same elements as a request for expungement by a named associated person during a customer arbitration.<sup>53</sup> Thus, the party requesting expungement on-behalf-of an unnamed person (typically, the firm) would be required to provide the applicable filing fee, the CRD number of the unnamed person, each CRD occurrence number that is the subject of the request and the case name and docket number that gave rise to the disclosure, if applicable. In addition, as discussed above, the party requesting expungement would be required to include the Form, signed by the unnamed person whose CRD record would be expunged and the party filing the request.

c. Deciding Expungement Requests during Customer Arbitrations

The proposed amendments would require that if there is a request for expungement by a named associated person or on-behalf-of an unnamed person during a customer arbitration, the panel from the customer arbitration must decide the expungement request if the customer arbitration closes by award after a hearing.<sup>54</sup> If the customer arbitration closes other than by award (e.g., settles) or by award without a

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<sup>53</sup> See proposed Rule 12805(a)(1)(C)(ii); see also supra Item II.A.1.(II)A.1.a.ii., "Required Contents of an Expungement Request."

<sup>54</sup> See proposed Rule 12805(a)(1)(D)(i) and (a)(2)(E)(i).

hearing, the panel would not consider the expungement request.<sup>55</sup> Instead, the associated person would have the option of filing a request to expunge the same customer dispute information as a new claim under proposed Rule 13805 against the member firm at which he or she was associated at the time the customer dispute arose.<sup>56</sup> A panel from the Special Arbitrator Roster would decide such an expungement request, as discussed in more detail below.<sup>57</sup>

i. Panel Decides the Expungement Request if the Customer's Claim Closes by Award after a Hearing

Currently, if a named associated person requests expungement, or a party files an on-behalf-of request, and the customer's claim closes by award after a hearing, the panel may consider and decide the expungement request during the customer arbitration and issue its decision in the award. If, however, the party requesting expungement does not raise the issue of expungement during the hearing, the panel will not decide the request and may deem it withdrawn without prejudice.<sup>58</sup> In this instance, the associated person has the option to file the request again at a later date.

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<sup>55</sup> See proposed Rules 12805(a)(1)(D)(ii) and (a)(2)(E)(ii).

<sup>56</sup> See supra note 54. Under the Codes, a "member" includes any broker or dealer admitted to membership in FINRA, whether or not the membership has been terminated, suspended, cancelled, revoked, the member has been expelled or barred from FINRA or the member is otherwise defunct. See FINRA Rules 12100(s) and 13100(q); see also Securities Exchange Act Release No. 88254 (February 20, 2020), 85 FR 11157 (February 26, 2020) (Order Approving File No. SR-FINRA-2019-027).

<sup>57</sup> See infra Item II.A.1.(II)B.2., "Panel from the Special Arbitrator Roster Decides Requests Filed Under the Industry Code."

<sup>58</sup> See FINRA Rules 12702 and 13702.

Under the proposed rule change, if, during the customer arbitration, a named associated person requests expungement or a party files an on-behalf-of request, and the customer's claim closes by award after a hearing, the panel in the customer arbitration would be required to consider and decide the request for expungement during the customer arbitration and issue a decision on the expungement request in the award.<sup>59</sup>

The panel would be required to decide the request even if the requesting party withdraws the request or fails to present a case in support of the request. In this instance, the panel must deny the expungement request with prejudice.<sup>60</sup> This requirement would foreclose the ability of associated persons to withdraw expungement requests to avoid having their requests decided by the panel who heard the evidence on the customer's arbitration claim, and then seeking to re-file the request and receive a new list of arbitrators and a potentially more favorable decision.

ii. Panel Does Not Decide Expungement if the Customer's Claim Closes Other than by Award or by Award without a Hearing

Currently, if a named associated person requests expungement or a party files an on-behalf-of request and the customer arbitration does not close by award after a hearing (e.g., settles) and the associated person or requesting party, if it is an on-behalf-of request, continues to pursue the expungement request, the panel from the customer

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<sup>59</sup> See proposed Rules 12805(a)(1)(D)(i) and 12805(a)(2)(E)(i).

<sup>60</sup> See proposed Rules 12805(a)(1)(D)(i) and 12805(a)(2)(E)(i). A party requesting expungement on-behalf-of an unnamed person may withdraw or not pursue an expungement request only with the written consent of the unnamed person. Under such circumstances, the panel would deny the expungement request with prejudice. See proposed Rule 12805(a)(2)(E)(i).

arbitration will hold a separate expungement-only hearing to consider and decide the expungement request. If the named associated person or party requesting expungement does not request that the panel hold a separate, expungement-only hearing, the panel may deem the request withdrawn without prejudice, and the associated person has the option to file the request again at a later date.

The proposed rule change would provide that if, during a customer arbitration, a named associated person requests expungement or a party files an on-behalf-of request and the customer arbitration closes other than by award or by award without a hearing, the panel from the customer arbitration would not be permitted to decide the expungement request.<sup>61</sup> Instead, the associated person would be required to seek expungement by filing a request to expunge the same customer dispute information as a straight-in request under proposed Rule 13805, where a panel from the Special Arbitrator Roster would decide the request.<sup>62</sup>

As discussed above, expungement requests may be complex to resolve, particularly straight-in requests where customers typically do not participate in the expungement hearing. Thus, having three arbitrators available to ask questions, request evidence and to serve generally as fact-finders in the absence of customer input would help ensure that a complete factual record is created to support the arbitrators' decision in such expungement hearings.

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<sup>61</sup> See proposed Rules 12805(a)(1)(D)(ii)a. and 12805(a)(2)(E)(ii)a.

<sup>62</sup> See infra Item II.A.1.(II)B.2., “Panel from the Special Arbitrator Roster Decides Requests Filed Under the Industry Code.”

FINRA believes this is the right approach because the panel selected by the parties in the customer arbitration has not heard the full merits of the case and, therefore, may not bring to bear any special insights in determining whether to recommend expungement. In addition, customers or their representative have little incentive to participate in an expungement hearing once their case has settled. Requiring that an associated person file the expungement request as a straight-in request under the Industry Code to be heard and decided by a three-person panel selected from the Special Arbitrator Roster would strengthen the expungement framework. As discussed in more detail below, this corps of specially trained arbitrators would follow the procedures set forth in proposed Rule 13805 and make a decision about whether FINRA Rule 2080(b)(1) grounds exist to recommend expungement, keeping in mind the importance of maintaining the integrity of information in the CRD system.

## 2. No Straight-in Requests Against Customers

The proposed amendments would prohibit an associated person from filing a straight-in request against a customer.<sup>63</sup> Currently, straight-in requests are rarely filed against a customer.<sup>64</sup> FINRA does not believe that customers should be compelled to participate in a separate proceeding to decide an expungement request after the customer has resolved his or her arbitration claim or civil litigation, or submitted his or her

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<sup>63</sup> See proposed Rules 12805(a)(1)(D)(ii)c. and 12805(a)(2)(E)(ii)c.

<sup>64</sup> From January 2016 through June 2019, FINRA is able to identify 5,718 requests to expunge customer dispute information. Of those, 3,114 were filed as straight-in requests; 66 of the straight-in requests were filed solely against a customer. See infra Item II.B.2., “Economic Baseline.”

customer complaint. Accordingly, the proposed amendments would prohibit an associated person from filing a straight-in request against a customer.

### 3. No Intervening in Customer Arbitrations to Request Expungement

The proposed amendments would also prohibit unnamed persons from intervening in a customer arbitration and requesting expungement.<sup>65</sup> If the associated person is neither a party to the arbitration nor the subject of an on-behalf-of request by another party to the arbitration, the associated person should not be able to intervene in the customers' arbitration to request expungement. In these circumstances, the associated person's conduct is unlikely to be fully addressed by the parties during the customer arbitration, and FINRA does not believe that the customer should have the presentation of their case interrupted by an associated person's intervention to request expungement. In addition, there have been instances in customer arbitrations in which the unnamed person learns that the customer's arbitration case is nearing conclusion. The associated person (or his or her representative) then files a motion to intervene in the case to ask the panel to consider recommending expungement. As an unnamed person, the individual is not a party to the case and, therefore, has not made any arguments in support of the expungement request. Further, if the motion is granted, the parties to the case will be required to wait for a decision on the expungement request (which may necessitate another hearing) before their dispute is resolved, causing delay and additional cost to the parties.

Accordingly, under the proposed rule change, associated persons would be prohibited from intervening in a customer arbitration and requesting expungement.

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<sup>65</sup> See proposed Rule 12805(a)(2)(E)(iii).

Instead, the unnamed person would have the option to file the request as a new claim under proposed Rule 13805, where a panel from the Special Arbitrator Roster would decide the request.<sup>66</sup>

B. Straight-in Requests and the Special Arbitrator Roster

Under the proposed rule change, all requests to expunge disclosures arising from customer complaints or civil litigations would be required to be made as straight-in requests under proposed Rule 13805.<sup>67</sup> In addition, an associated person could request expungement of customer dispute information arising from a customer arbitration under proposed Rule 13805 if: (1) the associated person is named in the arbitration or is the subject of an on-behalf-of request and the customer arbitration closes other than by award or by award without a hearing; or (2) the associated person is the subject of a customer arbitration, but is neither named in the arbitration nor the subject of an on-behalf-of request, and the customer arbitration closes for any reason. If an associated person requests expungement under proposed Rule 13805, a three-person panel selected from the Special Arbitrator Roster in accordance with proposed Rule 13806, would decide the expungement request.<sup>68</sup>

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<sup>66</sup> See infra Item II.A.1.(II)B.2., “Panel from the Special Arbitrator Roster Decides Requests Filed Under the Industry Code.”

<sup>67</sup> See proposed Rule 13805(a)(1).

<sup>68</sup> See infra Item II.A.1.(II)B.2.a. and b. (discussing eligibility requirements for and composition of the Special Arbitrator Roster).

1. Filing a Straight-in Request Under the Industry Code

a. Applicability

Under the proposed rule change, an associated person requesting expungement of customer dispute information under the Industry Code must make a straight-in request by filing a statement of claim in accordance with FINRA Rule 13302 against a member firm at which he or she was associated at the time the customer dispute arose, unless the request is ineligible for arbitration under proposed Rule 13805(a)(2).<sup>69</sup> Thus, the only way to request expungement of customer dispute information under the Industry Code would be to file the request under proposed Rule 13805.

The requirement that the associated person file the straight-in request against the member firm at which he or she was associated at the time the customer dispute arose would help ensure that there is a connection between the respondent firm and the subject of the expungement request. For example, the firm at which the person requesting expungement was associated at the time the dispute arose should have knowledge of the dispute and access to documents or other evidence relating to the dispute. In addition, the proposed requirement would help ensure that the panel from the Special Arbitrator Roster would be able to request evidence from a member firm with information that is relevant to the expungement request. If the requisite connection is not present, the Director would be authorized to deny the forum to the request.<sup>70</sup>

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<sup>69</sup> See proposed Rule 13805(a)(1). FINRA Rule 13302 provides, in relevant part, that to initiate an arbitration, a claimant must file with the Director a signed and dated Submission Agreement, and a statement of claim specifying the relevant facts and remedies requested through the Party Portal.

<sup>70</sup> See proposed Rule 13203(b).

b. Required Contents of Straight-in Requests

The required contents of a straight-in request would be the same as those required for expungement requests filed under proposed Rule 12805.<sup>71</sup> Thus, the associated person's straight-in request would be required to contain the applicable filing fee;<sup>72</sup> the CRD number of the party requesting expungement; each CRD occurrence number that is the subject of the request; the case name and docket number that gave rise to the disclosure, if applicable; and an explanation of whether expungement of the same customer dispute information was previously requested and, if so, how it was decided.<sup>73</sup> In addition, as discussed below, the proposed rule change would impose limitations on when such requests may be made.<sup>74</sup>

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<sup>71</sup> See supra Item II.A.1.(II)A.1.a.ii., "Required Contents of an Expungement Request."

<sup>72</sup> FINRA would not assess a second filing fee when an associated person files a straight-in request if the associated person or the requesting party in the case of an on-behalf-of request, had previously paid the filing fee to request expungement of the same customer dispute information during a customer arbitration.

<sup>73</sup> See proposed Rule 13805(a)(3).

<sup>74</sup> See infra Item II.A.1.(II)C., "Limitations on Expungement Requests." As discussed in more detail below in Item II.A.1.(II)C., the straight-in request would be ineligible for arbitration under the Industry Code if: (1) a panel held a hearing to consider the merits of the associated person's request for expungement of the same customer dispute information; (2) a court previously denied the associated person's request to expunge the same customer dispute information; (3) the customer arbitration, civil litigation or customer complaint that gave rise to the customer dispute information is not concluded; (4) more than two years has elapsed since the customer arbitration or civil litigation that gave rise to the customer dispute information has closed; or (5) there was no customer arbitration or civil litigation that gave rise to the customer dispute information and more than six years has elapsed since the date that the customer complaint was initially reported to the CRD system. See proposed Rule 13805(a)(2).

2. Panel from the Special Arbitrator Roster Decides Requests Filed Under the Industry Code

If a straight-in request is filed in accordance with proposed Rule 13805, a three-person panel selected from the Special Arbitrator Roster pursuant to proposed Rule 13806 would be required to hold an expungement hearing, decide the expungement request and issue an award.<sup>75</sup> The proposed amendments would also provide that if the associated person withdraws or does not pursue the request, the panel would be required to deny the expungement request with prejudice.<sup>76</sup> This requirement would foreclose the ability of associated persons to withdraw expungement requests to avoid having their requests decided by the panel, and then seeking to re-file the request with the hope of obtaining a potentially more favorable panel.

The proposed rule change would include several requirements to help ensure that arbitrators on the Special Arbitrator Roster have the qualifications and training to decide straight-in requests.

a. Eligibility Requirements for the Special Arbitrator Roster

Arbitrators on the Special Arbitrator Roster would be public arbitrators who are eligible for the chairperson roster.<sup>77</sup> Public arbitrators are not employed in the securities industry and do not devote 20 percent or more of their professional work to the securities industry or to parties in disputes concerning investment accounts or transactions or

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<sup>75</sup> See proposed Rule 13805(a)(4).

<sup>76</sup> See supra note 75.

<sup>77</sup> See proposed Rule 13806(b); see also FINRA Rule 12400(c).

employment relationships within the financial industry.<sup>78</sup> Arbitrators are eligible for the chairperson roster if they have completed chairperson training provided by FINRA and: (1) have a law degree and are a member of a bar of at least one jurisdiction and have served as an arbitrator through award on at least one arbitration administered by an SRO in which hearings were held; or (2) have served as an arbitrator through award on at least three arbitrations administered by an SRO in which hearings were held.<sup>79</sup> These requirements would help ensure that the persons conducting the expungement hearing are impartial and experienced in managing and conducting arbitration hearings in the forum.<sup>80</sup>

Further, the public chairpersons must have evidenced successful completion of, and agreement with, enhanced expungement training provided by FINRA.<sup>81</sup> FINRA currently provides an Expungement Training module for arbitrators.<sup>82</sup> This training,

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<sup>78</sup> See supra note 8.

<sup>79</sup> See FINRA Rule 12400(c). For purposes of this proposed rule change, public arbitrators who are eligible for the chairperson roster would include those arbitrators who have met the chairperson eligibility requirements of FINRA Rule 12400(c), regardless of whether they have already served as a chair on an arbitration case.

<sup>80</sup> The Task Force suggested that the arbitrators on its recommended special arbitration panel be chair-qualified, in part because of the training that arbitrators must complete before they can be added to the chairperson roster. See FINRA's "Advanced Arbitrator Training," available at <https://www.finra.org/arbitration-mediation/advanced-arbitrator-training>. See also supra note 13.

<sup>81</sup> See proposed Rule 13806(b)(2)(A).

<sup>82</sup> See supra note 80. FINRA requires arbitrators to take mandatory online training that focuses on the Guidance. In addition, among other tools, FINRA provides Neutral Workshops (an online discussion on specific arbitration topics) and articles in The Neutral Corner (a quarterly publication that provides arbitrators and mediators with updates on important rules and procedures within the FINRA arbitration forum) to keep arbitrators informed about the expungement process

however, would be expanded for arbitrators seeking to qualify for the Special Arbitrator Roster. This would allow FINRA to further emphasize, with the subset of arbitrators on the Special Arbitrator Roster, the unique, distinct role they play in deciding whether to recommend a request to expunge customer dispute information from a broker's CRD record, and that expungement should be granted in limited circumstances and only if one or more of the grounds in FINRA Rule 2080(b)(1) is met.

Under the proposed amendments, arbitrators on the Special Arbitrator Roster would also be required to have served as an arbitrator through award on at least four customer-initiated arbitrations administered by FINRA or by another SRO in which a hearing was held.<sup>83</sup> FINRA believes that if an arbitrator has served on four arbitrations through to award, it would indicate that the arbitrator has gained the knowledge and experience in the forum to conduct hearings.<sup>84</sup>

b. Composition of the Panel

The proposed amendments would require that three randomly-selected members of the Special Arbitrator Roster decide all expungement requests filed under proposed

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and to emphasize the critical role that arbitrators play in maintaining the relevancy and integrity of disclosure information in the CRD system and BrokerCheck. See Neutral Workshop Audio and Video Files, Spring 2019 Neutral Workshop: Expungement of Customer Dispute Information, <https://www.finra.org/arbitration-mediation/neutral-workshop-audio-and-video-files>; The Neutral Corner, <https://www.finra.org/arbitration-mediation/neutral-corner-view>.

<sup>83</sup> See proposed Rule 13806(b)(2)(B). The hearing requirement would exclude hearings conducted under the special proceeding option of the simplified arbitration rules. See FINRA Rule 12800(c)(3)(B).

<sup>84</sup> In 2019, 85 percent of FINRA customer arbitrations closed other than by award. See Dispute Resolution Statistics, "How Arbitration Cases Close," available at <https://www.finra.org/arbitration-mediation/dispute-resolution-statistics>.

Rule 13805.<sup>85</sup> As discussed above, expungement requests may be complex to resolve, particularly straight-in requests where customers typically do not participate in the expungement hearing. Thus, having three arbitrators available to ask questions, request evidence and generally to serve as fact-finders in the absence of customer input would help ensure that a complete factual record is created to support the arbitrators' decision in such expungement hearings.<sup>86</sup>

To minimize the potential for party influence in the arbitrator selection process, the proposed rule change would require NLSS randomly to select the three public chairpersons from the Special Arbitrator Roster to decide an expungement request filed by an associated person.<sup>87</sup> The parties would not be permitted to agree to fewer than three arbitrators. The associated person would not be permitted to strike any arbitrators selected by NLSS nor stipulate to their removal,<sup>88</sup> but would be permitted to challenge

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<sup>85</sup> See proposed Rule 13806(b)(1).

<sup>86</sup> See supra Item II.A.1.(I)C., "Concerns Regarding Expungement" (discussing the importance of having a three-person panel decide straight-in requests).

<sup>87</sup> See proposed Rule 13806(b)(1). The first arbitrator selected would be the chair of the panel. See proposed Rule 13806(b)(3).

<sup>88</sup> The parties also would not be permitted to stipulate to the use of pre-selected arbitrators (i.e., arbitrators that the parties find on their own to use in their cases). See proposed Rule 13806(b)(1).

any arbitrator selected for cause.<sup>89</sup> If an arbitrator is removed, NLSS would randomly select a replacement.<sup>90</sup>

FINRA believes that the current process for selecting arbitrators—striking and combining ranked lists—would not be appropriate to use to select arbitrators to decide straight-in requests.<sup>91</sup> In arbitrations outside of the expungement context, the parties are typically adverse, which means that during arbitrator selection, each side may rank arbitrators on the lists whom they believe may be favorable to their case.<sup>92</sup> The adversarial nature of the proceedings serves to minimize the impact of each party’s influence in arbitrator selection.<sup>93</sup> In contrast, a straight-in request filed by an associated person against a firm may not be adversarial in nature. In addition, typically the customer or customer’s representative will not appear at the expungement hearing.

FINRA recognizes that the proposed arbitrator selection process for straight-in requests would limit the associated person and member firm’s input on arbitration selection. However, the arbitrators on the Special Arbitrator Roster would have the experience, qualifications and training necessary to conduct a fair and impartial

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<sup>89</sup> See proposed Rule 13806(b)(4). In addition, before the first hearing session begins, the Director may remove an arbitrator for conflict of interest or bias, either upon request of a party or on the Director's own initiative. See FINRA Rule 12407(a).

<sup>90</sup> See proposed Rule 13806(b)(4); see also FINRA Rules 12402(g) and 12403(g).

<sup>91</sup> See generally FINRA Rules 12402 and 12403.

<sup>92</sup> See *infra* note 189.

<sup>93</sup> Once the parties have ranked the arbitrators, the Director creates a combined ranked list of arbitrators based on the parties’ numerical rankings. The Director appoints the highest-ranked available arbitrator from the combined list. See FINRA Rules 12402(e) and (f) and 12403(d) and (e).

expungement hearing in accordance with the proposed rules, and to render a recommendation based on a complete factual record developed during the expungement hearing. FINRA believes that the higher standards that the arbitrators must meet to serve on the Special Arbitrator Roster should mitigate the impact of the absence of party input on the selection of arbitrators. In addition, associated persons and member firms would still be permitted to challenge any arbitrator for cause.<sup>94</sup>

C. Limitations on Expungement Requests

Currently, Rules 12805 and 13805 do not address when a party would not be permitted to file an expungement request in the forum.<sup>95</sup> The Guidance, however, describes several circumstances in which an expungement request should be ineligible for arbitration. The proposed rule change would incorporate the limitations contained in the Guidance as well as add time limits to when an associated person may file a straight-in request.

1. Limitations Applicable to Both Straight-in Requests and Expungement Requests During a Customer Arbitration

The Guidance provides that if a panel or a court has issued an award or decision denying an associated person's expungement request, the associated person may not request expungement of the same customer dispute information in another arbitration. In particular, the Guidance states that arbitrators should ask a party requesting expungement whether an arbitration panel or a court previously denied expungement of the customer

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<sup>94</sup> See proposed Rule 13806(b)(4).

<sup>95</sup> But see supra note 14 (describing time limits that apply to all arbitration claims, including expungement requests).

dispute information at issue and, if there has been a prior denial, the arbitration panel must deny the expungement request.<sup>96</sup>

The proposed rule change would codify the Guidance by providing that an associated person may not file a request for expungement of customer dispute information if (1) a panel held a hearing to consider the merits of the associated person's expungement request for the same customer dispute information or (2) a court of competent jurisdiction previously denied the associated person's request to expunge the same customer dispute information.<sup>97</sup> These proposed amendments would prevent an associated person from forum shopping, or seeking to return to the arbitration forum administered by FINRA, to garner a favorable outcome on his or her expungement request.<sup>98</sup>

## 2. Limitations Applicable to Straight-in Requests Only

As discussed below, under the proposed amendments, three additional limitations would apply to straight-in requests.

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<sup>96</sup> See supra note 3.

<sup>97</sup> See proposed Rules 12805(a)(1)(B) and 13805(a)(2)(A). The proposed rule change would require that the requesting party provide information about previous expungement requests and how such requests were decided. See, e.g., proposed Rule 12805(a)(1)(C)(ii)e.

<sup>98</sup> FINRA notes that if a panel holds a hearing that addresses the merits of an associated person's request for expungement, the Director may deny the forum to any subsequent request by the associated person or another party on behalf of the associated person to expunge the same customer dispute information. See FINRA Rules 12203(a) and 13203(a); see also proposed Rules 12203(b) and 13203(b).

i. No Straight-In Request If a Customer Arbitration Has Not Concluded

The Guidance provides that an associated person may not file a separate request for expungement of customer dispute information arising from a customer arbitration until the customer arbitration has concluded. The proposed rule change would codify and expand upon the Guidance by providing that an associated person may not file a straight-in request under proposed Rule 13805 if the customer arbitration, civil litigation or customer complaint that gave rise to the customer dispute information has not closed.<sup>99</sup>

The proposed rule change would prevent an associated person from obtaining a decision on an expungement request while the customer arbitration is still ongoing. This change would help ensure that a decision in the customer arbitration is issued before the decision on the expungement request and avoid the possibility of inconsistent awards. The proposed amendment would also help ensure that the arbitrators who will decide the straight-in request are able to consider the final factual record from the customer arbitration.

ii. Time Limits Applicable to Disclosures Arising After the Effective Date of the Proposed Rule Change

FINRA is aware that a number of expungement requests are filed many years after a customer arbitration closes or the reporting of a customer complaint in the CRD system.<sup>100</sup> To encourage timelier filing of expungement requests, the proposed amendments would establish time limits for expungement requests that are specifically

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<sup>99</sup> See proposed Rule 13805(a)(2)(A)(iii).

<sup>100</sup> See infra Item II.B.3.D., “Time Limits for Straight-in Requests – Quantitative Description.”

tied to the closure of customer arbitrations and civil litigations, or the reporting of customer complaints in the CRD system, as applicable.<sup>101</sup> The proposed time limits should help encourage customer participation in expungement proceedings and help ensure that straight-in requests are brought before relevant evidence and testimony becomes stale or unavailable.<sup>102</sup>

a. Two Years from the Close of a Customer Arbitration or Civil Litigation

Under the proposed rule change, an associated person would be required to file a straight-in request within two years of the close of the customer arbitration or civil litigation that gave rise to the customer dispute information.<sup>103</sup> A two-year period would provide a reasonable amount of time for associated persons and their firms to gather the documents, information and other resources required to file the expungement request. In addition, the two-year period would help ensure that the expungement hearing is held close enough in time to the customer arbitration, when information regarding the customer arbitration is available and in a timeframe that could increase the likelihood for

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<sup>101</sup> FINRA Rules 12206 and 13206 provide that no claim shall be eligible for submission to arbitration where six years have elapsed from the occurrence or event giving rise to the claim. Under these Rules, the panel has discretion to determine if the claim, including an expungement request, is eligible for arbitration. See supra note 14. As discussed below, if the proposed rule change is approved by the Commission, this six-year eligibility rule would continue to apply to requests to expunge customer dispute information that arose prior to the effective date of the proposed rule change.

<sup>102</sup> All customers from a customer arbitration or civil litigation, and all customers who initiated a customer complaint, would be notified of the expungement request and encouraged to attend and provide their input. See proposed Rule 13805(b)(1)(A).

<sup>103</sup> See proposed Rule 13805(a)(2)(A)(iv).

the customer to participate if he or she chooses to do so. The shorter timeframe, therefore, could provide panels with more complete factual records on which to base their expungement decisions. At the same time, it would allow the associated person time to determine whether to seek expungement by filing a straight-in request.

b. Six Years from the Date a Customer Complaint Is Reported  
to the CRD System

Under the proposed rule change, an associated person would be prohibited from filing a straight-in request to expunge a customer complaint where more than six years has elapsed since the customer complaint was initially reported to the CRD system and there was no customer arbitration or civil litigation that gave rise to the customer dispute information.<sup>104</sup>

Consistent with FINRA's current eligibility rules,<sup>105</sup> FINRA believes that six years from the date a customer complaint is initially reported to the CRD system should provide a reasonable amount of time for the associated person to bring an expungement claim. The six-year period would allow firms to complete their investigation of the customer complaint and close it in the CRD system; for the complaint to evolve, or not evolve, into an arbitration; and for the associated person to determine whether to proceed with a request to expunge the complaint. The proposed six-year time limit would also provide a reasonable time limit to encourage customer participation and help ensure the availability of evidence related to customer complaints.

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<sup>104</sup> See proposed Rule 13805(a)(2)(A)(v).

<sup>105</sup> See supra note 14.

iii. Time Limits Applicable to Disclosures Arising on or Prior to the Effective Date of the Proposed Rule Change

If the Commission approves the proposed rule change, the proposal would also establish time limits for requests to expunge customer dispute information arising from customer arbitrations and civil litigations that close, and for customer complaints that were initially reported to the CRD system, on or prior to the effective date of the proposed rule change.

Specifically, the proposed amendments would provide that if an expungement request is otherwise eligible under the six-year limitation period of FINRA Rule 13206(a), an associated person would be permitted to file a straight-in request under the Industry Code if: (1) the request for expungement is made within two years of the effective date of proposed rule change, and the disclosure to be expunged arises from a customer arbitration or civil litigation that closed on or prior to the effective date;<sup>106</sup> or (2) the request for expungement is made within six years of the effective date of the proposed rule change, and the disclosure to be expunged arises from a customer complaint initially reported to the CRD system on or prior to its effective date.<sup>107</sup>

3. Director's Authority to Deny the Forum

If an associated person files an expungement request that is ineligible for arbitration under proposed Rules 12805 and 13805, the proposed rule change would give the Director the express authority to deny the use of FINRA's arbitration forum to decide

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<sup>106</sup> See proposed Rule 13805(a)(2)(B)(i).

<sup>107</sup> See proposed Rule 13805(a)(2)(B)(ii).

the request.<sup>108</sup> If the expungement request is ineligible for arbitration because a court or panel has decided previously an expungement request related to the same customer dispute information, the Director would deny the forum with prejudice as the request would be an attempt to receive a second decision on a request that had been decided previously on the merits. The Director would also deny the forum with prejudice if an expungement request is ineligible under the proposed time limitations.

If the request is ineligible because a customer arbitration that involves the same customer dispute information is not concluded, the Director would deny the forum without prejudice so that the associated person could file the request (or a party could file an on-behalf-of request) in the customer arbitration or as a straight-in request after the customer arbitration concludes.

D. Procedural Requirements Relating to All Expungement Hearings

The Codes currently provide a list of requirements panels must follow in order to decide an expungement request.<sup>109</sup> In addition, the Guidance provides best practices that arbitrators should follow when deciding expungement requests. To guide further the arbitrators' decision-making, the proposed rule change would expand the expungement hearing requirements currently in FINRA Rules 12805 and 13805 to incorporate the relevant provisions from the Guidance. The proposed amendments would apply to all expungement hearings.<sup>110</sup>

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<sup>108</sup> See proposed Rules 12203(b) and 13203(b). The panel would continue to have the authority to resolve any questions regarding eligibility of such claims under Rules 12206 and 13206, as applicable. See supra note 14.

<sup>109</sup> See supra note 24.

<sup>110</sup> See proposed Rules 12805(c) and 13805(c). The proposed procedural requirements for expungement hearings would apply to all expungement hearings,

1. Recorded Hearing Sessions

The Codes require a panel that is deciding an expungement request to hold a recorded hearing session (by telephone or in person) regarding the appropriateness of expungement.<sup>111</sup> Consistent with current practice, the proposed rule change would add the ability to hold a recorded hearing session by video conference.<sup>112</sup> Further, the proposed rule change would clarify that a panel would not be limited in the number of hearing sessions it should hold to decide the expungement request.<sup>113</sup>

2. Associated Person's Appearance

The proposed rule change would require the associated person who is seeking expungement of the customer dispute information to appear personally at the expungement hearing.<sup>114</sup> A party requesting expungement on behalf of an unnamed person would also be required to appear at the hearing. The panel would determine whether an appearance should be by telephone, in person, or by video conference.

As the associated person is requesting the permanent removal of information from his or her CRD record, FINRA believes the associated person whose CRD record would

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including hearings held during a customer arbitration or simplified arbitration (see infra Item II.A.1.(II)F., “Expungement Requests During Simplified Customer Arbitrations”) that consider an expungement request, and expungement hearings conducted by a panel from the Special Arbitrator Roster.

<sup>111</sup> See FINRA Rules 12805(a) and 13805(a).

<sup>112</sup> See proposed Rules 12805(c)(1) and 13805(c)(1).

<sup>113</sup> See supra note 112.

<sup>114</sup> See proposed Rules 12805(c)(2) and 13805(c)(2). The requirement to appear personally at the expungement hearing would also apply to an unnamed person who seeks to have his or her customer dispute information expunged.

be expunged must personally participate in the expungement hearing to respond to questions from the panel and those customers who choose to participate. Rather than restrict the method of appearance, FINRA is proposing to provide the panel with the authority to decide which method of appearance would be the most appropriate for the particular case. FINRA believes that providing flexibility as to the method of appearance would encourage appropriate fact-finding by the arbitrators and generally strengthen the process.

### 3. Customer's Participation during the Expungement Hearing

The Guidance states that it is important to allow customers and their representatives to participate in the expungement hearing if they wish to do so.<sup>115</sup>

Specifically, the Guidance provides that arbitrators should:

- Allow the customers and their representatives to appear at the expungement hearing;
- Allow the customer to testify (telephonically, in person, or other method) at the expungement hearing;
- Allow the representative for the customer or a pro se customer to introduce documents and evidence at the expungement hearing;

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<sup>115</sup> The Guidance directs arbitrators to permit customers and their counsel to participate in the expungement hearing. See supra note 3. FINRA Rules 12208 and 13208 permit a party to be represented pro se, by an attorney or by a person who is not an attorney. The proposed amendments would replace the term “counsel” with “representative.” See also Securities Arbitration—Should You Hire an Attorney? (Jan. 3, 2019), <https://www.finra.org/investors/insights/securities-arbitration>.

- Allow the representative for the customer or a pro se customer to cross-examine the broker or other witnesses called by the party seeking expungement; and
- Allow the representative for the customer or a pro se customer to present opening and closing arguments if the panel allows any party to present such arguments.

The proposed rule change would codify these provisions of the Guidance. The proposed rule change would make clear that all customers whose customer arbitrations, civil litigations and customer complaints gave rise to the customer dispute information that is a subject of the expungement request have a right to representation and are entitled to appear at the expungement hearing.<sup>116</sup> The proposed rule change would provide that the customer can appear by telephone, in person, by video conference or other means convenient to the customer and customer's representative.<sup>117</sup> By providing customers with options for how to participate in hearings, FINRA seeks to make it easier for customers to participate and, thereby, encourage customer participation. Customer participation during an expungement hearing provides the panel with important information and perspective that it might not otherwise receive.

In addition, the proposed rule change would provide that customers must be allowed to testify at the expungement hearing and be questioned by the customer's

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<sup>116</sup> See proposed Rules 12805(c)(3)(A) and 12805(c)(4); see also proposed Rules 13805(c)(3)(A) and 13805(c)(4). The proposed rule change would make clear that customers also have the option to provide their position on the expungement request in writing in lieu of attending the hearing.

<sup>117</sup> See proposed Rules 12805(c)(3)(B) and 13805(c)(3)(B).

representative.<sup>118</sup> If a customer testifies, the associated person or a party requesting expungement on-behalf-of an unnamed person would be allowed to cross-examine the customer.<sup>119</sup> Similarly, the customer or customer's representative would be permitted to cross-examine the associated person or party requesting expungement on-behalf-of an unnamed person and any witnesses called by the associated person or party requesting expungement on-behalf-of an unnamed person during the expungement hearing.<sup>120</sup> If the customer introduces any evidence at the expungement hearing, the associated person or party requesting expungement on-behalf-of an unnamed person could object to the introduction of the evidence, and the panel would decide any objections.<sup>121</sup> The customer or customer's representative would also be permitted to present opening and closing arguments if the panel permits any party to present such arguments.<sup>122</sup> FINRA believes the proposal strikes the right balance of allowing the customer to participate fully in the hearing and giving the associated person or party requesting expungement on-behalf-of an unnamed person the opportunity to substantiate arguments in support of the expungement request.

#### 4. Panel Requests for Additional Documents or Evidence

Arbitrators on the panel do not conduct their own research when hearing an arbitration case; instead, they review the materials provided by the parties. If they need

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<sup>118</sup> See proposed Rules 12805(c)(5)(A) and 13805(c)(5)(A).

<sup>119</sup> See supra note 118.

<sup>120</sup> See proposed Rules 12805(c)(5)(C) and 13805(c)(5)(C).

<sup>121</sup> See proposed Rules 12805(c)(5)(B) and 13805(c)(5)(B).

<sup>122</sup> See proposed Rules 12805(c)(5)(D) and 13805(c)(5)(D).

more information, they can request it from the parties.<sup>123</sup> In deciding an expungement request, particularly in cases that settle before an evidentiary hearing or in cases where the customer does not participate in the expungement hearing, the arbitrator's role as fact-finder is critical. Given this significant role, arbitrators must ensure that they have all of the information necessary to make a fully-informed decision on the expungement request on the basis of a complete factual record. Thus, the proposed rule change would codify the ability of arbitrators to request from the associated person, or other party requesting expungement, any documentary, testimonial or other evidence that they deem relevant to the expungement request.<sup>124</sup>

#### 5. Review of Settlement Documents

Current FINRA Rule 12805(b) provides that, in the event the parties from the customer arbitration settle their case, the panel considering the expungement request must review the settlement documents and consider the amount of payments made to any party and any other terms and conditions of the settlement.<sup>125</sup> The proposed rule change would retain this requirement.<sup>126</sup>

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<sup>123</sup> See proposed Rules 12805(c)(6) and 13805(c)(6).

<sup>124</sup> See supra note 123. The Guidance also suggests that arbitrators should ask the associated person seeking expungement or the party seeking expungement on an associated person's behalf to provide a current copy of the BrokerCheck report for the person whose record would be expunged, paying particular attention to the "Disclosure Events" section of the report. See supra note 3. FINRA continues to encourage arbitrators to request a current copy of the associated person's BrokerCheck report.

<sup>125</sup> The panel should review all settlement documents related to the customer dispute information the associated person is seeking to be expunged, regardless of whether the associated person was a party to the settlement.

<sup>126</sup> See proposed Rules 12805(c)(7) and 13805(c)(7).

In addition, the Guidance encourages arbitrators to inquire and fully consider whether a party conditioned a settlement of the arbitration upon agreement not to oppose the request for expungement in cases in which the customer does not participate in the expungement hearing or the requesting party states that a customer has indicated that he or she will not oppose the expungement request. The proposed rule change would codify this language in the Guidance.<sup>127</sup> Conditioned settlements violate FINRA Rule 2081 and may be grounds to deny an expungement request.<sup>128</sup>

#### 6. Awards

Current FINRA Rules 12805(c) and 13805(c) require that the panel indicate in the arbitration award which of the FINRA Rule 2080 grounds for expungement serves as the basis for its expungement recommendation and provide a brief written explanation of the reasons for its finding that one or more FINRA Rule 2080 grounds for expungement applies to the facts of the case. The proposed rule change would retain this requirement, but would remove the word “brief” to indicate to the panel that it must provide enough detail in the award to explain its rationale for recommending expungement.<sup>129</sup> As the

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<sup>127</sup> See proposed Rules 12805(c)(7) and 13805(c)(7).

<sup>128</sup> FINRA Rule 2081 provides that no member firm or associated person shall condition or seek to condition settlement of a dispute with a customer on, or to otherwise compensate the customer for, the customer's agreement to consent to, or not to oppose, the member's or associated person's request to expunge such customer dispute information from the CRD system. See also Prohibited Conditions Relating to Expungement of Customer Dispute Information FAQ, <https://www.finra.org/arbitration-mediation/faq/prohibited-conditions-relating-expungement-customer-dispute-information>.

<sup>129</sup> In addition, all awards rendered under the Codes, including awards recommending expungement, must comply with the requirements of FINRA Rules 12904 or 13904.

Guidance suggests, the explanation must be complete and not solely a recitation of one of the FINRA Rule 2080 grounds or language provided in the expungement request.

In addition, the proposed rule change would incorporate language from the Guidance that the panel's explanation should identify any specific documentary, testimonial or other evidence relied on in recommending expungement.<sup>130</sup>

The proposed rule change would also make clarifying revisions to FINRA Rules 12805(c) and 13805(c). The proposed amendments would indicate that the FINRA Rule 2080 grounds that the panel must indicate serve as the basis for the expungement order are the grounds found in paragraph (b)(1) of FINRA Rule 2080.<sup>131</sup> The proposed amendments would also provide that the panel would "recommend" rather than "grant" expungement.<sup>132</sup>

#### 7. Forum Fees

The proposed rule change would retain the current requirements in FINRA Rules 12805(d) and 13805(d) that addresses how forum fees are assessed in expungement hearings.<sup>133</sup> Specifically, the panel must assess against the parties requesting expungement all forum fees for each hearing in which the sole topic is the determination of the appropriateness of expungement.

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<sup>130</sup> See proposed Rules 12805(c)(8) and 13805(c)(8).

<sup>131</sup> See infra note 238, and accompanying text.

<sup>132</sup> The word "recommend" more accurately describes the panel's role in the expungement process, consistent with FINRA's longstanding practice to state in expungement awards that the arbitrators "recommend," rather than "grant," expungement. See supra note 10.

<sup>133</sup> See proposed Rules 12805(c)(9) and 13805(c)(9).

E. Notifications to Customers and States Regarding Expungement Requests

1. Associated Person Serves Customer with Statement of Claim

The Guidance suggests that when a straight-in request is filed against a firm, arbitrators order the associated person to provide a copy of the statement of claim to the customers involved in the customer arbitration that gave rise to the customer dispute information. This helps ensure that the customers know about the expungement request and have an opportunity to participate in the expungement hearing or provide a position in writing on the associated person's request. The proposed rule change would codify this practice in the Industry Code by requiring that the associated person provide all customers whose customer arbitrations, civil litigations and customer complaints gave rise to the customer dispute information that is a subject of the expungement request with notice of the expungement request by serving a copy of the statement of claim requesting expungement.<sup>134</sup> The panel would be authorized to decide whether extraordinary circumstances exist that make service on the customers impracticable.<sup>135</sup>

Given the associated person's personal interest in obtaining expungement, FINRA believes that the panel should review all documents that the associated person used to inform the customers about the expungement request as well as any customer responses

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<sup>134</sup> See proposed Rule 13805(b)(1)(A). The associated person would be required to notify the customer before the first scheduled hearing session is held so that the customer would be aware of the expungement request in advance and could plan to participate once he or she is notified of the time and place of the hearing. See FINRA Rule 13100(p) (providing that a hearing session could be a hearing or prehearing conference).

<sup>135</sup> See proposed Rule 13805(b)(1)(A).

received. Accordingly, the proposed amendments would require the associated person to file with the panel all documents provided by the associated person to the customers, including proof of service, and any responses received by the associated person from a customer.<sup>136</sup> The proposed requirement would help ensure that the associated person does not attempt to dissuade a customer from participating in the expungement hearing.

## 2. Notification to Customers of Expungement Hearing

To help ensure that the customer is notified about the expungement hearing, the proposed rule change would provide that the Director shall notify all customers whose customer arbitrations, civil litigations and customer complaints gave rise to the customer dispute information that is a subject of the expungement request, of the time, date and place of the expungement hearing using the customer's current address provided by the party seeking expungement.<sup>137</sup> The associated person would be required to provide a current address for the customer, or the expungement request would be considered deficient and would not be served.

## 3. State Notification of Expungement Requests

The proposed rule change would require FINRA to notify state securities regulators, in the manner determined by FINRA, of an expungement request within 30 days after receiving a complete request for expungement.<sup>138</sup> The proposed amendments

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<sup>136</sup> See proposed Rule 13805(b)(1)(C).

<sup>137</sup> See proposed Rule 13805(b)(2). This requirement would apply to straight-in requests filed under the Industry Code; notice to customers would not be necessary for requests filed under proposed Rule 12805 of the Customer Code as the customer would be a named party.

<sup>138</sup> See proposed Rules 12805(b) and 13805(b)(3).

would help ensure that state securities regulators are timely notified of the expungement requests.<sup>139</sup>

F. Expungement Requests During Simplified Customer Arbitrations

Customer arbitrations involving \$50,000 or less, called simplified arbitrations, are governed by FINRA Rule 12800. FINRA Rule 12800 provides customers with expedited procedures to make the FINRA forum economically feasible for these smaller claims. Simplified arbitrations are decided on the pleadings and other materials submitted by the parties, unless the customer requests a hearing.<sup>140</sup> Further, a single arbitrator from the chairperson roster is appointed to consider and decide simplified arbitrations, unless the parties agree in writing otherwise.<sup>141</sup>

The customer who files a simplified arbitration determines how the claim will be decided. In particular, the customer has the option of having the case decided in one of three ways: (1) without a hearing (referred to as “on the papers”), where the arbitrator decides the case on the pleadings or other materials; (2) in an “Option One” full hearing, in which prehearings and hearings on the merits take place pursuant to the regular provisions of the Code; or (3) in an “Option Two” special proceeding, whereby the

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<sup>139</sup> FINRA would make this notification in connection with expungement requests under the Customer and Industry Codes. Such notification could be achieved by notifying NASAA of the expungement requests.

<sup>140</sup> See FINRA Rule 12800(a).

<sup>141</sup> See FINRA Rule 12800(b). The parties could agree to have a three-person panel decide the simplified case. For ease of reference, when discussing expungement requests in simplified arbitrations under the proposed rule change, the rule filing uses the term “arbitrator,” unless otherwise specified, to mean either a panel or single arbitrator.

parties present their case in a hearing to the arbitrator in a compressed timeframe, so that the hearings last no longer than one day.<sup>142</sup>

Currently, named associated persons and parties requesting expungement on-behalf-of unnamed persons request expungement during simplified arbitrations. FINRA Rule 12800 does not, however, expressly address how an expungement request should be filed or considered during a simplified arbitration. The proposed amendments would codify an associated person's ability to request expungement when named as a respondent in a simplified arbitration, and for other parties to request expungement on-behalf-of an unnamed person. The proposed rule change would also establish procedures for requesting and considering expungement requests in simplified arbitrations that are consistent with the expedited nature of these proceedings.<sup>143</sup>

#### 1. Requesting Expungement

The proposed rule change would permit a named associated person to request expungement, or a party to file an on-behalf-of request, during a simplified arbitration. Unlike in a non-simplified arbitration, if expungement is not requested during the simplified arbitration, the associated person would be permitted to request it as a straight-in request filed under the Industry Code.<sup>144</sup>

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<sup>142</sup> See FINRA Rule 12800(c).

<sup>143</sup> Under the proposed rule change, an associated person would not be permitted to request expungement in a simplified arbitration administered under the Industry Code, FINRA Rule 13800. All expungement requests under the Industry Code must be filed in accordance with proposed Rule 13805.

<sup>144</sup> See infra Item II.A.1.(II)F.1.c., "When No Expungement Request is Made in a Simplified Arbitration."

a. By a Named Associated Person During the Simplified Arbitration

Under the proposed rule change, an associated person named as a respondent in a simplified arbitration could request expungement during the arbitration of the customer dispute information arising from the customer's statement of claim, provided the request is eligible for arbitration.<sup>145</sup>

If a named associated person requests expungement during a simplified arbitration, the proposed rule change would require the request to be filed in an answer or pleading requesting expungement and include the same information required as a request filed in a non-simplified arbitration.<sup>146</sup> Because of the expedited nature of simplified arbitrations, if the named associated person requests expungement in a pleading other than answer, the request must be filed within 30 days after the date that FINRA notifies the associated person of arbitrator appointment,<sup>147</sup> which is the last deadline provided to

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<sup>145</sup> See proposed Rule 12800(d)(1)(A). The limitations that apply to expungement requests filed by a named associated person under proposed Rule 12805(a)(1)(B) would apply to these requests. See supra Item II.A.1.(II)C., "Limitations on Expungement Requests."

<sup>146</sup> See proposed Rules 12800(d)(1)(B)(i) and 12805(a)(1)(C)(ii). Thus, the associated person's expungement request would be required to contain the applicable filing fee; the CRD number of the party requesting expungement; each CRD occurrence number that is the subject of the request; the case name and docket number that gave rise to the disclosure, if applicable; and an explanation of whether expungement of the same customer dispute information was previously requested and, if so, how it was decided.

<sup>147</sup> FINRA would notify state securities regulators, in the manner determined by FINRA, of an expungement request within 30 days after receiving a complete expungement request. See proposed Rule 12800(f)(1).

the parties in a simplified arbitration to submit any additional documents before the case is submitted to the arbitrator.<sup>148</sup>

To limit arbitrator shopping, the arbitrator would be required to decide an expungement request once it is filed by the associated person.<sup>149</sup> If an associated person withdraws or does not pursue the request after filing, the arbitrator would be required to deny the request with prejudice so that it could not be re-filed.<sup>150</sup>

b. By a Party On-Behalf-Of an Unnamed Person

Under the proposed amendments, the requirements for a party to file an on-behalf-of request during a simplified arbitration would be the same as the requirements for a named associated person filing an expungement request during a simplified arbitration, with one distinction. A named party would only be able to file an on-behalf-of request during a simplified arbitration with the consent of the unnamed person. As with on-behalf-of requests filed in customer arbitrations under proposed Rule 12805(a)(2), the unnamed person who would benefit from the expungement request must consent to such filing by signing the Form.<sup>151</sup>

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<sup>148</sup> FINRA notifies the parties when an arbitrator has been appointed. FINRA informs the parties that they have 30 days from the date of notification to submit additional documents or other information before the case is submitted to the arbitrator.

<sup>149</sup> See proposed Rule 12800(e)(1).

<sup>150</sup> See proposed Rule 12800(d)(1)(C).

<sup>151</sup> See proposed Rule 12800(d)(2). The request must also meet the same requirements as an on-behalf-of request filed under proposed Rule 12805(a)(2). See proposed Rules 12805(a)(1)(C)(ii), 12805(a)(2)(C)(ii) and 12805(a)(2)(D); see also supra Items II.A.1.(II)A.1.b., “Expungement Requests By a Party Named in the Customer Arbitration On-Behalf-Of an Unnamed Person.”

c. When No Expungement Request is Made in a Simplified Arbitration

If expungement is not requested during the simplified arbitration under proposed Rule 12800(d), the associated person would be able to file a straight-in request under proposed Rule 13805 and have the request decided by a three-person panel randomly selected from the Special Arbitrator Roster.<sup>152</sup> The request would be subject to the limitations on whether and when such requests may be filed under the Industry Code.<sup>153</sup>

Due to the expedited nature of simplified proceedings, FINRA believes that the associated person should be able to seek expungement separately under the Industry Code and have his or her expungement request decided by a panel randomly selected from the Special Arbitrator Roster. In simplified arbitrations, there may be less discovery, and the customer may dictate the extent of the evidence presented to the arbitrator. The customer may, for example, determine to have the arbitration decided on the papers. Because there may be less information available for the arbitrator to evaluate an expungement request during a simplified arbitration—even when the simplified arbitration results in an award—the associated person would retain the ability to choose to file the request as a straight-in request under the Industry Code.

2. Deciding Expungement Requests during Simplified Arbitrations

If a named associated person or party on-behalf-of an unnamed person requests expungement during a simplified arbitration, the arbitrator would be required to decide

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<sup>152</sup> See proposed Rules 12800(e)(2), 13805 and 13806.

<sup>153</sup> See proposed Rule 13805(a)(2); see also supra Item II.A.1.(II)C., “Limitations on Expungement Requests.”

the expungement request, regardless of how the simplified arbitration case closes (e.g., even if the case settles).<sup>154</sup>

Under the proposed rule change, how and when the expungement request is decided would depend on which option the customer selects to decide the simplified arbitration.

a. No Hearing or Option Two Special Proceeding

If the customer opts not to have a hearing or chooses an Option Two special proceeding, the arbitrator would decide the customer's dispute first and issue an award.<sup>155</sup> After the customer's dispute is decided, the arbitrator must hold a separate expungement-only hearing to consider and decide the expungement request and issue a separate award.<sup>156</sup>

The arbitrator would decide the customer's dispute first and issue an award to minimize any delays in resolving the customer arbitration and any delays in potential recovery that a customer may be awarded. Further, because the customer arbitration may not be as fully developed when an "on the papers" or special proceeding is requested, the arbitrator must hold a separate expungement-only hearing to ensure that he or she has access to sufficient evidence to make a fully-informed decision on the expungement request. The Director would notify all customers whose simplified customer arbitrations

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<sup>154</sup> See proposed Rule 12800(e)(1).

<sup>155</sup> See proposed FINRA Rule 12800(e)(1)(A).

<sup>156</sup> See supra note 155. The arbitrator must conduct the expungement hearing pursuant to proposed Rule 12805(c). The expungement award must meet the requirements of proposed Rule 12805(c)(8), and forum fees would be assessed pursuant to proposed Rule 12805(c)(9).

and customer complaints gave rise to the customer dispute information that is a subject of the expungement request, of the time, date and place of the expungement hearing.<sup>157</sup>

b. Option One Hearing

If the customer chooses to have a full “Option One” hearing on his or her claim and it closes by award, the arbitrator would be required to consider and decide the expungement request during the customer arbitration and include the decision in the award.<sup>158</sup> This process would be the same as deciding an expungement request during a non-simplified customer arbitration that closes by award after a hearing, where the customer’s claim and expungement request are addressed during the customer arbitration. As there would be a more complete factual record from the full hearing on the merits of the customer case, the arbitrator could decide the customer dispute and the expungement request after the hearing concludes.

If the customer arbitration closes other than by award or by award without a hearing, the arbitrator would be required to hold a separate expungement-only hearing to consider and decide the expungement request and issue the decision in an award.<sup>159</sup> The arbitrator would need to conduct a separate expungement hearing to develop a complete factual record in order to make a fully-informed decision on the expungement request.<sup>160</sup>

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<sup>157</sup> See proposed Rule 12800(f)(2). The Director would also notify these customers of the expungement hearing, if the associated person opts to file the request under the Industry Code after the simplified case closes.

<sup>158</sup> See proposed Rule 12800(e)(1)(B)(i).

<sup>159</sup> See proposed Rule 12800(e)(1)(B)(ii).

<sup>160</sup> See supra note 156.

Given the generally less complex nature of simplified arbitrations, FINRA does not believe that it is necessary for a panel from the Special Arbitrator Roster to decide an expungement request if a simplified customer arbitration closes other than by award or by award without a hearing. However, if the Commission approves the proposed rule change, FINRA will continue to monitor expungement requests and decisions in simplified arbitrations to determine if such requests should be decided by the Special Arbitrator Roster, particularly if the customer chooses to have his or her case decided on the papers or in a special proceeding.

G. Non-substantive changes

FINRA is also proposing to amend the Codes to make non-substantive, technical changes to the rules impacted by the proposed rule change. For example, the proposed rule change would require the renumbering of paragraphs and the updating of cross-references in the rules impacted by the proposed rule change. In addition, the title of Part VIII of the Customer Code would be amended to add a reference to “Expungement” proceedings. Similarly, the title of Part VIII of the Industry Code would be amended to add a reference to “Expungement Proceedings” and “Promissory Note Proceedings.” FINRA believes the proposed changes to the titles would more accurately reflect the contents of Part VIII of the Customer and Industry Codes. FINRA is also proposing to re-number current FINRA Rule 13806 (Promissory Note Proceedings) as new FINRA Rule 13807, without substantive change to the current rule language.

If the Commission approves the proposed rule change, FINRA will announce the effective date of the proposed rule change in a Regulatory Notice to be published no later than 60 days following Commission approval. The effective date will be no later than

120 days following publication of the Regulatory Notice announcing Commission approval of the proposed rule change.

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>161</sup> which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest.

The proposed rule change seeks to balance the important investor protection objectives of maintaining the integrity and accuracy of the information in the CRD system and BrokerCheck with the interest of brokers and firms in the fairness and accuracy of the disclosures contained in the systems.

The proposed rule change will enhance the current expungement framework and improve the efficiency of the FINRA arbitration forum by codifying the Guidance as rules that arbitrators and parties must follow. In addition, when an associated person files a claim against a firm for the sole purpose of requesting expungement, these cases can be complex to resolve, particularly if the customer or customer's representative does not participate in the hearing. Having three arbitrators available to ask questions, request evidence and generally to serve as fact-finders in the absence of customer input will help ensure that a complete factual record is created to support the arbitrators' decision in such expungement hearings. In addition, the proposed rule change will help ensure that arbitrators who will decide these requests meet heightened qualifications and have

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<sup>161</sup> 15 U.S.C. 78o-3(b)(6).

completed enhanced expungement training. FINRA believes that by requiring a three-person panel from the Special Arbitrator Roster to decide expungement requests filed under the Industry Code, the proposed rule change will help ensure expungement is recommended in limited circumstances.

The proposed rule change will foreclose a practice that has emerged in the existing expungement process where parties seek expungement after a prior denial by a court or panel of a request to expunge the same customer dispute information, or where parties withdraw or do not pursue an expungement request and then make another request for expungement of the same customer dispute information. The proposed rule change imposes procedures and requirements around when and how a party may request expungement, and expressly provides that omission of certain of the requirements will make the expungement request deficient. Further, the proposed rule change provides the Director with express authority to deny the forum if an expungement request is ineligible for arbitration under the proposed rules. Thus, FINRA believes the proposed rule change will add more transparency to the expungement process.

Moreover, the proposed rule change seeks to protect investors and the public interest by notifying customers of expungement requests filed under the Industry Code. Although a straight-in request will be filed against a firm, customers whose disputes are a subject of the request will be notified and encouraged to participate in the expungement hearing. Such notifications will make clear to arbitrators and parties the rights of customers who choose to participate in these hearings. The customers' input will provide the panel with additional insight on the customer dispute and help create a complete factual record, which will result in more informed decisions on expungement requests.

FINRA believes this enhancement, which will encourage and facilitate customer participation in expungement hearings, will help to maintain the integrity of the information in the CRD system.

Further, the process of requesting expungement during a simplified arbitration will be codified to help ensure that customers are aware of their rights under the process and how an expungement request will affect (and not affect) their arbitration claims. By expressly incorporating the practice of requesting expungement during simplified proceedings, the proposed amendments add consistency to the rules and provide more guidance to the arbitrators and the parties requesting expungement.

The proposed rule change will also help ensure that state securities regulators have knowledge of expungement requests by requiring notification to the states, in the manner determined by FINRA, after FINRA receives a complete expungement request.

For these reasons, the proposed rule change represents a significant step towards addressing concerns with the current expungement framework. FINRA believes the proposed rule change will improve the expungement framework by incorporating the Guidance, establishing a Special Arbitrator Roster and addressing gaps that have emerged in the existing expungement framework. In addition, FINRA believes these changes will help to maintain the accuracy and integrity of the information in the CRD system and BrokerCheck, while also protecting brokers from the publication of false allegations against them.

B. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

Economic Impact Assessment

FINRA has undertaken an economic impact assessment to analyze the regulatory need for the proposed rule change, its potential economic impacts, including anticipated costs, benefits and distributional and competitive effects, relative to the current baseline, and the alternatives FINRA considered in assessing how best to meet FINRA's regulatory objectives.

1. Regulatory Need

The proposed rule change would address concerns relating to the expungement process that are not consistent with the regulatory intent to permit expungement in limited circumstances. The concerns include the potential impact of the absence of customers and their representatives from an expungement hearing which may result in the arbitrator or panel receiving information only from the associated person. The concerns also include associated persons having their straight-in requests heard by a single arbitrator instead of a three-person panel, and the selection of arbitrators to hear these requests. Lastly, the concerns include requests to expunge the same customer dispute information in multiple proceedings. The proposed rule change would also codify and expand upon the provisions of the Guidance to help ensure that arbitrators and parties are adhering to these procedures for all expungement requests, and to encourage and facilitate customer participation in expungement hearings.

## 2. Economic Baseline

The economic baseline for the proposed rule change includes the current provisions under the Codes that address the process for parties to seek expungement relief. In addition, because arbitrators are generally believed to be adhering to the best practices and recommendations that are a part of the Guidance, the economic baseline also includes the Guidance.<sup>162</sup> The proposed rule change is expected to affect associated persons and other parties to expungement requests including member firms, customers and arbitrators. The proposed rule change may also affect users of customer dispute information contained in the CRD system and displayed through BrokerCheck.<sup>163</sup>

The customer dispute information contained in the CRD system is submitted by registered securities firms and regulatory authorities in response to questions on the uniform registration forms.<sup>164</sup> The information can be valuable to current and prospective customers to learn about the conduct of associated persons.<sup>165</sup> Current and

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<sup>162</sup> See supra note 3.

<sup>163</sup> Users of customer dispute information include investors; member firms and other companies in the financial services industry; individuals registered as brokers or seeking employment in the brokerage industry; and FINRA, states and other regulators.

<sup>164</sup> See supra note 5 and accompanying text for additional discussion of the uniform registration forms and the information contained in the CRD system. Some of the information may involve pending actions or allegations that have not been resolved or proven.

<sup>165</sup> Recent academic studies provide evidence that the past disciplinary and other regulatory events associated with a firm or individual can be predictive of similar future events. See Hammad Qureshi & Jonathan Sokobin, Do Investors Have Valuable Information About Brokers? FINRA Office of the Chief Economist Working Paper, Aug. 2015; see also Mark Egan, Gregor Matvos, & Amit Seru, The Market for Financial Adviser Misconduct, *Journal of Political Economy* 127, no. 1 (February 2019): 233-295.

prospective customers may not select or remain with an associated person or a member firm that employs an associated person with a record of customer disputes. Similarly, member firms and other companies in the financial services industry may use the information when making employment decisions.<sup>166</sup> In this manner, the customer dispute information contained in the CRD system (and displayed through BrokerCheck) may positively or negatively affect the business and professional opportunities of associated persons. Where the information is reliable, it also provides for customer protections and information useful for member firms.

Any negative impact on the business and professional opportunities of associated persons may be appropriate and consistent with investor protection, such as when the customer dispute information has merit. Any such negative impact may be inappropriate, however, if, for example, the customer dispute information is factually impossible, clearly erroneous, or false. Regardless of the merit, associated persons have an incentive to remove customer dispute information from the CRD system and its public display through BrokerCheck.

An associated person, or a party on-behalf-of an unnamed person, typically begins the process to remove customer dispute information from the CRD system by filing an expungement request in FINRA arbitration. FINRA is able to identify 6,928 requests to expunge customer dispute information in FINRA arbitration from January 2016 through

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<sup>166</sup> Customer dispute information submitted to the CRD system and displayed through BrokerCheck may have other uses. For example, investors may use the information when deciding with whom to do business. FINRA, states and other regulators also use the information to regulate brokers.

December 2019 (the “sample period”). More than one expungement request can be made in a single arbitration, and multiple expungement requests may relate to the same arbitration, civil litigation or complaint if the dispute relates to more than one associated person.

Among the 6,928 expungement requests, 3,203 requests (46 percent) were made during a customer arbitration, and 3,725 requests (54 percent) were filed as a straight-in request.<sup>167</sup> The 3,203 expungement requests made during a customer arbitration include 2,936 requests made during a non-simplified customer arbitration and 267 requests made during a simplified customer arbitration. The 3,725 requests to expunge customer dispute information disclosures filed as a straight-in request include 3,657 requests in arbitrations filed solely against a member firm or against a member firm and a customer, and 68 requests in arbitrations filed solely against a customer. In the 3,203 expungement requests made during a customer arbitration, the associated person was a named party in 1,504 of the requests (47 percent), and an unnamed party in 1,699 of the requests (53 percent).

Among the expungement requests during the sample period, FINRA is able to identify 82 requests to expunge the same customer dispute information in a subsequent arbitration.<sup>168</sup> For purposes of this analysis, FINRA limited the identification of

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<sup>167</sup> Sixteen requests to expunge customer dispute information were made during industry arbitrations that were not straight-in requests. To simplify the analysis, we exclude these 16 requests from the sample.

<sup>168</sup> Eighty of the 82 subsequent expungement requests relate to previous requests in another arbitration that were withdrawn or otherwise not pursued by the associated person or party that filed the request. For the two remaining subsequent expungement requests, one relates to a previous request on behalf of an unnamed person that was denied, and the other to a previous request that was

additional expungement requests to those requests where both the initial request and the subsequent request were made during the sample period. Additional subsequent expungement requests may have been filed during the sample period if the initial expungement request was made prior to the sample period (i.e., before January 2016). The 82 requests to expunge the same customer dispute information in a subsequent arbitration can, therefore, be considered a lower bound for the number of these requests during the sample period. The proposed rule change would foreclose associated persons from filing additional requests.

As of December 2019, 5,159 of the 6,928 expungement requests were made in an arbitration that closed. Among the 5,159 expungement requests, 2,255 requests (44 percent) were made during a customer arbitration and 2,904 requests (56 percent) were filed as a straight-in request. The 2,255 expungement requests made during a customer arbitration include 2,015 requests made during a non-simplified customer arbitration and 240 requests made during a simplified customer arbitration. The 2,904 requests filed as a straight-in request include 2,838 requests in arbitrations filed solely against a member firm or a member firm and a customer, and 66 requests in arbitrations filed solely against

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determined by the panel to be ineligible for arbitration. An arbitrator or panel recommended expungement in 60 of the 82 subsequent expungement requests and denied eight. One of the granted requests relates to the previous request that was denied. Another of the granted requests relates to the previous request that was deficient and therefore not decided. Seven subsequent expungement requests were withdrawn or deficient and, therefore, not decided. In addition, seven subsequent expungement requests were still pending as of the end of the sample period. In 42 of the 82 subsequent expungement requests, the associated person was an unnamed party in the first arbitration.

a customer. Under the proposed rule change, an associated person would be prohibited from filing a straight-in request against a customer.

An arbitrator or panel made a decision in arbitrations relating to 3,722 of the 5,159 requests in arbitrations that closed, and made no decision in arbitrations relating to the remaining 1,437 requests. A single arbitrator made a decision in arbitrations relating to 2,692 of the 3,722 requests, and a two- or three-person panel made a decision in arbitrations relating to the remaining 1,030 requests. For the customer arbitrations, the decision by an arbitrator or panel may relate to the arbitration, an expungement request, or both. For the straight-in requests, the decision would relate to the expungement request only. In arbitrations where no decision on the merits of the customer case or an expungement request was made, the requests were either not eligible (as determined by the arbitrator or panel), withdrawn, or otherwise not pursued by the associated person or party that filed the request.

As detailed in the next paragraph, the percentage of expungement requests that are recommended is higher when the arbitrator or panel receives information only from the associated person or other party requesting expungement. The arbitrator or panel is likely to receive information only from the party requesting expungement when (1) the customer arbitration does not close by award after a hearing (e.g., settles), or (2) an associated person files a straight-in request against a member firm. In both circumstances, the customer and his or her representative have little incentive to participate in an expungement hearing.

Among the 3,722 expungement requests in arbitrations where an arbitrator or panel made a decision, 2,874 resulted in an arbitrator or panel recommending

expungement (77 percent). Among the 3,722 expungement requests, 976 requests were made during a non-simplified or simplified customer arbitration, and 2,746 requests were filed as a straight-in request. An arbitrator or panel recommended expungement in response to 595 of the 976 requests (61 percent) made during a customer arbitration. This includes 168 of the 369 requests (46 percent) made during a customer arbitration that closed by award after a hearing, and 427 of the 607 expungement requests (70 percent) made during a customer arbitration that closed by award without a hearing or other than by award. An arbitrator or panel recommended expungement in 2,279 of the 2,746 requests filed as a straight-in request (83 percent).<sup>169</sup>

A recommendation for expungement in FINRA arbitration is not the final step in the expungement process. If the arbitrator or panel recommends expungement, then the firm or associated person must confirm the arbitration award in a court of competent jurisdiction and serve the confirmed award on FINRA.<sup>170</sup> As of July 2020, FINRA had removed 2,641 customer dispute information disclosures from the CRD system from the possible 2,874 requests (92 percent) in which an arbitrator or panel recommended expungement. Firms or associated persons may have not yet sought or obtained a court order for the remaining disputes.

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<sup>169</sup> Among the 976 expungement requests during a non-simplified or simplified customer arbitration, a single arbitrator made a decision in arbitrations relating to 306 requests, and a two- or three-person panel made a decision in arbitrations relating to 670 requests. In addition, among the 2,746 straight-in requests, a single arbitrator made a decision in arbitrations relating to 2,386 requests and a two- or three-person panel made a decision in arbitrations relating to 360 requests. See infra note 190 for a discussion of the percentage of expungement requests recommended between two- or three-person panels and one-person panels.

<sup>170</sup> See supra note 10.

Approximately one-third of the 2,641 customer dispute information disclosures (965, or 37 percent) that were expunged were submitted to the CRD system from 2014 to 2019. The 965 customer dispute information disclosures reflect three percent of the total number of customer dispute information disclosures submitted to the CRD system during this period of time (approximately 37,000). The remaining 1,676 customer dispute information disclosures were submitted to the CRD system prior to 2014. The number of customer dispute information disclosures expunged during the sample period that were submitted to the CRD system prior to 2014 suggests that associated persons may yet still expunge customer dispute information disclosures submitted to the CRD system during or prior to the sample period. The three percent of expunged customer dispute information disclosures should therefore be considered a lower bound for the rate at which customer dispute information disclosures are expunged.

A firm or associated person can also initiate a proceeding directly in a court of competent jurisdiction without first going through any arbitration proceeding. From January 2016 through December 2019, the expungement of 138 customer dispute information disclosures were sought directly in court. As of July 2020, court proceedings had concluded for 118 of those disclosures and proceedings remained ongoing for 20 disclosures. Among the 118 disclosures for which the court proceeding had concluded, 86 disclosures were ordered expunged by a court and 32 disclosures were not ordered to be expunged. FINRA will challenge these requests in court in appropriate circumstances.

### 3. Economic Impact

#### A. Overview

The proposed rule change would codify the best practices described in the Guidance.<sup>171</sup> The best practices include the prohibition on the filing of an expungement request if (1) an arbitration panel or court of competent jurisdiction previously denied a request to expunge the same customer dispute information, or (2) the customer dispute information arises from a customer's arbitration that has not concluded. Based on FINRA staff observations, arbitrators are generally believed to be adhering to these best practices and, therefore, codifying them should not result in new material economic impacts. Codifying the best practices in the Guidance should, however, clarify among parties how the practices should be applied, including what is permitted during the expungement hearing and the responsibilities of the parties and the arbitrator or panel when expungement is requested. Codifying the Guidance may also help inform customers more generally of the practices that the forum has implemented to encourage and facilitate customer participation in expungement hearings. In addition, parties may incur fewer costs from the codification of the practices, including the costs from actions or decisions (e.g., requesting expungement of customer dispute information that was previously denied in another arbitration or court) that would be denied by an arbitration panel pursuant to the Guidance.

The proposed rule change would also introduce other changes to the Codes that expand upon or that are not a part of the Guidance. In particular, the proposed rule change would restrict when an associated person is permitted to request expungement in

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<sup>171</sup> See supra note 3.

FINRA arbitration. The proposed rule change would also require an arbitrator or panel from a customer arbitration that closes by award after a hearing, from a simplified customer arbitration, or a panel from the Special Arbitrator Roster to decide an expungement request. Finally, the proposed rule change would address the participation by associated persons and customers in expungement hearings. These changes may result in new material economic benefits and costs. These economic effects are discussed in further detail below.

B. Expungement Requests during Customer Arbitrations

The proposed rule change would set forth requirements for expungement requests during customer arbitrations. The proposed rule change would establish different requirements for non-simplified customer arbitrations and simplified customer arbitrations, and for an associated person named or unnamed to a (non-simplified or simplified) customer arbitration.

i. Expungement Requests by Named Associated Persons  
during Non-Simplified Customer Arbitrations

The proposed rule change would require an associated person named in a non-simplified customer arbitration to request expungement during the customer arbitration regarding the conduct that gave rise to the arbitration. Otherwise, the associated person would forfeit the opportunity to seek expungement of the same customer dispute information in any subsequent proceeding. The arbitrator or panel from a non-simplified

customer arbitration would decide an expungement request if the arbitration closes by award after a hearing.<sup>172</sup>

The proposed rule change would help ensure that, if possible, the arbitrator or panel from a non-simplified customer arbitration, with input from all parties and access to all evidence, testimony and other documents, would decide an expungement request. These arbitrators or panels would be best situated to decide the related issue of expungement, and thereby help ensure that expungement recommendations and the customer dispute information contained in the CRD system and displayed through BrokerCheck reflect the conduct of associated persons.

An associated person named in a non-simplified customer arbitration may lose the ability to request expungement of the customer dispute information arising from the arbitration. A named associated person who does not request expungement during a non-simplified customer arbitration (or within the required time) would lose the ability to seek expungement relief.<sup>173</sup> Because the named associated person may lose the ability to assess information that arises as a part of arbitration before they are required to request expungement, associated persons may incur costs to preserve their right to request expungement by filing a request with or without the expectation that the arbitrator or panel would recommend expungement. FINRA believes, however, that the proposed rule

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<sup>172</sup> See supra Item II.A.1.(II)A.1.a., “Expungement Requests During the Customer Arbitration, By a Respondent Named in a Customer Arbitration.”

<sup>173</sup> Under the proposed rule change, a party that does not file or serve an expungement request at least 30 days before the first scheduled hearing begins could file a motion seeking an extension. The motion, however, may be opposed by another party and denied.

change would mitigate these potential costs by providing associated persons a reasonable amount of time (i.e., within 45 days of receipt of the customer's statement of claim if the request is included in an answer, or 30 days before the first scheduled hearing begins if the request is included in a pleading) during the arbitration to consider whether to file a request. Parties may also incur other, indirect costs if, for example, the deadline to request expungement during a non-simplified customer arbitration causes them to incur costs to expedite the filing of the expungement request or constrains their ability to engage in other activities (i.e., incur opportunity costs).

ii. Expungement Requests during a Non-Simplified Customer Arbitration that Close other than by Award or by Award without a Hearing

Associated persons who request expungement during a non-simplified customer arbitration (either as a named party or as an unnamed party that consents to an on-behalf-of request) that closes other than by award or by award without a hearing (and would have otherwise had their expungement request decided as part of the customer arbitration) would incur additional costs to file a straight-in request.<sup>174</sup> Associated persons may incur delays in receiving a decision on the request, and may incur additional legal fees and forum fees to resolve the straight-in request. The member firms with which the associated persons were associated at the time the customer dispute arose

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<sup>174</sup> Associated persons who would otherwise request expungement as a counterclaim during an industry arbitration, which is rare, or who would otherwise intervene in a customer arbitration and have an expungement request decided during the arbitration, would instead be required to file a straight-in request under proposed Rule 13805. These associated persons and member firms with which the associated persons were associated would incur similar costs.

would also incur additional legal and forum fees. These costs would be imposed by the proposed rule change if the expungement requests would have otherwise been decided as part of the non-simplified customer arbitration. These costs would not be imposed by the proposed rule change, however, if regardless of the proposed rule change associated persons would have filed a straight-in request after the close of the non-simplified customer arbitration.

The additional costs for an associated person to resolve a straight-in request after the close of a non-simplified customer arbitration (that closes other than by award or by award without a hearing) may reduce the likelihood that the parties settle a customer arbitration.<sup>175</sup> In particular, the associated person may factor the cost to resolve a separate straight-in request into the decision regarding whether to settle the arbitration or have the case decided by the arbitrator or panel to the arbitration. In addition, even if the parties continue to settle the dispute, the associated person may subtract the cost to resolve a separate straight-in request from the potential settlement amount.

An associated person (or a party on behalf of an associated person) who files a straight-in request would incur the minimum hearing session fee of \$1,125 for each session the panel conducts to decide the expungement request.<sup>176</sup> The member firm at

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<sup>175</sup> FINRA notes, however, that the determination regarding whether to settle a customer arbitration can depend on a number of factors, including the parties' respective estimates of the additional costs they would incur to continue the customer arbitration, the value that the associated person places on expungement, the associated person's estimate of the likelihood that he or she could obtain expungement in the customer case compared to in a straight-in request and the cost that they estimate the associated person would incur to pursue the straight-in request.

<sup>176</sup> The associated person would not, however, incur an additional filing fee to file the straight-in expungement request. See infra Item II.C.8.

which the broker was associated at the time the customer dispute arose would also be assessed a minimum surcharge fee of \$1,900 and a minimum process fee of \$3,750. The fees associated with non-monetary claims would help ensure that costs to the forum for administering expungement requests are allocated as intended to the party or parties requesting expungement and, as applicable, the member firms at which the broker was associated at the time the customer dispute arose.

iii. Expungement Requests by Unnamed Persons in Non-Simplified Customer Arbitrations and by Named and Unnamed Persons in Simplified Customer Arbitrations

The proposed rule change would not require an unnamed person in a non-simplified customer arbitration, an associated person named in a simplified customer arbitration, or an unnamed person in a simplified customer arbitration to request expungement of the customer dispute information during the customer arbitration. Instead, similar to today, these associated persons may wait until after the customer arbitration has concluded to request expungement as a straight-in request.<sup>177</sup>

The option to wait until after the customer arbitration has concluded to request expungement is not a benefit created by the proposed rule change, but is instead currently permitted under the Codes. FINRA believes that an associated person who is not named in a non-simplified customer arbitration, or an associated person who is either named or not named in a simplified customer arbitration, should be able to seek expungement as a

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<sup>177</sup> This requirement would help ensure that the panel from the Special Arbitrator Roster is aware of the outcome of the arbitration when deciding the request.

straight-in request and have their request decided by a panel from the Special Arbitrator Roster.

Associated persons who are not required and choose not to request expungement during the customer arbitration may also incur additional costs. Any incremental costs from not filing an expungement request during a customer arbitration, however, are not imposed by the proposed rule change. Instead, they are borne at the discretion of the parties who make the determination of when to request expungement, and are similar to the costs they would incur under the Codes today.

iv. Time Limit for Requesting Expungement in Simplified and Non-Simplified Customer Arbitrations

A named associated person or a party on-behalf-of an unnamed person would be required to request expungement in a simplified customer arbitration within 30 days of the date that FINRA provides notice of arbitrator appointment.<sup>178</sup> A named associated person or a party requesting expungement on-behalf-of an unnamed person in a non-simplified customer arbitration would be required to request expungement no later than 30 days before the first scheduled hearing.<sup>179</sup>

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<sup>178</sup> The proposed rule change would require that if the named associated person or party on-behalf-of an unnamed person requests expungement in a pleading other than an answer, the request must be filed within 30 days after the date FINRA provides the associated person with notice of arbitrator appointment, which is the last deadline provided to the parties in a simplified arbitration to submit additional documents before the case is submitted to the arbitrator. See proposed Rules 12800(d)(1)(B)(i) and 12800(d)(2)(B)(i).

<sup>179</sup> See proposed Rules 12805(a)(1)(C)(i) and 12805(a)(2)(C)(iii). The proposed rule change also provides that FINRA would notify state securities regulators, in the manner determined by FINRA, of an expungement request within 30 days of receiving a complete request for expungement. See proposed Rule 12805(b). State securities regulators would, therefore, have additional time to review the

Associated persons who do not request expungement within these time limits may incur additional costs that may include costs arising from delays in receiving a decision on the request and legal and forum fees. The member firms with which the brokers were associated at the time the customer dispute arose would also incur additional legal and forum fees. These costs would be imposed by the proposed rule change.

#### C. Time Limits for Filing Straight-in Requests

The proposed rule change would also set forth requirements for an associated person to file a straight-in request. For customer dispute information reported to the CRD system after the effective date of the proposed rule change, the proposed rule change would require an associated person to file a straight-in request within two years of a customer arbitration or civil litigation closing, or, if no customer arbitration or civil litigation, within six years from the initial reporting of the customer complaint to the CRD system.<sup>180</sup>

The proposed rule change would also require a two-year time limit for requests to expunge customer dispute information that arose from a customer arbitration or civil litigation that closed on or prior to the effective date of the proposed rule change or a six-year time limit to request expungement of customer dispute information arising from a customer complaint initially reported to the CRD system on or prior to the effective date

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request and decide whether to oppose expungement if confirmation of an expungement recommendation is later sought in court.

<sup>180</sup> See proposed Rules 13805(a)(2)(A)(iv) and 13805(a)(2)(A)(v).

of the proposed rule change.<sup>181</sup> These time limits would begin from the effective date of the proposed rule change.

Arbitrators on the Special Arbitrator Roster would have the experience, qualifications and training necessary to decide straight-in requests. These time limits may increase customer participation in the proceedings and the likelihood that the panel from the Special Arbitrator Roster receives the relevant evidence and testimony to decide an expungement request. The time limits would help ensure that the expungement hearing is held close in time to the customer arbitration or civil litigation, or the events that led to the customer dispute information disclosure, and foreclose the option of an associated person to choose the timing of a straight-in request to potentially reduce the likelihood of customer participation. Similar to other amendments proposed herein, an increase in customer participation may provide a panel from the Special Arbitrator Roster with additional information to decide an expungement request and help ensure the accuracy of the customer dispute information contained in the CRD system and displayed through BrokerCheck.

These time limits, however, may constrain an associated person from filing a straight-in request.<sup>182</sup> Associated persons who would otherwise delay the filing of a straight-in request may incur additional costs to file a straight-in request within the

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<sup>181</sup> See proposed Rules 13805(a)(2)(B)(i) and 13805(a)(2)(B)(ii).

<sup>182</sup> If the Commission approves the proposed rule change, FINRA expects that a number of associated persons would file a straight-in request to expunge customer dispute information reported to the CRD system prior to or soon after the effective date of the proposed rule change to help ensure that they are not constrained from seeking expungement because of the proposed time limitations.

required time limits (e.g., opportunity costs, as described above). These time limits may also constrain an associated person from filing more than one expungement request in the same straight-in request. For example, associated persons may lose the ability to delay the filing of a straight-in request to expunge a complaint from a particular customer until other customers make additional complaints, if the filing of the straight-in request to expunge the complaint of the first customer would be time barred. Instead, an associated person may be required (as a result of the time limits) to file more than one straight-in request.

Associated persons who are restricted from including more than one request to expunge customer dispute information in the same straight-in request would incur additional legal and forum fees for each straight-in request or not seek expungement for all of the disclosures. The member firm at which the associated person was associated at the time the customer disputes arose would incur additional legal and forum fees if the associated person were to file multiple, separate straight-in requests.

#### D. Time Limits for Straight-in Requests – Quantitative Description

As discussed as part of the Economic Baseline, 3,725 expungement requests were filed as straight-in requests during the sample period. The following estimates demonstrate that the majority of these straight-in requests would not have been permitted under the proposed time limits, and associated persons may not have been able to include more than one expungement request in the same straight-in request. The estimates, however, do not take into account the potential change in the behavior of associated persons; associated persons would have incentive under the proposed amendments to file

the straight-in requests within the time limits or otherwise lose the ability to make or file a request.<sup>183</sup>

Among the 3,725 expungement requests filed as a straight-in request, 1,140 requests followed a (non-simplified or simplified) customer arbitration (of the same underlying dispute). Two-hundred ninety of the 1,140 requests (25 percent) were filed as a straight-in request within the two-year time limit and would have been permitted under the proposed rule change. The remaining 850 requests (75 percent) were filed as a straight-in request after the two-year time limit and would not have been permitted. The median time from the close of the customer arbitration to the filing of the straight-in request was six years.

The 3,725 expungement requests filed as a straight-in request also include 2,585 requests that did not follow a (non-simplified or simplified) customer arbitration (of the same underlying dispute). Among the 2,585 requests, 813 requests (31 percent) were filed as a straight-in request within six years from the initial reporting of the disclosure to the CRD system and would have been permitted under the proposed rule change. The remaining 1,772 requests (69 percent) were filed as a straight-in request after the six-year time limit and would not have been permitted.

As discussed above, more than one expungement request can be made in a single arbitration, and the time limits may limit the ability of an associated person to include multiple expungement requests in the same straight-in request. The 3,725 expungement

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<sup>183</sup> The following estimates also do not take into account the number of straight-in requests of customer dispute information arising from a previous (non-simplified or simplified) customer arbitration which, under the proposed rule change, may have been decided as part of the customer arbitration.

requests filed as a straight-in request relate to 1,778 arbitrations. Associated persons included more than one request to expunge customer dispute information in 810 of the 1,778 arbitrations. Under the proposed time limits, associated persons would not have been able to include all expungement requests in at least 225 of the 810 arbitrations.

E. Arbitrators or Panels Deciding Expungement Requests

The proposed rule change would require that the arbitrator or panel from a non-simplified customer arbitration decide expungement requests during the arbitration if the arbitration closes by award after a hearing.<sup>184</sup> In addition, the proposed rule change would require the arbitrator from a simplified customer arbitration to decide expungement requests if there is a full hearing, or in a separate expungement-only hearing after the simplified arbitration closes if the arbitration is decided “on the papers” or in a special proceeding.<sup>185</sup> The proposed rule change would also require a randomly selected panel from the Special Arbitrator Roster to decide straight-in requests.<sup>186</sup>

The proposed rule change is not structured to increase or decrease the likelihood that an arbitrator or panel recommends expungement in any individual hearing except as it relates to the merits of the request. The proposed rule change is structured, however, to place an arbitrator or panel in a better position to determine whether to recommend expungement of customer dispute information, and thereby help ensure the accuracy of the customer dispute information contained in the CRD system and displayed through

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<sup>184</sup> See proposed Rules 12805(a)(1)(D)(i) and 12805(a)(2)(E)(i).

<sup>185</sup> See proposed Rule 12800(e)(1).

<sup>186</sup> See proposed Rule 13806(b)(1).

BrokerCheck. Under the proposed rule change and in general, the arbitrator or panel that decides a request would either hear the full merits of the customer case or have additional training and qualifications when they are likely to receive information only from the party requesting expungement. In addition, panels from the Special Arbitrator Roster would be able to request evidence from the member firm at which the associated person was associated at the time the customer dispute arose

The proposed rule change is also structured to reduce the potential influence of associated persons and member firms on the selection of the arbitrator or panel that decides an expungement request. First, a panel from the Special Arbitrator Roster would be randomly selected to decide a straight-in request, thereby decreasing the extent to which an associated person and member firm with which the associated person was associated at the time the customer dispute arose may together select arbitrators who are more likely to recommend expungement.<sup>187</sup>

Second, the proposed rule change would foreclose the option for an associated person to withdraw a request and seek expungement of the same customer dispute information in a subsequent arbitration.<sup>188</sup> Associated persons may exercise this option if

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<sup>187</sup> See supra Item II.A.1.(II)B.2.b., “Straight-in Requests and the Special Arbitrator Roster, Composition of the Panel.”

<sup>188</sup> This includes the requirement for an unnamed person to provide written consent to an on-behalf-of request for it to proceed, thereby preventing an unnamed person from subsequently arguing that they were unaware of an expungement request on their behalf. See proposed Rule 12805(a)(2)(A). This also includes the requirement that a case be closed with prejudice if an associated person withdraws a straight-in request after a panel from the Special Arbitrator Roster is appointed (unless the panel decides otherwise). See proposed Rule 13805(a)(4). In the sample period, an associated person withdrew 155 of the 2,904 straight-in requests (five percent) filed in cases that closed. The 155 straight-in requests include 118 requests where an arbitrator or panel was appointed.

they believe that they have a higher probability of obtaining an expungement recommendation with a different arbitrator or panel in another arbitration, and in particular if the associated person files a straight-in request against the member firm with which the broker was associated at the time the customer dispute arose. To the extent that the associated person and his or her employer's interests are aligned and both seek to increase the likelihood that expungement is recommended, they would together be expected to select arbitrators who may be more likely to recommend expungement.<sup>189</sup> Though these proposed amendments are consistent with the regulatory intent to permit expungement in limited circumstances, it may decrease the likelihood that associated persons are able to obtain an award recommending expungement.

In general, under the proposed rule change, a three-person panel would consider and decide expungement requests during non-simplified customer arbitrations that close by award after a hearing and straight-in requests. Expungement decisions by a three-person panel may differ from expungement decisions by a single arbitrator. In addition, the decisions may differ depending on the arbitrators selected and the interaction among

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<sup>189</sup> A recent academic study finds evidence that suggests parties can use previous expungement decisions to predict the potential likelihood that an arbitrator would recommend expungement. See Colleen Honigsberg & Matthew Jacob, "Deleting Misconduct: The Expungement of BrokerCheck Records," November 2018, <https://www-cdn.law.stanford.edu/wp-content/uploads/2018/11/SSRN-id3284738.pdf>. The study also finds evidence that suggests both successful and unsuccessful expungement attempts predict future broker misconduct. An unsuccessful expungement attempt is associated with an approximately four times higher probability of future misconduct. Although expungement decisions are based on the information available at the time of the request, including the facts and circumstances of the arbitration, this finding suggests that the decisions being made by arbitrators are related to the potential future harm posed by the requesting broker.

the arbitrators when deciding an expungement request. The extent to which a three-person panel would decide an expungement request differently than a single arbitrator, however, is not known.<sup>190</sup> As discussed above, expungement requests may be complex to resolve, particularly straight-in requests where customers typically do not participate in the expungement hearing. Thus, having three arbitrators available to ask questions, request evidence and to serve generally as fact-finders in the absence of customer input would help ensure that a complete factual record is created to support the arbitrators' decision in such expungement hearings.

#### F. Arbitrators or Panels Deciding Expungement Requests – Quantitative Description

As discussed as part of the Economic Baseline, 5,159 of the 6,928 expungement requests sought during the sample period were filed in an arbitration that closed. Among the 5,159 expungement requests, 4,521 requests (88 percent) would have required a panel from the Special Arbitrator Roster. The 4,521 requests include 2,456 expungement requests made during a non-simplified customer arbitration that closed by award without a hearing or other than by award, and 2,065 requests that were filed as a straight-in

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<sup>190</sup> Among the 2,746 expungement requests filed as a straight-in request where an arbitrator or panel made a decision, a similar percentage of requests was recommended by a two- or three-person panel (306 of 360 requests, or 85 percent) as was recommended by a one-person panel (1,973 of 2,386 requests, or 83 percent). In addition, among the 976 expungement requests during a non-simplified or simplified customer arbitration where an arbitrator or panel made a decision, a similar percentage of requests was recommended by a two- or three-person panel (422 of 670 requests, or 63 percent) as was recommended by a one-person panel (173 of 306 requests, or 57 percent).

request but did not relate to a previous (non-simplified or simplified) customer arbitration.

An arbitrator or panel from a (non-simplified or simplified) customer arbitration would have been required to decide 590 of the 5,159 expungement requests (11 percent). The 590 expungement requests include 292 requests made during a non-simplified customer arbitration that closed by award after a hearing, 240 expungement requests made during a simplified customer arbitration, and 58 requests filed as a straight-in request to expunge customer dispute information arising from a previous non-simplified customer arbitration that closed by award after a hearing.

Finally, a panel from the Special Arbitrator Roster, or an arbitrator from a simplified customer arbitration, would have been required to decide the remaining 48 arbitration requests that relate to customer dispute information arising from a previous simplified customer arbitration. The arbitrator or panel that would have decided the request is dependent on whether an associated person, or a party on-behalf-of an associated person, would have requested expungement during the simplified arbitration.

#### G. Participation in Expungement Hearings

The proposed rule change would require an associated person to appear personally at an expungement hearing.<sup>191</sup> This requirement would provide the arbitrator or panel the opportunity to ask questions of an associated person to better assess his or her credibility. An associated person would be permitted to cross-examine and seek

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<sup>191</sup> See proposed Rules 12805(c)(2) and 13805(c)(2).

information from customers who testify.<sup>192</sup> This may provide associated persons with the opportunity to substantiate their arguments in support of their expungement request.

Associated persons may incur additional costs to appear at an expungement hearing. The additional costs may depend on the method of appearance (i.e., by telephone, videoconference, or in person), which, under the proposed rule change, would be determined by the arbitrator or panel. For example, associated persons who would otherwise not appear in person may incur additional costs under the proposed rule change if they are so required. The additional costs include the time and expense to appear, and other direct and indirect costs (e.g., opportunity costs) associated with the associated person's appearance.

The proposed rule change would also help encourage customer participation in an expungement hearing. As noted above, the proposed rule change would require that a named associated person request expungement during a non-simplified customer arbitration and that the arbitrator or panel decide the expungement request if the arbitration closes by award after a hearing. In addition, an expungement request during a non-simplified customer arbitration would be considered and decided by the arbitrator or panel from that arbitration.

Further, the proposed time limits for filing straight-in requests may increase customer participation during these arbitrations. The proposed rule change would also provide customers the option to appear at an expungement hearing using whichever method is convenient for them. The proposed rule change would also codify elements of the Guidance that permit the customer to testify, cross-examine the associated person and

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<sup>192</sup> See proposed Rules 12805(c)(5)(A) and 13805(c)(5)(A).

other witnesses, present evidence at the hearing and make opening and closing arguments.<sup>193</sup>

#### H. Impact on Business and Professional Opportunities

As a result of the proposed rule change, associated persons may determine that the additional costs to seek expungement relief are higher than the anticipated benefits. In addition, although the proposed rule change is intended to help ensure arbitrators recommend expungement when appropriate as it relates to the merits of the request, an arbitrator or panel may be less likely to recommend expungement depending on the information that becomes available for the reasons described above. This may cause associated persons not to seek expungement where expungement is likely (or unlikely) to be recommended.

Associated persons who no longer seek, or are not able to expunge customer dispute information from the CRD system and its display through BrokerCheck, or are delayed in doing so, may experience a loss of business and professional opportunities. The loss of business and professional opportunities by one associated person, however, may be the gain of another. Associated persons who may benefit in this regard include those who still determine that the additional costs to seek expungement relief under the

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<sup>193</sup> Other amendments to the proposed rule change would also help encourage customer participation. For example, the proposed rule change would allow customers to be represented at an expungement hearing and thereby mitigate any potential concern they may have regarding a direct confrontation with the associated person. In addition, the proposed rule change provides that FINRA would notify the customer of the time and place of the expungement hearing. Customers would still retain the option to participate in the expungement hearing or provide their position on the expungement request in writing. The costs to participate would therefore be borne at the customers' discretion.

proposed rule change is less than the anticipated benefits and continue to seek expungement of customer dispute information, and other associated persons who do not have similar disclosures.

A firm or associated person can also initiate an expungement proceeding directly in a court of competent jurisdiction without first going through any arbitration proceeding. The proposed rule change may incent firms or associated persons to initiate an expungement proceeding directly in a court of competent jurisdiction without first going through any arbitration proceeding. For some firms and associated persons, the anticipated costs to first go through arbitration may be greater than the similar costs to proceed directly in a court of competent jurisdiction. Firms and associated persons who would otherwise first go through arbitration as a result of the proposed rule change may incur additional costs to seek expungement relief.

The number of firms or associated persons who would instead initiate an expungement proceeding directly in a court of competent jurisdiction is dependent not only on the additional costs under the proposed rule change, but the costs a firm or associated person would expect to incur in the different forums to initiate an expungement proceeding. This information is generally not available, and accordingly the potential effect of the proposed rule change on direct-to-court expungement requests is uncertain.

#### I. Other Economic Effects

Finally, the proposed rule change may have other marginal economic effects. First, the prohibition of a subsequent expungement request would decrease the potential inefficient allocation of resources resulting from a subsequent request that would have

resulted in the same decision (i.e., denial) as the first. The resources of the forum allocated to the additional expungement request could instead be used for other claims or requests that were not previously adjudicated or for other purposes.<sup>194</sup>

Second, the proposed rule change may increase the efficiency of the forum by requiring that a party provide certain information when filing an expungement request. The information includes identification of the customer dispute information that is the subject of the request, and whether expungement of the same customer dispute information was previously requested and, if so, how it was decided. This would increase the efficiency of the forum by enabling FINRA to identify and track a request through the expungement process, and by alerting arbitrators and FINRA to another expungement request of the same customer dispute information. The efficiency of the forum would also increase by requiring an unnamed person to consent to an on-behalf-of expungement request in writing. This would help ensure that an unnamed person is aware of the request and prevent another expungement request by the unnamed person of the same customer dispute information.

In addition, the proposed rule change may affect the value of the customer dispute information to describe the conduct of associated persons. The change in the value of the information depends on the merit of the disclosures that would have otherwise been expunged. The merit of these disclosures also depends on many factors which are difficult to predict. These factors include the incentive of parties to file an expungement request under the proposed rule change, the decisions by the arbitrator or panel to

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<sup>194</sup> The resources relate to the specific costs to administer the claim, as well as the overall attendant costs to administer the forum.

recommend expungement dependent on the information that is available, and the merit of the customer dispute information that would have otherwise been sought to be expunged.

As stated above, the proposed rule change is not structured to increase or decrease the likelihood that an arbitrator or panel recommends expungement in any individual hearing except as it relates to the merits of the request. The proposed rule change may, however, reduce the incentive for an associated person to request expungement even when warranted. The effect of the proposed rule change on the extent to which the customer dispute information available in the CRD system (and its public display through BrokerCheck) accurately describes the conduct of associated persons is, therefore, uncertain.

#### 4. Alternatives Considered

Alternatives to the proposed rule change include amendments that were proposed in Notice 17-42. Notice 17-42 proposed to restrict when a party can file or serve an expungement request during a customer arbitration to 60 days before the first hearing session begins. Although 60 days would provide a customer with more time to address an expungement request, 60 days may further restrict a party from seeking expungement during a customer arbitration relative to the 30 days before the first scheduled hearing begins in the proposed rule change. FINRA believes that the proposed 30-day period would provide customers with enough time to address an expungement request, and FINRA with sufficient time to notify the states of the request. FINRA also believes that 30 days would reduce the potential that parties would lose their ability to file an expungement request during an arbitration.

Notice 17-42 also proposed that an arbitrator or panel find that the customer dispute information has “no investor protection or regulatory value,” and that there must be a unanimous rather than a majority decision by a panel to recommend expungement. These proposed amendments may increase the difficulty for an associated person to receive an expungement recommendation, and thereby deter an associated person from seeking expungement. After considering the comments, FINRA has determined not to propose that the panel must find “no investor protection or regulatory value” to recommend expungement. FINRA agrees with some commenters that the standard may, if codified into rule language, create confusion among arbitrators and the potential for inconsistent application among different arbitrators and panels.<sup>195</sup> A majority decision is also consistent with what is required for other decisions in customer and industry arbitrations. FINRA also believes that the overall proposal, coupled with the existing standards in FINRA Rule 2080, would be sufficient to help preserve in the CRD system information that is valuable to investors and regulators, while allowing associated persons to remove information that is inaccurate.

Another alternative to the proposed rule change includes different time limits for an associated person to file a straight-in request. Although shorter (longer) time limits

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<sup>195</sup> FINRA notes that in its Order approving NASD Rule 2130 (now FINRA Rule 2080), which describes the current findings that arbitrators must make to recommend expungement, the SEC stated that “it believes the proposal strikes the appropriate balance between permitting members and associated persons to remove information from the CRD system that holds no regulatory value, while at the same time preserving information on the CRD system that is valuable to investors and regulators.” See Securities Exchange Act Release No. 48933 (December 16, 2003) 68 FR 74667, 74672 (December 24, 2003) (Order Approving File No. SR-NASD-2002-168).

may increase (decrease) customer participation in the proceedings and the likelihood that the panel from the Special Arbitrator Roster receives the relevant evidence and testimony to decide an expungement request, shorter (longer) time limits may further (less) constrain an associated person from filing a straight-in request or including more than one expungement request in the same straight-in request. FINRA believes that the time limits proposed herein would facilitate customer participation but also provide associated persons sufficient opportunity to file a straight-in request.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

In December 2017, FINRA published Notice 17-42, requesting comment on proposed amendments to the expungement process including establishing a roster of arbitrators with additional training and specific backgrounds or experience from which a panel would be selected to decide an associated person's request for expungement of customer dispute information. The arbitrators from this roster would decide expungement requests where the customer arbitration is not resolved on the merits or the associated person files a straight-in request to expunge customer dispute information. FINRA received 70 comments in response to Notice 17-42.<sup>196</sup> A copy of Notice 17-42 is attached as Exhibit 2a. A list of comment letters received in response to Notice 17-42 is attached as Exhibit 2b and copies of the comment letters are attached as Exhibit 2c.

In general, individual commenters supported some aspects of the proposal and raised concerns with others. A summary of the comments and FINRA's responses are discussed below.

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<sup>196</sup> All references to commenters are to the comment letters as listed in Exhibit 2b.

1. Requirement to Request Expungement during a Customer Arbitration

In Notice 17-42, FINRA proposed that an associated person who is named as a party in a customer arbitration must request expungement during the arbitration or be prohibited from seeking to expunge the customer dispute information arising from the customer's statement of claim during any subsequent proceeding under the Codes.

NASAA and PIABA supported the proposed limitation. NASAA stated that the limitation would help ensure timelier expungement requests and help avoid requests made years after the underlying customer arbitration has closed. PIABA stated that it did not believe that requiring associated persons to request expungement during the customer arbitration would result in more expungement requests because the rule proposal contained "heightened standards applicable to expungement requests" and a "clear process for requesting expungement following the close of the customer case," which may cause "associated persons [to] be more deliberate in making expungement requests."

Some commenters opposed the limitation for a variety of reasons.<sup>197</sup> Cornell stated that it "could lead associated persons to request expungement in every dispute in order to preserve the right to request expungement." Keesal stated that these additional expungement requests could result in increased expenses to associated persons and member firms and "could impede the goals of protecting investors and ensuring that FINRA arbitration remains an expedient and cost-effective forum." Herskovits expressed a concern that an associated person "may be unaware of the important rights he is

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<sup>197</sup> See Behr, Cornell, Herskovits, JonesBell, Keesal and Saretsky.

waiving by failing to file a request for expungement in the underlying arbitration.”

Saretsky, responding to FINRA’s concern that customers and documents may be unavailable when an associated person files a separate expungement request years after the customer arbitration closed, stated that customers can be located through counsel or internet searches, and that securities industry rules mandate the retention of important customer and account records for several years. JonesBell and Behr stated that the requirement to request expungement during the customer arbitration should apply only to named associated persons who have also appeared in the arbitration.

FINRA believes that requiring an associated person who is named in a customer arbitration to request expungement during that arbitration or be prohibited from doing so should help limit expungement requests filed years after the customer arbitration concludes, facilitate customer participation in expungement hearings and help ensure that relevant evidence does not become stale or unavailable.<sup>198</sup> The proposed requirement would also help ensure that the panel that has heard the merits of the customer’s claim at a hearing would decide the expungement request. Accordingly, FINRA believes that all associated persons who are named in non-simplified arbitrations should be required to request expungement during the arbitration, and that the requirement should not depend on whether the associated person has chosen to enter an appearance in response to the complaint. In addition, FINRA notes that if the named associated person requests expungement, under the proposed rule change, the associated person would be required to appear at the expungement hearing.

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<sup>198</sup> See supra Item II.B.3.D., “Time Limits for Straight-in Requests – Quantitative Description.”

The proposed amendments would also provide a detailed framework governing the expungement process, which should help ensure that both associated persons and customers are aware of their rights.

FINRA acknowledges commenters' concerns that the proposed limitation could potentially result in an increase in the number of expungement requests and their associated costs. To address this concern, as well as the related concern that the requirement could result in expungement requests by associated persons simply to preserve their right to request expungement, FINRA has modified the proposed rule to allow the associated person to make the request 30 days before the hearing in the customer arbitration.<sup>199</sup> This should provide sufficient time during the customer arbitration for the associated person to evaluate whether an expungement request is warranted and help avoid unnecessary expungement requests.

2. Deadline to File Expungement Request during a Customer Arbitration

In Notice 17-42, FINRA proposed that an expungement request made in a pleading during a customer arbitration must be made no later than 60 days before the first hearing session begins. Three commenters opposed the proposal, stating that the 60-day filing deadline was an impractical or unnecessary restriction that could cause an associated person to miss the deadline and, therefore, an opportunity to file a request.<sup>200</sup> These commenters suggested that the proposal retain the status quo, which allows an

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<sup>199</sup> See supra Item II.A.1.(II)A.1.a.i., “Method of Requesting Expungement.”

<sup>200</sup> See Behr, JonesBell and SIFMA.

associated person to request expungement up to and during any hearing. One commenter, Keesal, supported a deadline of 60 days before the first scheduled hearing date, provided, however, that the associated person “has appeared in [the] Underlying Customer Case.” Keesal stated that this would “ensure[] that all participants” were “on notice of the issues to be addressed and determined at the evidentiary hearing.” SIFMA stated that the proposed requirement “to file for expungement 60 days prior to the first scheduled hearing date” was impractical and would require the payment of expungement fees even though a large portion of cases settle within 60 days of the hearing.

After considering the comments, FINRA does not believe that it is necessary to require a 60-day filing deadline. Instead, the proposed rule change would require that an expungement request be filed no later than 30 days before the first scheduled hearing.<sup>201</sup> This should provide the parties with sufficient case preparation time, as the expungement issues will overlap with the issues raised by the customer’s claim. If a named associated person seeks to request expungement after the 30-day filing deadline, the panel would be required to decide whether to grant an extension and permit the request.<sup>202</sup> The purpose of the deadline is to provide the parties other than the associated person with sufficient notice that expungement will be addressed at the hearing.

In addition, FINRA has determined that requiring the party to request expungement at least 30 days before the first “hearing session,” which is typically the initial pre-hearing conference (“IPHC”) rather than the first hearing on the merits, may not provide the requesting party with sufficient time to make an informed decision about

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<sup>201</sup> See supra Item II.A.1.(II)A.1.a.i., “Method of Requesting Expungement.”

<sup>202</sup> See supra note 37.

whether to request expungement.<sup>203</sup> Therefore, FINRA has modified the proposal to require that an expungement request must be made 30 days before the first scheduled “hearing” begins to provide time for the requesting party to make a better-informed decision.<sup>204</sup>

3. Panel from the Customer Arbitration Decides Expungement Requests Where the Customer Arbitration Closes by Award after a Hearing

In Notice 17-42, FINRA proposed that if the customer arbitration closes by award, the panel from the customer arbitration would consider and decide the expungement request during the customer arbitration.

Some commenters disagreed with this aspect of the proposal and suggested that a panel selected from the Special Arbitrator Roster should decide all expungement requests, even if the customer arbitration was decided by an award.<sup>205</sup> For example, PIABA stated that a panel from the Special Arbitrator Roster should decide the expungement request separate from the customer’s claim because the “decision a panel is

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<sup>203</sup> The term “hearing session” means any meeting between the parties and arbitrator(s) of four hours or less, including a hearing or a prehearing conference. See FINRA Rules 12100(p) and 13100(p). The IPHC is scheduled after the panel is appointed. During the IPHC, the panel will set discovery, briefing, and motions deadlines, schedule subsequent hearing sessions, and address other preliminary matters. The parties may agree, however, to forgo the IPHC. See generally FINRA Rules 12500 and 13500.

<sup>204</sup> Under the Codes, a “hearing” means a hearing on the merits. See supra note 21.

<sup>205</sup> See AdvisorLaw, Georgia State, Grebenik, PIABA, St. John’s, Tinklenberg and UNLV. In addition, St. John’s “strongly agree[d] with requiring associated or unnamed persons to wait until the conclusion of a customer’s case to file an expungement request.”

asked to make with respect to expungement is different than deciding whether or not to find liability on a customer claim” and because it is “unfair to require a customer to participate in a potentially lengthy expungement hearing that they did not ask for.” Grebenik stated that the expungement request should be evaluated separately by an independent panel because the arbitrator may “have bias” and “has heard comments and issues from the customer [about] the actual claim.” AdvisorLaw stated that all expungement requests should receive the “same level of review and consideration by a specially trained arbitration panel.”

Cornell expressed a concern that the proposed requirement could “transform hearings designed to determine the merits of a customer dispute into lengthy expungement hearings.” Cornell proposed, as an alternative, that the same panel from the customer arbitration make the expungement determination, but do so in a separate proceeding to avoid inconveniencing the customer.

Keesal questioned whether the proposed requirement that the panel from the customer arbitration decide the expungement request if the customer arbitration “closes by award” would require the panel to decide an expungement request if the cases closes as a result of an order dismissing the case.

In response to the comments, FINRA is clarifying that the panel from the customer arbitration would be required to decide the expungement request and include its decision in the award if the arbitration “closes by award after a hearing” instead of where the arbitration “closes by award.” FINRA believes that where the panel from the customer arbitration has heard the parties’ presentation of the evidence about the customer’s claim, that same panel is best situated to decide the expungement request. In

addition, it would generally be more efficient and less costly for the panel from the customer arbitration to decide the expungement request in these circumstances. Although FINRA Rule 2080(b)(1) requires the panel to make a separate, different determination than its determination on the merits of the customer's claim, the evidence offered with respect to both determinations should generally overlap. Accordingly, FINRA does not believe that it would overly burden the parties if, when the customer arbitration closes by award after a hearing, the panel must also decide the expungement request in addition to the merits of the customer's claim.

#### 4. Qualifications of Arbitrators on the Special Arbitrator Roster

In Notice 17-42, FINRA proposed that to qualify for the Special Arbitrator Roster, a public chairperson would be required to: (i) have completed enhanced expungement training; (ii) be admitted to the practice of law in at least one jurisdiction; and (iii) have five years' experience in litigation, federal or state securities litigation, administrative law, service as a securities regulator or service as a judge. Commenters generally supported the proposed requirements,<sup>206</sup> but were split on whether the members of the Special Arbitrator Roster should be required to be attorneys.<sup>207</sup> One commenter, Black, did not oppose the proposed qualifications but suggested that they would likely

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<sup>206</sup> See, e.g., SIFMA (supporting the proposal, and stating that more highly qualified and trained arbitrators should lead to a more efficient and fair process); NASAA (supporting the proposal, and stating that the extent to which the panels truly appreciate the nuanced regulatory issues related to expungement largely depended on the content and effectiveness of the proposed enhanced expungement training).

<sup>207</sup> See AdvisorLaw, FSI, Gocsek, Keesel, Osiason, Rodriguez and White (all opposing the requirement that members of the Special Arbitrator Roster be attorneys). But cf. Cornell, Georgia State, NASAA, PIABA, Schlein, SIFMA, St. John's and Tinklenberg (all supporting the requirement).

result in fewer eligible arbitrators for straight-in requests. PIABA stated that the Special Arbitrator Roster should be made up of attorneys because it would be difficult for FINRA, in some areas of the country, to alternatively fill the Special Arbitrator Roster with local chair-qualified arbitrators that had served on three arbitrations through award. PIABA also stated that arbitrators with legal training may be better equipped to make the distinction between the FINRA Rule 2080 grounds for expungement and deciding the merits of the underlying claim. Keesal, in contrast, stated that there was no rationale for allowing non-attorneys to decide expungement requests made during the customer arbitration, but not brought as a stand-alone claim.

Some commenters also expressed concerns that the arbitrators on the Special Arbitrator Roster were not required to have securities industry experience.<sup>208</sup> FSI stated that without this background “it may be difficult to appreciate whether information has regulatory significance or investor protection value.” AdvisorLaw stated that “[r]equiring all expungement arbitrators to have a minimum of five years’ experience with the financial services industry [would be] appropriate considering the complexity of expungement requests in cases involving customer dispute information.” In contrast, Public Citizen suggested that at least one FINRA employee who meets the requirements

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<sup>208</sup> See AdvisorLaw, Behr, FSI and JonesBell. Behr and JonesBell also criticized the proposal as allowing claimants’ attorneys “whose business is the ligation of customer complaints” to serve on the Special Arbitrator Roster. FINRA notes, however, that the proposal requires that arbitrators on the Special Arbitrator Roster be public arbitrators, and that FINRA’s definition of public arbitrators excludes, among other persons, those who devote 20 percent or more of their professional time to representing parties in disputes concerning investment accounts or transactions, or employment relationships within the financial industry. See FINRA Rules 12100(aa) and 13100(x); see also *supra* note 8.

of the Special Arbitrator Roster be a member of every three-person panel that considers an expungement request.

After considering the comments, FINRA has determined not to propose requiring that the members of the Special Arbitrator Roster be attorneys; instead, they would be required to be public arbitrators who have evidenced successful completion of, and agreement with, enhanced expungement training, and have served as an arbitrator through award on at least four customer-initiated arbitrations.<sup>209</sup> FINRA believes that the non-attorneys on its roster who meet these qualifications and complete enhanced expungement training should be appropriately knowledgeable and experienced to decide straight-in requests. The requirement that the arbitrators on the Special Arbitrator Roster be public arbitrators should help ensure that the arbitrators are free of bias. The requirement that they have served on four cases through to award would help ensure that the members of the Special Arbitrator Roster have the necessary knowledge and experience to conduct hearings in the forum.

Although FINRA believes that a sufficient number of arbitrators on its roster would meet these additional qualifications, if the Commission approves the proposed rule change, FINRA would engage in efforts to recruit arbitrators for the Special Arbitrator Roster. FINRA notes that its Office of Dispute Resolution has embarked on an aggressive campaign to recruit new arbitrators, with a particular focus on adding arbitrators from diverse backgrounds, professions and geographical locations.<sup>210</sup>

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<sup>209</sup> See proposed Rule 13806(b)(2)(B). In addition, to qualify for the Special Arbitrator Roster, the arbitrators must be chairpersons and, therefore, will have completed the training that arbitrators must complete before they can be added to the chairperson roster. See also supra note 80.

<sup>210</sup> See Our Commitment to Achieving Arbitrator and Mediator Diversity at FINRA,

FINRA's commitment and focus on this critical initiative have resulted in increases in under-represented categories of arbitrators.<sup>211</sup> FINRA believes its continued commitment to this important initiative will help the forum improve the quality, depth and diversity of its public chairperson roster.

5. Special Arbitrator Roster Decides Expungement Requests if the Customer Arbitration Closes other than By Award or By Award Without a Hearing

In Notice 17-42, FINRA proposed that if the customer arbitration closes other than by award (e.g., the parties settle the arbitration), the panel in that arbitration would not decide the associated person's expungement request. Instead, the associated person would be permitted to file an expungement request as a new claim under the Industry Code against the member firm at which he or she was associated at the time of the events giving rise to the customer dispute.

The SEC Investor Advocate supported the proposal because FINRA's data showed that where the arbitration case was not decided on the merits, the expungement rate was "simply too high for an extraordinary remedy." (emphasis in original). NASAA also supported the proposal, stating that "post-settlement expungement hearings often consist of a one-sided presentation of the facts" because "investors and their counsel have little incentive to participate after the customer's concerns have been resolved."

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<https://www.finra.org/arbitration-mediation/our-commitment-achieving-arbitrator-and-mediator-diversity-finra>.

<sup>211</sup> See supra note 210.

Some commenters disagreed with the proposal to require the associated person to file a new arbitration under the Industry Code if the customer arbitration closes other than by award, as inefficient or burdensome on associated persons.<sup>212</sup> As an alternative, SIFMA suggested that the panel from the customer arbitration decide the request; but, to address FINRA's concern for greater training and increased qualifications for those arbitrators determining expungement, SIFMA suggested that the proposed rule change require that at least one arbitrator on every three-person panel be selected from the Special Arbitrator Roster at the inception of each customer arbitration.

Saretsky stated that associated persons should be able to name the customer, and that the "minor inconvenience" to the customer was outweighed by the harm to the associated person. PIABA stated that it would be "inappropriate" to name customers. St. John's "support[ed] allowing the proposed expungement process to proceed without the customer having to be named a party to the request."

Schlein expressed concerns that a former employing member firm may have "little or no economic incentive to cooperate in an expungement proceeding," and that it "would also be difficult for the panel to elicit potentially relevant facts" where the "economic and reputational interests of the associated person and the employer are aligned." Schlein also stated that an "aggrieved customer has no economic incentive to

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<sup>212</sup> See Behr, Herskovits, JonesBell, Saretsky and SIFMA. Herskovits also stated that "[financial advisors] will respond to the proposed rule by filing a counterclaim or cross claim for expungement in the customer arbitration, thus preventing the customer arbitration from closing before a hearing is held on expungement or the [financial advisors'] other claims for relief." FINRA notes, however, that under the proposed rule change, a request for expungement relief would not prevent a customer arbitration from closing.

participate in an expungement proceeding that occurs only after the underlying case has concluded.” Schlein also expressed concern that expungement requests would be referred to the Special Arbitrator Roster even if the matter settled on the eve of hearing, when it may be more efficient and promote investor protection to require the existing panel to hear the expungement request. Schlein stated that “FINRA could ameliorate the possibility that a panel might receive one-sided information” by (i) providing the expungement panel with significant filings from the underlying customer dispute, (ii) permitting the panel to review the parties’ settlement papers and (iii) giving the associated person, firm, and the customer the right to provide the panel with transcripts of the underlying customer proceeding.

FINRA believes that where there has not been a hearing on the merits of the customer’s claim, the members of the Special Arbitrator Roster, who would be public chairpersons who have served on at least four customer arbitrations in which a hearing was held and received enhanced expungement training, would be better situated to decide expungement requests than the panel from the customer arbitration. FINRA does not believe that requiring the associated person to file a new arbitration under the Industry Code would unduly burden the associated person—instead of presenting evidence related to the expungement request to the arbitrators in the customer arbitration in a separate expungement hearing, they would instead present the evidence supporting the expungement request to a panel randomly selected from the Special Arbitrator Roster.

FINRA shares commenters’ concerns that the factual record could be less well-developed where a straight-in request is filed against a member firm and the associated person or member firm’s interests are aligned, or where the customer does not participate.

FINRA does not believe, however, that the customer should be named as a respondent or be required to participate in an expungement proceeding after the customer's claim has been resolved (e.g., after the claim is settled). Instead, the proposed rule change addresses concerns that straight-in requests filed against the member firm may be non-adversarial or lack customer participation by, among other things (i) requiring that straight-in requests be decided by three randomly selected public chairpersons with enhanced training and experience,<sup>213</sup> (ii) requiring the panel to review the settlement documents,<sup>214</sup> (iii) granting the panel the explicit authority to request from the associated person, the member firm at which he or she was associated at the time the customer dispute arose or other party requesting expungement, any documentary, testimonial or other evidence that it deems relevant to the expungement request,<sup>215</sup> and (iv) including provisions to encourage and facilitate customer participation in expungement hearings.<sup>216</sup>

In response to commenters' concerns, FINRA has modified the language in the proposed rule change to require that a straight-in request be filed against the member firm at which he or she was associated "at the time the customer dispute arose," consistent with the language used in other FINRA rules, instead of "at the time of the events giving rise to the customer dispute."<sup>217</sup>

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<sup>213</sup> See supra Item II.A.1.(II)B.2.b., "Straight-in Requests and the Special Arbitrator Roster, Composition of the Panel."

<sup>214</sup> See proposed Rules 12805(c)(7) and 13805(c)(7).

<sup>215</sup> See proposed Rules 12805(c)(6) and 13805(c)(6).

<sup>216</sup> See supra Item II.A.1.(II)D.3., "Customer's Participation during the Expungement Hearing."

<sup>217</sup> See, e.g., FINRA Rules 12901(a)(1)(C) and 13903(b); see also Kessal.

6. Three Randomly Selected Arbitrators Decide Straight-in Requests

In Notice 17-42, FINRA proposed that the NLSS would randomly select three public chairpersons to serve on the Special Arbitrator Roster who would decide the request for expungement, and that the first arbitrator selected would be the chairperson. The parties would not be permitted to agree to fewer than three arbitrators or to the use of pre-selected arbitrators. The associated person seeking expungement would not be permitted to strike any arbitrators, but would be able to challenge a selected arbitrator for cause.

PIABA and AdvisorLaw supported the proposed random selection of three arbitrators. PIABA stated that the random selection of three arbitrators would “reduce the risk of arbitrators being concerned about ruling against an associated person for fear they may not be selected for another panel.”

Other commenters opposed the proposed rule change. SIFMA expressed concerns that not permitting parties to rank and strike arbitrators would remove the parties’ involvement and input.<sup>218</sup> SIFMA also stated that there was no compelling need to use three rather than a single arbitrator, and that the proposal would increase the financial burden on registered representatives seeking expungement. Walter stated that a single FINRA-qualified arbitrator with the special qualifications would be “more than

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<sup>218</sup> SIFMA also proposed that “to preserve arbitrator neutrality and foster greater transparency,” FINRA make publicly available all training materials, communications with arbitrators regarding expungement, and documents related to the addition, removal or exclusion of any arbitrators from the roster. FINRA notes that making such communications and documents publicly available could have a chilling effect on arbitrator recruitment and communications. FINRA does, however, make expungement training materials publicly available. See supra note 82.

qualified to make a determination as to expungement” and that “[h]aving to coordinate the schedules of three arbitrators will delay the processing and will impose unnecessarily high additional costs on all parties involved.”<sup>219</sup> Tinklenberg opposed the three-person panel requirement because of the associated costs. Baritz stated that the three-person panel requirement would increase expenses to associated persons and the “time necessary to rank and choose a panel,” and “significantly delay the process.”

Keesal opposed the random selection of three arbitrators as unfair to associated persons, and suggested that FINRA “randomly select a minimum of 12 proposed arbitrators to serve on an expungement case, from which the associated person and anyone else involved in the case can rank and strike the proposed panelists.”

FINRA notes that since straight-in requests may be complex, may not be actively opposed by another party and the customer or customer’s representative typically does not appear at the hearing, having three arbitrators from the Special Arbitrator Roster available to ask questions and request evidence would help ensure that a complete factual record is developed to support the arbitrators’ decision. In addition, FINRA believes that requiring two out of three randomly selected public chairpersons with enhanced training and qualifications to agree that expungement is appropriate in straight-in requests should help FINRA maintain the integrity of its CRD records and ensure that expungement is recommended in limited circumstances and only when one of the FINRA Rule 2080(b)(1) grounds applies.

FINRA does not believe that selecting three rather than one arbitrator would overly burden the parties during the proceeding or result in undue delay. As the parties

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<sup>219</sup> See also Saretsky.

would not be permitted to rank or strike these arbitrators, this should shorten the average length of the proceeding.<sup>220</sup> In addition, pursuant to FINRA Rule 13403, FINRA would send the lists generated by the NLSS to all parties at the same time, within approximately 30 days after the last answer is due, regardless of the parties' agreement to extend any answer due date.

FINRA recognizes that the proposed random arbitrator selection process would limit party input on arbitrator selection. However, the arbitrators on the Special Arbitrator Roster would have the experience, qualifications and training necessary to conduct a fair and impartial expungement hearing in accordance with the proposed rules, and to render a recommendation based on a complete factual record developed during the expungement hearing. FINRA believes that the higher standards that the arbitrators must meet to serve on the Special Arbitrator Roster should mitigate the impact of the absence of party input on the selection of arbitrators. In addition, associated persons and member firms would still be permitted to challenge any arbitrator for cause.<sup>221</sup>

#### 7. Simplified Arbitrations

In Notice 17-42, FINRA proposed to require that an associated person or unnamed person wait until the conclusion of a customer's simplified arbitration case to file an expungement request, which would be filed under the Industry Code against the

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<sup>220</sup> Under the Codes, the lists of ranked arbitrators must be completed and returned to the Director no more than 20 days after the date the Director sends the lists to the parties. See, e.g., FINRA Rules 12403(c)(3) and 13404. However, the parties may agree to extend the due date. See FINRA Rules 12105 and 13105.

<sup>221</sup> See proposed Rule 13806(b)(4).

member firm at which he or she was associated at the time the customer dispute rose and would be heard by a panel selected from the Special Arbitrator Roster.

Some commenters supported the proposal.<sup>222</sup> PIABA stated that it would address a flaw in the current process, whereby a hearing is held to consider expungement even if the customer has not requested a hearing under FINRA Rule 12800, and that it would eliminate delays in securing an award because the arbitrator is considering the request for expungement. PIABA also stated that a single arbitrator should not be permitted to decide an expungement request in a simplified arbitration because the goals of the proposed amendments should not be affected simply because the misconduct involved \$50,000 or less.<sup>223</sup> The SEC Investor Advocate stated that it would be easier for a broker to convince one arbitrator to recommend expungement. St. John's stated that "separating the expungement request from the underlying customer case" should result in "faster decisions in simplified cases."

Some commenters opposed the proposed change and stated that the arbitrator who heard the evidence in the underlying simplified customer arbitration would be most qualified to determine an expungement request, and that it was unfair to impose the burden of a subsequent arbitration on the associated person in this circumstance.<sup>224</sup>

After considering the comments, FINRA has revised the proposed rule change to provide that if a party requests expungement during a simplified arbitration, the single arbitrator from the simplified arbitration would be required to decide the expungement

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<sup>222</sup> See NASAA, PIABA, The SEC Investor Advocate, St. John's and UNLV.

<sup>223</sup> See also UNLV.

<sup>224</sup> See Behr, JonesBell and Keesal.

request, regardless of how the simplified arbitration case closes (e.g., even if the case settles).<sup>225</sup> FINRA believes that it is appropriate for the single arbitrator in a simplified arbitration case to decide expungement requests, regardless of how the underlying case closes, due to the lower monetary requirement and generally less complex nature of these cases. To address concerns that customers should not be required to participate in a hearing addressing expungement requests in simplified arbitrations, the proposed rule change would require arbitrators to hold a separate expungement-only hearing after the customer's dispute is decided to consider the expungement request if the customer elects to have his or her claim decided on the papers or through an Option Two special proceeding. The arbitrator would be required to issue a subsequent, separate award in connection with the expungement-only hearing.<sup>226</sup>

8. Fees that Parties Will Incur to File a New Claim Under the Industry Code to Request Expungement

Some commenters expressed concerns that if an associated person were required to file a separate claim under the Industry Code to request expungement after the customer arbitration closes other than by award, the member firm and associated person would be assessed the filing fee, member surcharge and process fees twice, in both the underlying customer arbitration and the separate straight-in request.<sup>227</sup> SIFMA stated that this could increase the costs of expungement and have the “indirect effect of increasing

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<sup>225</sup> See proposed Rule 12800(e)(1).

<sup>226</sup> See proposed Rule 12800(e)(1)(A).

<sup>227</sup> See Janney, Keesal and SIFMA.

the costs of settlement, potentially discouraging settlement in smaller cases due to the increased costs associated with expungement.”

FINRA believes that it is appropriate to assess the member surcharge and process fee for straight-in requests because they are separate arbitrations before a separate panel of specially trained arbitrators. The member firm, having not previously paid a member surcharge and process fee for the expungement request, would be assessed these fees when and if a straight-in request is filed. FINRA would not, however, assess a second filing fee when an associated person files a straight-in request if the associated person, or the requesting party if it is an on-behalf-of request, has previously paid the filing fee to request expungement of the same customer dispute information during a customer arbitration.

9. Arbitrators “Recommend” Rather than “Grant” Expungement

In Notice 17-42, FINRA requested comment on whether to revise FINRA Rules 12805 and 13805 to state that the panel may “recommend” rather than “grant” expungement if the FINRA Rule 2080 standards are satisfied. Several commenters supported the revision as a clarifying change that would more accurately reflect the panel’s role in the expungement process.<sup>228</sup> For example, PIABA stated that after the panel recommends expungement, under FINRA Rule 2080 the member or associated person “must obtain an order from a court of competent jurisdiction confirming the arbitration award containing expungement relief.” AdvisorLaw and Tinklenberg opposed the proposed rule change, with AdvisorLaw stating that “grant” should be retained because “[i]t has long been established that the decisions made in arbitration are final and

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<sup>228</sup> See Black, Cornell, Georgia State, Gocek, Keesal and PIABA.

binding upon the parties,” and that “[c]hanging the language of the Rule from the word ‘grant’ to ‘recommend’ may lessen the perceived binding effect of the decision.”<sup>229</sup>

FINRA believes that “recommend” more accurately captures the panel’s authority in the expungement process. Pursuant to FINRA Rule 2080, FINRA will only expunge customer dispute information after a court of competent jurisdiction enters an order requiring it to do so. Accordingly, the proposed rule change would change the word “grant” to “recommend” in proposed Rules 12805 and 13805.<sup>230</sup>

#### 10. Unanimity of Decision

In Notice 17-42, FINRA proposed that to recommend expungement, a three-person panel of arbitrators would be required to agree unanimously to recommend expungement. Some commenters opposed the unanimity requirement as making it too difficult to obtain expungement or because it was inconsistent with the ability of a customer to prevail by a majority decision.<sup>231</sup> SIFMA, for example, stated that the unanimity requirement would “impinge upon the fundamental fairness of the expungement process in providing an effective balance to the allegation-based complaint reporting regime and will have a significant impact on registered representatives’ ability to protect their livelihoods and reputations.” JonesBell and Behr stated that “[t]o require a unanimous decision on any expungement request obviously would give a single individual sitting on a three-member panel the power to prevent, for improper reason or

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<sup>229</sup> See also Wellington.

<sup>230</sup> See supra note 10.

<sup>231</sup> See AdvisorLaw, Behr, Gocsek, Hagenstein, Higgenbotham, Janney, JonesBell, Keesal, Leven, Mahoney, Saretsky, SIFMA, Smart, Speicher, Tinklenberg and White.

no good reason at all, a meritorious request that a false or erroneous claim be removed from a representative's CRD record."

Other commenters supported requiring a unanimous decision to recommend expungement.<sup>232</sup> For example, PIABA stated that the unanimity requirement would help ensure that expungement was an extraordinary remedy that is only granted when it has no meaningful investor protection or regulatory value. The SEC Investor Advocate stated that the requirement would provide greater "assurance that only meritless complaints are expunged," and expressed hope "that this requirement will encourage brokers to only seek expungement when the underlying customer dispute information is meritless." Cornell stated that the "unanimity requirement protects public investors by ensuring that the threshold for expungement is high," and that, "given the history of abuse of the expungement process," would "help[] to ensure that when expungement is granted, the expungement is legitimate."

After considering the comments, FINRA has determined to allow arbitrators to recommend expungement through a majority decision, consistent with what is required for other decisions in customer and industry arbitrations.<sup>233</sup> FINRA believes that requiring a majority of arbitrators to agree that expungement is appropriate should be sufficient to help preserve in the CRD system information that is valuable to investors and regulators, while allowing associated persons a reasonable mechanism to remove

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<sup>232</sup> See Black, Cornell, Georgia State, Liebrader, NASAA, PIABA, Public Citizen, The SEC Investor Advocate and UNLV. In addition, Wellington stated that if an expungement was endorsed unanimously, the term "grant" should be retained, there should be little or no cost to the requesting party, and the associated person should not have to obtain a court order directing the expungement.

<sup>233</sup> See FINRA Rules 12904(a) and 13904(a).

information that is inaccurate. FINRA notes, however, that if the SEC approves the proposed rule change, FINRA will continue to monitor the expungement process to determine if additional changes are needed.

11. No Investor Protection or Regulatory Value

In Notice 17-42, FINRA proposed to require that a panel find that customer dispute information has “no investor protection or regulatory value” to recommend expungement. Several commenters opposed the requirement.<sup>234</sup> For example, Herskovits stated that the standard was vague and opened the possibility of inconsistent rulings among different panels. FSI stated that the proposal was “confusing as it is difficult to imagine a scenario where information that is false, clearly erroneous, factually impossible or did not involve the advisor, would have regulatory or investor protection value.” SIFMA stated that the requirement was redundant in light of the current high standards in FINRA Rule 2080(b)(1), may have the effect of discouraging meritorious expungement claims, was already incorporated into the Guidance and would transform the traditional role of arbitrators as fact-finders and require them to make a policy determination in each case. Keesal stated that the change would unnecessarily complicate the expungement process to the detriment of associated persons with no corresponding investor protection value. Saretsky proposed that arbitrators instead be required to find that the customer dispute had no “reasonable” investor protection or regulatory value.

NASAA expressed a concern with the proposal because it would allow arbitrators, rather than regulators, to make the finding. The SEC Investor Advocate expressed the

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<sup>234</sup> See Baritz, FSI, Gocek, Herskovits, Janney, Keesal, Saretsky, SIFMA and White.

same concern, and suggested that FINRA provide a framework on how the standard should be interpreted and applied to avoid disparate interpretations and outcomes. Schlein stated that arbitrators “should receive supplemental training on the proposed new standard,” and that FINRA should also “offer training or instructional materials to judges” who will be required to confirm an expungement award.

Other commenters supported the requirement.<sup>235</sup> For example, PIABA suggested that arbitrators should be required to make the finding because in practice arbitration panels “often believe that the Rule 2080 standards are easily met” and “do not grasp the fact that” a claim may not be factually impossible or false even though a customer has not met his or her burden of proof for purposes of establishing liability or rebutting an affirmative defense. St. John’s stated that the proposed requirement would “help strengthen investor protection by improving confidence in the accuracy of the CRD system and BrokerCheck.” Cornell stated that the requirement would allow the panel to look beyond the claim and at the associated person's record as a whole, including other customer dispute information, which would protect public investors. Liebrader stated that “[t]oo many legitimate claims disappear from public view in the largely uncontested expungement process.”

After considering the comments, FINRA has determined not to propose that the panel must find “no investor protection or regulatory value” to recommend expungement. FINRA agrees with some commenters that the standard may, if codified into rule language, create confusion among arbitrators and the potential for inconsistent

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<sup>235</sup> See Cornell, Liebrader, PIABA, St. John’s and UNLV.

application among different arbitrators and panels.<sup>236</sup> FINRA also believes that the overall proposal, coupled with the existing standards in FINRA Rule 2080, would be sufficient to help preserve in the CRD system information that is valuable to investors and regulators, while allowing associated persons to remove information that is inaccurate.

12. Panel Must Identify One of the FINRA Rule 2080(b)(1) Grounds for Expungement

In Notice 17-42, FINRA clarified in proposed Rules 12805 and 13805 that the FINRA Rule 2080 grounds for expungement that the panel must identify to recommend expungement are the grounds stated in paragraph (b)(1) of FINRA Rule 2080. In response to Notice 17-42, PIABA supported clarifying “that an arbitration panel may not recommend expungement on grounds other than those set forth in Rule 2080.” Keesal, however, viewed FINRA’s proposal as “remov[ing] the arbitrator’s ability to grant expungement relief based on judicial or arbitral findings other than those listed in Rule 2080(b)(1).”<sup>237</sup>

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<sup>236</sup> FINRA notes that in its Order approving NASD Rule 2130 (now FINRA Rule 2080), which describes the current findings that arbitrators must make to recommend expungement, the SEC stated that “it believes the proposal strikes the appropriate balance between permitting members and associated persons to remove information from the CRD system that holds no regulatory value, while at the same time preserving information on the CRD system that is valuable to investors and regulators.” See Securities Exchange Act Release No. 48933 (December 16, 2003) 68 FR 74667, 74672 (December 24, 2003) (Order Approving File No. SR-NASD-2002-168).

<sup>237</sup> See also Baritz; compare SIFMA (stating that “FINRA already imposes high standards in order for arbitrators to recommend expungement,” and that “FINRA Rule 2080(b)(1) requires a finding either that: (i) the claim or allegation is factually impossible or clearly erroneous; (ii) the registered person was not

FINRA notes that under current FINRA Rule 12805, arbitrators are required to base their expungement recommendations on one of the three grounds listed in FINRA Rule 2080(b)(1).<sup>238</sup> Accordingly, the proposed rule change clarifies in proposed Rules 12805 and 13805 that the grounds for expungement that the panel must indicate in its award are the grounds in FINRA Rule 2080(b)(1).<sup>239</sup>

### 13. Time Limits for Straight-in Requests

In Notice 17-42, FINRA proposed that for customer arbitrations, associated persons must file straight-in requests within one-year from the date the customer arbitration closed. For customer complaints, FINRA proposed that associated persons must file straight-in requests within one-year from the date that a member firm initially reported the complaint to the CRD system. For customer arbitrations that close and customer complaints that are reported prior to the effective date of the proposed rule change, the associated person would have six months from the effective date of the rule, if approved by the Commission, to file the expungement request.

Some commenters opposed the proposed time limitations as unwarranted or too short.<sup>240</sup> For example, SIFMA stated that the one-year time limitation is unnecessary

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involved in the alleged sales practice violation, forgery, theft, misappropriation or conversion of funds, or (iii) the claim, allegation, or information is false”).

<sup>238</sup> See Regulatory Notice 08-79 (December 2008) (stating that “[t]he arbitration panel must indicate which of the grounds for expungement under Rule 2130(b)(1)(A)–(C) serve as the basis for their expungement order, and provide a brief written explanation of the reasons for ordering expungement”).

<sup>239</sup> See proposed Rules 12805(c)(8) and 13805(c)(8).

<sup>240</sup> See AdvisorLaw, Barber, Baritz, Behr, Brookes, FSI, Glenn, Grebenik, Herskovits, Higgenbotham, JonesBell, Keesal, Leven, Saretsky, SIFMA, Smart, Speicher, Stephens and Walter.

because the general six-year period to file all claims also applies to expungement requests. SIFMA also stated that the one-year time limitation is insufficient for firms to properly investigate and respond to customer complaints, and would create inefficiency by requiring the filing of requests to expunge customer complaints that would then be stayed if they evolved into an arbitration. SIFMA also requested “further guidance on the extended time period that will be afforded registered representatives who have eligible claims for expungement that would become ineligible if the rule proposals were implemented.”<sup>241</sup> JonesBell and Behr stated that an associated person may be unaware that a member firm “has reported a customer complaint on his or her CRD.”<sup>242</sup> FSI stated that associated persons should have three years to file expungement requests to provide them with time to assess how the information will impact their business, which may not be immediately apparent. Keesal stated that because customers may wait up to six years to file an arbitration claim under FINRA Rule 12206 after making a customer complaint, the proposed time limits would be unfair and would increase the frequency of requests, as the associated person would have to make a second expungement request if the customer complaint was later the subject of an arbitration claim. Saretksy stated that the time restriction was unnecessary because arbitrators are “free to weigh the evidentiary value (if any) of an associated person’s undue delay.” Herskovits stated that FINRA’s concern about document retention was “misplaced” because SEC and FINRA rules “generally

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<sup>241</sup> See also AdvisorLaw (stating that providing six months where the customer arbitration closes on or prior to the effective date of the proposed rule change was arbitrary and creates an unjustifiable distinction between cases that close prior to the rules and those that close after).

<sup>242</sup> See supra note 48.

mandate the preservation of most records for 3 to 6 years (and many firms preserve documents for longer periods of time).” Grebenik expressed concerns with the proposed time limits because there were “thousands of advisors who have customer disputes and do not know about the expungement process.”

Other commenters supported the time limits.<sup>243</sup> For example, UNLV stated that the proposed time limit would ensure “that relevant evidence is available and increases investors’ ability to participate.” In response to other commenters’ suggestion that brokers may not be aware of a customer complaint, Cornell stated that “public investors should not be penalized for the failure of firms to implement streamlined notification and recordkeeping procedures,” and that “it is not too much to ask that the associated person follow up as to disposition by the firm.”

PIABA “strongly support[ed] a definite cut-off date for requests for expungement,” and stated that a customer is “far more likely to participate in an expungement hearing when it takes place in close proximity to the resolution of the underlying arbitration proceeding.” PIABA also stated that a more stringent time limit would lead to higher quality evidence, which becomes less reliable and available with the passage of time. PIABA stated that when the arbitration results in an award, a shorter timeframe of 90 days is preferable because significant time will already have passed from the filing of the customer’s arbitration claim, and because 90 days matches the deadline to file a motion to vacate an arbitration award under the Federal Arbitration Act. PIABA also stated that, because member firms and associated persons control the date that information is reported in the CRD system, the time limit for customer complaints should

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<sup>243</sup> See Cornell, Georgia State, PIABA, Public Citizen and Schlein.

run from the shorter of the date the firm initially reported the complaint in the CRD system or a month after the associated person receives notice of the complaint.

After considering the comments, FINRA believes that adjustments to the originally proposed time limitations are warranted to provide sufficient time for associated persons to determine whether to seek expungement of customer dispute information. Accordingly, FINRA has revised the proposal to provide for a two-year period to file an expungement request when a customer arbitration or civil litigation that gives rise to customer dispute information closes.<sup>244</sup> The two-year period would help ensure that the expungement hearing is held close in time to the customer arbitration or civil litigation, when information regarding the customer arbitration is available and in a timeframe that would increase the likelihood for the customer to participate if he or she chooses to do so. At the same time, it would allow the associated person time to determine whether to seek expungement.

For customer complaints where no customer arbitration or civil litigation gave rise to the customer dispute information, the proposed rule change would provide for six years from the date that the customer complaint was initially reported to the CRD system for the associated person to file the expungement request.<sup>245</sup> Six years would allow firms time to complete investigations of customer complaints and close them in the CRD system and for the complaints to evolve, or not evolve, into an arbitration. Thus, the revised proposal would help avoid unnecessary duplicative requests to expunge customer complaints that subsequently evolve into arbitrations or civil litigations, while providing

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<sup>244</sup> See proposed Rule 13805(a)(2)(A)(iv).

<sup>245</sup> See proposed Rule 13805(a)(2)(A)(v).

reasonable time limits to encourage customer participation and help ensure the availability of evidence. The proposed six-year time limitation is also consistent with FINRA's general eligibility rule, which provides that no claim shall be eligible for submission to arbitration under the Code where six years have elapsed from the occurrence or event giving rise to the claim.<sup>246</sup>

The proposed rule change makes similar revisions to the time limits described in Notice 17-42 to seek to expunge customer dispute information that arose prior to the effective date of the proposed rule change. For customer dispute information arising from customer arbitrations or civil litigations that closed on or prior to the effective date of the proposed rule change, the expungement request would be required to be made within two years of the effective date of the proposed rule change.<sup>247</sup> For customer complaints initially reported to the CRD system on or prior to the effective date of the proposed rule change, where no customer arbitration or civil litigation gave rise to the customer dispute information, the expungement request would be required to be made within six years of the effective date of the proposed rule change.<sup>248</sup>

#### 14. Effect of Withdrawal of Expungement Request

In Notice 17-42, FINRA proposed that if the associated person withdraws an expungement request after the panel is appointed in a straight-in request, the case would be closed with prejudice, unless the panel decides otherwise. AdvisorLaw supported the proposal, stating that it would “create safeguards, and prevent an associated person from

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<sup>246</sup> See supra note 14.

<sup>247</sup> See proposed Rule 13805(a)(2)(B)(i).

<sup>248</sup> See proposed Rule 13805(a)(2)(B)(ii).

simply withdrawing their case and refile in hopes of drawing a more favorable pool of randomly selected arbitrators.”

Under the proposed rule change, for expungement requests during customer arbitrations and straight-in requests, if the associated person withdraws or does not pursue the expungement request (or the party, with the written consent of the unnamed person, withdraws or does not pursue the request), the panel would be required to deny the expungement request with prejudice.<sup>249</sup> These requirements would foreclose the ability of associated persons withdrawing expungement requests to avoid having their requests decided by the panel, and then seeking to re-file the request and receive a new list of arbitrators and a potentially more favorable panel and decision.

15. Associated Person’s Appearance Required at the Expungement Hearing

In Notice 17-42, FINRA proposed that an associated person seeking to have his or her CRD record expunged would be required to appear at the expungement hearing either in person or by video conference. Five commenters supported the proposal, stating generally that this would allow the arbitrators to better assess the associated person’s demeanor and credibility.<sup>250</sup> UNLV also stated that requiring videoconferencing would carry minimal costs given its widespread availability at FINRA’s regional offices and other venues. NASAA stated that the broker should be required to appear in-person, “given the extraordinary relief the broker is seeking.” Georgia State also supported requiring an associated person to appear in person at the hearing, and stated that

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<sup>249</sup> See proposed Rules 12805(a)(1)(D)(i), 12805(a)(2)(E)(i) and 13805(a)(4).

<sup>250</sup> See Black, Caruso, Cornell, PIABA and UNLV.

appearance by video conference should only “be permitted, if at all, in those simplified cases where a hearing did not take place.”

Six commenters preferred to allow the associated person to appear by telephone.<sup>251</sup> SIFMA, for example, stated that there appeared to be no basis for allowing customers, but not associated persons, to appear by telephone, and that the proposal would “greatly increase the cost of expungement through attendant travel costs and loss of productivity.” Three commenters stated that the arbitrators should decide the method of appearance.<sup>252</sup> White, for example, stated that telephonic testimony “might be acceptable in limited circumstances,” and suggested that “arbitrators can make this determination and the Rule should not limit their flexibility to do so.”

After considering the comments, the proposed rule change would allow the panel to determine the method of appearance by the associated person—by telephone, in person or by video conference.<sup>253</sup> As the associated person is requesting the permanent removal of information from his or her CRD record, FINRA believes the associated person should personally participate in the expungement hearing to respond to questions from the panel and those customers who choose to participate. Rather than restrict the method of appearance, the panel would have the authority to decide which method of appearance would be the most appropriate for the particular case.<sup>254</sup> FINRA believes that providing

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<sup>251</sup> See Baritz, Gocek, Grebenik, Keesal, SIFMA and Tinklenberg.

<sup>252</sup> See AdvisorLaw, Robbins and White.

<sup>253</sup> See proposed Rules 12805(c)(2) and 13805(c)(2).

<sup>254</sup> See supra note 253.

flexibility as to the method of appearance would encourage appropriate fact-finding by the arbitrators and generally strengthen the process.

16. Customer Notification

In Notice 17-42, FINRA proposed that when an expungement request is filed separately from the customer arbitration, FINRA would notify the parties from the customer arbitration or the customer who initiated the complaint that is the subject of the request about the expungement request. PIABA supported the proposed customer notification requirement. Georgia State recommended “additional notifications to the investor about the expungement hearing.”

The proposed rule change modifies the proposal in Notice 17-42 to add an additional notification to help ensure that customers receive timely notice of both the expungement request and the expungement hearing. The associated person would be required to serve all customers whose customer arbitrations, civil litigations and customer complaints gave rise to customer dispute information that is a subject of the expungement request with notice of the request by serving on the customers a copy of the statement of claim requesting expungement before the first scheduled hearing session is held.<sup>255</sup> The Director would then notify the customers of the time, date and place of the expungement hearing using the customers’ current address provided by the party seeking expungement.<sup>256</sup>

17. Customer Participation during the Expungement Hearing

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<sup>255</sup> See proposed Rule 13805(b)(1)(A); see also supra note 134.

<sup>256</sup> See proposed Rule 13805(b)(2); see also supra note 137.

In Notice 17-42, FINRA proposed that, consistent with the Guidance, all customers in the customer arbitration or who filed a customer complaint would be entitled to appear at the expungement hearing. At the customer's option, the customer could appear by telephone.

In response to Notice 17-42, PIABA and The SEC Investor Advocate stated that FINRA should codify all of the customer rights provided in the Guidance, including, for example, allowing the customer or their counsel to introduce documents and other evidence and to cross-examine the broker or other witnesses called by the broker seeking expungement.<sup>257</sup>

FINRA agrees that the customer rights contained in the Guidance should be codified, as reflected in the proposed rule change.<sup>258</sup> In addition to incorporating the customer rights contained in the Guidance, the proposed rule change also clarifies that the customer may be represented and states that the customer may appear at the expungement hearing by telephone, in person, or by video conference. In addition, if a customer testifies, the associated person or other person requesting expungement would be allowed to cross-examine the customer. If the customer introduces any evidence at the expungement hearing, the associated person or party requesting expungement could object to the introduction of the evidence, and the panel would decide any objections. The proposed rule change would allow and encourage customers to participate fully in

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<sup>257</sup> See also St. John's.

<sup>258</sup> See proposed Rules 12805(c) and 13805(c).

the expungement hearing, while providing the associated person with a reasonable opportunity to rebut evidence introduced by the customer.<sup>259</sup>

18. State Notification

In response to Notice 17-42, NASAA requested “earlier notices to state regulators of an expungement request to better facilitate regulator involvement where appropriate.”<sup>260</sup> The proposed rule change provides that FINRA would notify state securities regulators, in the manner determined by FINRA, of the associated person’s expungement request within 30 days after receiving a complete request for expungement, so that the states are timely notified of the request.<sup>261</sup>

19. Unnamed Persons

In Notice 17-42, FINRA proposed to codify the ability of a party in a customer arbitration to request expungement on behalf of an unnamed person. AdvisorLaw stated that it opposed the practice and suggested that FINRA prohibit it entirely as there would be an “inherent conflict” of interest for the firm’s counsel because the interest of the member (who is the counsel’s client) and the associated person rarely align. AdvisorLaw also suggested that the associated person’s consent may be compromised “in the likely

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<sup>259</sup> In response to the Notice 17-42, White stated that if the customer chooses to object to the expungement request, “it would be helpful if it was mandated that the customer participate in the hearing or file a substantive statement or brief opposing expungement.” Schlein stated that FINRA should consider requiring the associated person to “bear the cost of the customer’s attendance if the customer wishes to participate in person.” FINRA believes that these requirements would be unduly burdensome and, therefore, has determined not to propose them as requirements.

<sup>260</sup> See also The SEC Investor Advocate.

<sup>261</sup> See proposed Rules 12805(b) and 13805(b)(3).

scenario where the member firm is providing financial assistance for the legal representation, as the associated person may agree under financial duress.” NASAA supported codifying the practice, but noted that it would “require cooperation between firms and their associated persons” and that FINRA would have to develop “robust, mandated notification procedures.”<sup>262</sup>

FINRA notes that under the proposed rule change, filing an on-behalf-of request would be permissive, not mandatory. In addition, FINRA would require the party and the unnamed person to sign a form consenting to the on-behalf-of request to help ensure that the unnamed person is fully aware of the request and that the firm is agreeing to represent the unnamed person for the purpose of requesting expungement during the customer arbitration, regardless of how the arbitration closes.<sup>263</sup>

20. No Interventions by Associated Persons to Request Expungement

In Notice 17-42, FINRA proposed to foreclose the option of an unnamed person to intervene in a customer arbitration to request expungement. Keesal opposed this proposal, stating that intervention “often can be economical, given that the evidence on the merits (or lack thereof) of the customer’s complaint will be presented at the evidentiary hearing and that same evidence will provide the basis for expungement relief.”<sup>264</sup>

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<sup>262</sup> See NASAA (noting support for this change along with the proposal in the Notice 17-42 that would prevent an unnamed associated from filing an arbitration claim seeking expungement against an investor).

<sup>263</sup> See proposed Rules 12805(a)(2)(C)(ii) and 12805(a)(2)(D).

<sup>264</sup> See also Behr and JonesBell.

FINRA believes that where no party to the arbitration has filed a claim against the associated person or requested expungement on his or her behalf, the associated person's conduct is less likely to be addressed fully by the parties during the customer arbitration. In those circumstances, FINRA believes that the associated person should not be able to intervene in the customer arbitration, and that any expungement request should be decided separately by the Special Arbitrator Roster.<sup>265</sup>

21. Application of Expungement Framework to Customer Complaints

In Notice 17-42, FINRA proposed to allow an associated person to file an arbitration against a member firm for the sole purpose of seeking expungement of a customer complaint and have the request decided by the Special Arbitrator Roster. In response to Notice 17-42, NASAA stated that it objected to “expanding the scope of Rule 2080 to apply to all information related to [non-arbitrated] customer complaints.” NASAA stated that today, the expungement process is used to expunge customer complaints that are not the subject of arbitration, but believed that this practice was “beyond the scope originally intended with the rules” and that codification would “further embed a flawed process that does not afford regulators the ability to preserve information already considered to have regulatory value and provide investor protection.” The SEC Investor Advocate also indicated that it did not believe that “now is the time to expand the Rule 2080 expungement process to claims that do not result in arbitration,” and that it would “prefer to see the results of the new process before introducing an entirely new class of complaints to the mix.”

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<sup>265</sup> See proposed Rule 12805(a)(1)(E)(iii); see also supra Item II.A.1.(II)A.3, “No Intervening in Customer Arbitrations to Request Expungement.”

FINRA notes that customer complaints have always been within the contemplated scope of FINRA Rule 2080. In proposing and adopting predecessor NASD Rule 2130, and in proposing to adopt FINRA Rule 2080 without material change, FINRA defined “customer dispute information” as including “customer complaints, arbitration claims, and court filings made by customers, and the arbitration awards or court judgments that may result from those claims or filings.”<sup>266</sup> The proposed amendments would continue to allow associated persons to file a claim in arbitration against a member firm for the sole purpose of seeking expungement of a customer complaint that is reported in the CRD system.

22. Other General Comments in Response to Notice 17-42

A. Personal Experiences with the Expungement Process

Some commenters opposed the proposal as set forth in Notice 17-42 because of their experiences with what they considered to be meritless customer arbitration claims.<sup>267</sup> In addition, a number of commenters described their personal experiences with the customer complaint and expungement process or generally criticized the current process and the proposed rule change as unfair.<sup>268</sup> FINRA acknowledges and appreciates

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<sup>266</sup> See Notice to Members 04-16 (March 2004); Securities Exchange Act Release No. 47435 (March 4, 2003), 68 FR 11435 (March 10, 2003) (Notice of Filing and Amendment No. 1 of File No. SR-NASD-2002-168); Securities Exchange Act Release No. 59771 (April 15, 2009), 74 FR 18411 (April 22, 2009) (Notice of Filing and Amendment No. 1 of File No. SR-FINRA-2009-016).

<sup>267</sup> See Anzaldúa, Barber, Braschi, Brookes, Burrill, Christ, Decker, Di Silvio, Gamblin, Glenn, Harmon, Harris, Higgenbotham, Isola, Joyce, Leven, Lindsey, Ram, Rosser, Scrydloff, Skafo, Slaughter, Stephens, Stewart, Tinklenberg, Walter, Weinerf and Zanolli.

<sup>268</sup> See e.g., Higgenbotham (describing CRD disclosures “related to funds offered by my employer [that] crashed during the 2007-2008 Financial Crisis”); see also AdvisorLaw (providing a hyperlink to an online petition that requested signatures

the commenters' concerns and has considered them in connection with the proposed rule change as a whole.

B. General Perspectives on the Proposed Rule Change

Some commenters also offered more general perspectives on the rule proposal as set forth in Notice 17-42. The SEC Investor Advocate, while generally supporting the proposed rule change, expressed a concern that the proposed amendments may cause brokers to seek to avoid the FINRA Rule 2080 process entirely, and instead request expungement directly in a court of competent jurisdiction. FINRA notes that today, a broker can seek expungement by going through the FINRA arbitration process or by going directly to court.<sup>269</sup>

SIFMA stated that FINRA already has in place a robust set of rules and expanded guidance to safeguard the expungement process, and that there did not appear to be any empirical justification for the additional regulations contained in the proposal, such as that expungements are too numerous or are being improperly granted.

PIABA stated that FINRA should only promulgate rules that facilitate removal of customer dispute information from the CRD system in the most extraordinary of circumstances. NASAA supported the proposal as an "important first step" that "add[ed] beneficial requirements and limitations related to the procedure of expungement."

FINRA appreciates the commenters' differing perspectives. FINRA's review suggests that the percentage of expungement requests that are recommended is higher

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to "support a balanced, cost and time effective, expungement process," and collecting associated comments).

<sup>269</sup> See FINRA Rule 2080; see also supra note 12 (describing the requirement to name FINRA as a party when brokers seek expungement in court).

when the arbitrator or panel receives information only from the associated person or other party requesting expungement.<sup>270</sup> FINRA believes that the expungement process that would be established by the proposed rule change would help ensure that expungement is recommended in limited circumstances, while providing associated persons with a reasonable framework to seek expungement of information on their CRD records by establishing one or more of the grounds set forth in FINRA Rule 2080(b)(1).

C. Alternatives to the CRD Disclosure and Expungement Framework

Several commenters suggested alternatives to the current CRD disclosure and expungement framework.<sup>271</sup> For example, Mahoney stated that where an arbitration panel renders an award denying a customer's claims against an associated person, "the associated person should automatically have their CRD record expunged of all references to the complaint." Mahoney also stated that FINRA should not subject associated persons who are not named in a customer complaint, but were determined by member firms to have been involved in the sales practice violation(s), to disclosure and expungement standards that "create an unprecedented rebuttable presumption of liability."<sup>272</sup> In contrast, St. John's suggested that associated persons be prohibited from seeking expungement if there has been a finding of liability in the arbitration.

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<sup>270</sup> See supra Item II.B.2., "Economic Baseline."

<sup>271</sup> See Barber, Baumgardner, Burrill, Butt, Chepucavage, Commonwealth, Harmon, Harris, Mahoney, Penzell, PIABA, Stewart, Tinklenberg and Wellington.

<sup>272</sup> See also FSI.

PIABA stated that although it supported the proposed rule change, expungement requests would be best handled separate from the arbitration and determined by FINRA itself rather than arbitrators. NASAA proposed further reform to the expungement process built around several principles including, for example, increased regulatory participation that allows for a regulatory determination regarding the merits of the expungement request.

FINRA appreciates the commenters' suggestions. As indicated by the proposed rule change, FINRA believes that revising the current expungement process as set forth in the proposed rule change, particularly the establishment of a panel of arbitrators randomly selected from the Special Arbitrator Roster to consider and decide straight-in requests, would best help achieve the goal that expungement should be recommended in limited circumstances. However, FINRA welcomes continued engagement to discuss further ways to enhance the expungement process.

#### D. Other Comments

In response to Notice 17-42, Public Citizen stated that the explanation of expungement decisions that arbitrators write should be made public to ensure transparency. FINRA notes that arbitrators are required to provide a brief written explanation of the reasons for recommending expungement in the arbitration award.<sup>273</sup> The proposed rule change would retain this requirement, but would remove the word “brief” to indicate to the arbitrators that they must provide enough detail in the award to explain their rationale for recommending expungement.<sup>274</sup> As the Guidance suggests, the

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<sup>273</sup> See FINRA Rule 12805.

<sup>274</sup> See proposed Rules 12805(c)(8) and 13805(c)(8).

explanation must be complete and not solely a recitation of one of the FINRA Rule 2080 grounds or language provided in the expungement request.<sup>275</sup>

In addition, FINRA makes arbitration awards publicly available in the FINRA Arbitration Awards Online database (which provides arbitration awards rendered in FINRA's arbitration forum as well as other forums).<sup>276</sup> To provide information to the public, BrokerCheck links directly to the FINRA Arbitration Awards Online database. When a broker's BrokerCheck record includes a reportable arbitration award, the BrokerCheck record provides a hyperlink directly to the relevant document.

PIABA stated that removal of customer dispute information from the CRD system diminishes the ability of reputation to police business misconduct because of "FINRA's embrace of widespread pre-dispute arbitration agreements," and because records from FINRA proceedings are not available to the public on the same terms as public court proceedings. As discussed above, the proposed rule change is intended to help preserve in CRD information that is valuable to investors and regulators, while allowing associated persons a reasonable mechanism to remove information that is inaccurate.

Keesal suggested that orders from other respected arbitration forums, such as the American Arbitration Association ("AAA"), should be afforded the same weight as arbitral findings from arbitrators in FINRA-administered arbitration, provided that (1) the

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<sup>275</sup> See supra note 3.

<sup>276</sup> Arbitration Awards Online is available at <http://www.finra.org/arbitration-and-mediation/arbitration-awards>. This database enables users to perform Web-based searches for FINRA and historical NASD arbitration awards. Also available through the database are historical awards for the New York Stock Exchange, the American Stock Exchange, the Philadelphia Stock Exchange, the Chicago Board Options Exchange, the Pacific Exchange/ARCA and the Municipal Securities Rulemaking Board.

arbitrators make written, factual findings as the basis for expungement under FINRA Rule 2080 and (2) the requirements of FINRA Rule 12805 are satisfied. FINRA appreciates the commenter's suggestion and would consider how to treat arbitration awards recommending expungement in accordance with the proposed rule change from other recognized arbitration forums, such as AAA or JAMS, if the proposed rule change is approved by the Commission.

In addition, Keesal requested that FINRA provide guidance to associated persons and registration personnel regarding the meaning and effect of an expunged claim in the context of licensing and registration questionnaires. Although the impact on licensing and registration questionnaires is outside the scope of the proposed rule change, FINRA will consider whether additional guidance is appropriate.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve or disapprove such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2020-030 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2020-030. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only

information that you wish to make available publicly. All submissions should refer to File Number SR-FINRA-2020-030 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>277</sup>

Jill M. Peterson  
Assistant Secretary

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<sup>277</sup> 17 CFR 200.30-3(a)(12).

# Regulatory Notice

17-42

## Expungement of Customer Dispute Information

### FINRA Requests Comment on Proposed Amendments to the Codes of Arbitration Procedure Relating to Requests to Expunge Customer Dispute Information

Comment Period Expires: February 5, 2018

#### Summary

FINRA seeks comment on establishing a roster of arbitrators with additional training and specific backgrounds or experience from which a panel would be selected to decide an associated person's request for expungement of customer dispute information.<sup>1</sup> The arbitrators from this roster would decide expungement requests where the underlying customer-initiated arbitration is not resolved on the merits or the associated person files a separate claim requesting expungement of customer dispute information. The *Notice* also proposes additional changes to the expungement process that would apply to all requests for expungement of customer dispute information.

This proposal is one in a series of regulatory initiatives that FINRA is considering related to the expungement process. For example, the FINRA Board of Governors has approved filing with the Securities and Exchange Commission (SEC) proposed amendments to the Codes of Arbitration Procedure for Customer and Industry Disputes (Codes) to make the best practices from the Notice to Arbitrators and Parties on Expanded Expungement Guidance<sup>2</sup> (Guidance) rules that arbitrators must follow when considering expungement requests. In addition, FINRA staff has been working with the North American Securities Administrators Association (NASAA) on various expungement issues, including potential amendments to the existing regulatory review process.

The text of the proposed amendments can be found at [www.finra.org/notices/17-42](http://www.finra.org/notices/17-42).

December 6, 2017

#### Notice Type

- ▶ Request for Comment

#### Suggested Routing

- ▶ Compliance
- ▶ Legal
- ▶ Operations
- ▶ Registered Representatives
- ▶ Senior Management

#### Key Topics

- ▶ Arbitration
- ▶ Associated Person
- ▶ Code of Arbitration Procedure
- ▶ Dispute Resolution

#### Referenced Rules & Notices

- ▶ Code of Arbitration Procedure for Customer Disputes, Rule 12000 Series
- ▶ Code of Arbitration Procedure for Industry Disputes, Rule 13000 Series
- ▶ FINRA Rule 12100
- ▶ FINRA Rule 12805
- ▶ FINRA Rule 13805
- ▶ FINRA Rule 13806

Questions concerning this *Notice* should be directed to:

- ▶ Kenneth L. Andrichik, Senior Vice President and Chief Counsel, Office of Dispute Resolution, at (212) 858-3915;
- ▶ Victoria Crane, Associate General Counsel, Office of General Counsel, at (202) 728-8104; or
- ▶ Mignon McLemore, Assistant Chief Counsel, Office of Dispute Resolution, at (202) 728-8151.

### Action Requested

FINRA encourages all interested parties to comment on the proposal. Comments must be received by February 5, 2018.

Member firms and other interested parties can submit their comments using the following methods:

- ▶ Emailing comments to [pubcom@finra.org](mailto:pubcom@finra.org); or
- ▶ Mailing comments in hard copy to:  
 Marcia E. Asquith  
 Office of the Corporate Secretary  
 FINRA  
 1735 K Street, NW  
 Washington, DC 20006-1506

To help FINRA process and review comments more efficiently, persons should use only one method to comment on the proposal.

**Important Notes:** The only comments that FINRA will consider are those submitted pursuant to the methods described above. All comments received in response to this *Notice* will be made available to the public on the FINRA website. Generally, FINRA will post comments as they are received.<sup>3</sup>

Before becoming effective, a proposed rule change must be authorized for filing with the SEC by the FINRA Board of Governors, and then must be filed with the SEC pursuant to Section 19(b) of the Securities Exchange Act of 1934 (SEA).<sup>4</sup>

## Background & Discussion

Through the expungement process, associated persons may seek to remove allegations made by customers from the Central Registration Depository (CRD ®) system and hence from the FINRA BrokerCheck (BrokerCheck ®) system.<sup>5</sup> It has been FINRA's long-held position that expungement of customer dispute information is an extraordinary measure, but it may be appropriate in certain circumstances.

CRD is the central licensing and registration system for the U.S. securities industry. In general, registered securities firms and regulatory authorities submit information in CRD in response to questions on the uniform registration forms.<sup>6</sup> These forms collect administrative, disciplinary and other information about registered personnel, including customer complaints, arbitration claims and court filings made by customers, and the arbitration awards or court judgments that may result from those claims or filings (*i.e.*, customer dispute information).<sup>7</sup> The SEC, FINRA, state and other regulators use this information in connection with their licensing and regulatory activities. Most of the CRD information is made publicly available through BrokerCheck. Associated persons may seek to have customer dispute information removed from CRD (and thereby, from BrokerCheck) pursuant to FINRA Rule 2080 because the claim or allegation is factually impossible, clearly erroneous or false, or if the associated person was not involved in the alleged investment-related sales practice violation.<sup>8</sup>

Critics of expungement have raised specific concerns about expungement hearings held after a settlement in the customer's arbitration case that gave rise to the customer dispute information (Underlying Customer Case). In these instances, critics argue that the panel from the Underlying Customer Case has not heard the full merits of that case and, therefore, may not have any special insights in determining whether to grant a request for expungement of customer dispute information under Rule 2080. Further, claimants and their counsel have little incentive to participate in an expungement hearing after the Underlying Customer Case settles and typically do not participate in such hearings. Thus, during these expungement hearings, the panel may receive information that is one-sided, which may favor the associated person requesting expungement.

The proposed amendments to the Codes would make a number of important changes to the current framework related to the expungement of customer dispute information. Among other things, the proposed amendments would:

### ***All Requests for Expungement of Customer Dispute Information***

- ▶ amend the Codes to require that for all requests for expungement of customer dispute information:
  - ▶ the associated person who is seeking to have his or her CRD record expunged must appear at the expungement hearing; and
  - ▶ to grant expungement, a three-person panel of arbitrators must unanimously agree that expungement is appropriate under Rule 2080(b)(1) and find that the customer dispute information has no investor protection or regulatory value.

***Expungement Requests During the Underlying Customer Case***

- ▶ limit an associated person who is named as a party to one opportunity to request expungement, and that opportunity must be exercised during the Underlying Customer Case;
- ▶ create limitations on requests for expungement of customer dispute information, including a one-year limitation period after the Underlying Customer Case closes for an associated person to file an expungement request that was not decided during the Underlying Customer Case;
- ▶ codify a party's ability to request expungement on behalf of an associated person not named as a respondent in the Underlying Customer Case (hereinafter referred to as an unnamed person)<sup>9</sup> during the Underlying Customer Case, and establish procedures for such requests;
- ▶ require associated persons who file expungement requests outside of the Underlying Customer Case to file the request under the Industry Code against the firm at which he or she was associated at the time of the events giving rise to the customer dispute;
- ▶ remove the option to file an expungement request outside of the Underlying Customer Case against a customer; and
- ▶ specify a minimum filing fee of \$1,425 for expungement requests.

***Expungement Arbitrator Roster***

- ▶ establish a roster of public chairpersons with additional qualifications to decide expungement requests (Expungement Arbitrator Roster) filed against a firm under the Industry Code.

***Expungement Requests in Simplified Arbitration Cases***

- ▶ require that an associated person or an unnamed person wait until the conclusion of a customer's simplified arbitration case to file an expungement request, which must be filed against the firm not the customer and would be heard by a panel selected from the Expungement Arbitrator Roster.

***Expungement Requests relating to Customer Complaints that Do Not Result in an Arbitration Claim***

- ▶ require that the associated person seek expungement of the customer dispute information relating to a customer complaint within one year of the member firm initially reporting the customer complaint to CRD.

## **I. Requesting Expungement Relief During the Underlying Customer Case**

Current FINRA Rule 12805 provides a list of requirements that arbitrators must meet before they may grant expungement.<sup>10</sup> The rule does not, however, provide any guidance for associated persons on how and when an associated person may request expungement relief during the Underlying Customer Case. As discussed further below, the proposal would amend Rule 12805 to set forth requirements for expungement requests filed by an associated person as a party as well as on behalf of an unnamed person.

### **A. *Expungement Requests by an Associated Person Named as a Party***

#### **1. Applicability**

Currently, under FINRA Rule 12805, an associated person who is a named party in an arbitration may request expungement during that arbitration, but is not required to do so. Some associated persons have filed requests seeking to expunge customer dispute information years after FINRA closed the Underlying Customer Case. Given the length of time between case closure and filing of the request, in many of these instances, the customers cannot be located and any documentation that could explain what happened in the case is not available or cannot be located. Thus, under the proposal, an associated person who is named as a party would be required to request expungement in the Underlying Customer Case. If the associated person does not request expungement in the Underlying Customer Case, the associated person would be prohibited from seeking to expunge the customer dispute information arising from the customer's statement of claim during any subsequent proceeding under the Codes. Requiring an associated person who is named in an arbitration to request expungement of the customer dispute information during the Underlying Customer Case would eliminate expungement requests filed years after the Underlying Customer Case concludes.

#### **2. Method of Request and Fees**

The proposed amendments would permit the associated person to file an expungement request or include such request in the answer or any pleading.<sup>11</sup> The associated person would be permitted to file the request no later than 60 days before the first scheduled hearing session,<sup>12</sup> otherwise, the associated person would be required to file a motion<sup>13</sup> to seek an extension to file the expungement request. Thus, if an associated person files an expungement request after the 60-day timeframe, the non-moving parties could object and the panel would be required to decide the associated person's motion.

Along with the expungement request, the associated person would be required to pay a filing fee of \$1,425 or the applicable filing fee provided in Rule 12900(a)(1), whichever is greater.<sup>14</sup> In addition, consistent with existing provisions under the Codes, there would be an assessment of a member surcharge<sup>15</sup> and process fee<sup>16</sup> against each member that is named as a party or respondent, or that employed the associated person named as a respondent or party at the time of the events giving rise to the dispute, as applicable.<sup>17</sup>

### 3. Underlying Customer Case Closes by Award

If the Underlying Customer Case closes by award, the panel would be required to consider and decide the expungement request during the Underlying Customer Case. The panel must, among other things, agree unanimously to grant expungement and in the arbitration award: (1) identify at least one of the Rule 2080(b)(1) grounds for expungement that serves as the basis for expungement and provide a brief written explanation of the reasons for its finding that one or more Rule 2080(b)(1) grounds for expungement applies to the facts of the case; and (2) find that the customer dispute information has no investor protection or regulatory value.

The unanimity requirement would apply to all requests for expungement of customer dispute information. Thus, when a panel decides an associated person's expungement request during the Underlying Customer Case, the panel would be required to agree unanimously to grant expungement. In deciding the customer's claims, however, a majority agreement of the panel would continue to be sufficient.

### 4. Underlying Customer Case Closes Other than by Award

If the Underlying Customer Case closes other than by award (*e.g.*, the parties settle the arbitration), the panel in the Underlying Customer Case would not decide the associated person's expungement request. In this situation, the associated person would be permitted to file the expungement request as a new claim under the Industry Code against the firm at which he or she was associated at the time of the events giving rise to the customer dispute.<sup>18</sup> Under the proposal, an associated person would not be permitted to file the new expungement request against the customer because the customer should not be asked to participate in another arbitration hearing that could increase the customer's costs and expenses. Instead, the associated person would be required to name the firm at which he or she was associated at the time of the events giving rise to the customer dispute with the goal of having a more robust expungement proceeding that will help the panel determine whether to grant expungement. As discussed in further detail below, this new claim would be decided by a three-person panel selected from the Expungement Arbitrator Roster.

### 5. Limitations on Expungement Requests

For the expungement request to be considered after the Underlying Customer Case closes other than by award, the associated person would be required to file the request within one year after FINRA closes the Underlying Customer Case, provided the expungement request is not barred. Under the proposal, an associated person would be barred from requesting expungement relief if: (1) a panel or arbitrator in the Underlying Customer Case issued a decision on the expungement request for the same customer dispute information; (2) the associated person requested expungement of the same customer dispute information in court and the court denied the request; (3) the Underlying Customer Case has not concluded; (4) it has been more than a year since FINRA closed the Underlying Customer Case; or (5) if there was no Underlying Customer Case involving the customer dispute information, more than one year has elapsed since the date that the member firm initially reported the customer complaint to CRD.<sup>19</sup>

The first two limitations would prevent an associated person from forum shopping to garner a favorable outcome on his or her expungement request. Under the proposal, these limitations would apply to all requests for expungement of customer dispute information filed in the forum, including requests decided prior to the effective date of the proposal.

With respect to the third limitation, if an associated person's expungement request was not decided during the Underlying Customer Case, the associated person would be required to wait until the Underlying Customer Case concludes before filing a request for expungement. Thus, under the proposal, if the Underlying Customer Case has not concluded and an associated person has filed a request for expungement of the customer dispute information at issue in the Underlying Customer Case, FINRA would stay the associated person's expungement request until the Underlying Customer Case concludes and permit the associated person to refile it under the Industry Code so that it could be heard by a panel from the Expungement Arbitrator Roster.

With respect to the fourth limitation, if the expungement request is not filed within a year after the Underlying Customer Case closes, the associated person would forfeit his or her right to request expungement. The one-year limitation period would ensure that the expungement hearing is held close in time to the Underlying Customer Case, when information regarding the Underlying Customer Case is available and in a timeframe that would increase the likelihood for the customer to participate if he or she chooses to do so.

Under the proposal, the one-year limitation period would apply where the Underlying Customer Case closes after the effective date of the proposal. If the Underlying Customer Case closes on or prior to the effective date of the proposal, the associated person would have six months from the effective date to file the expungement request.

The fifth limitation would establish a one-year period for associated persons to expunge customer dispute information that arose from a customer complaint and did not result in an arbitration claim. Under the proposal, the associated person would have a year from the date that a member firm initially reported a customer complaint to CRD to file an expungement request.<sup>20</sup> If a member firm initially reports a customer complaint to CRD on or prior to the effective date of the proposal, the associated person would have six months from the effective date of the proposal to file the expungement request.

#### *B. Expungement Requests by a Party on Behalf of an Unnamed Person*

##### *1. Applicability*

The proposal would define an unnamed person to mean an associated person or formerly associated person who is identified in Forms U4 or U5 as having been the subject of an investment-related customer-initiated arbitration that alleged that he or she was involved in one or more sales practice violations, but who was not named as a respondent in the arbitration.<sup>21</sup>

Currently, unnamed persons have three arbitration avenues to pursue expungement under the Codes: (1) a party to an arbitration may request expungement on their behalf during the Underlying Customer Case; (2) the unnamed persons may try to intervene in the Underlying Customer Case; and (3) the unnamed persons may file a separate arbitration case seeking expungement after the Underlying Customer Case closes.

As explained further below, the proposed amendments would codify the ability of a party in the Underlying Customer Case to request expungement on behalf of an unnamed person with the written approval of the unnamed person. The proposed amendments would also codify procedures regarding when and how an unnamed person may file a separate case seeking expungement of customer dispute information after the Underlying Customer Case closes.

As these would be the only avenues by which an unnamed person may request expungement of customer dispute information under the Codes, the proposed amendments would foreclose the option for an unnamed person to intervene in the Underlying Customer Case and thereby remove the potential for the unnamed person to become a party in the Underlying Customer Case.

## 2. Procedural Similarities to Expungement Requests by an Associated Person Named as a Party

The proposed procedures discussed above that would apply to expungement requests by an associated person named as a party (*i.e.*, method of request and fees, customer case closure either by award or otherwise, and one-year limitation period) would also apply to expungement requests by a party on behalf of an unnamed person, with some modifications as explained below.

First, a party requesting expungement relief on behalf of an unnamed person would be required to file with the Director of the Office of Dispute Resolution<sup>22</sup> (Director) and serve on all parties no later than 60 days before the first scheduled hearing session: (1) a Form Requesting Expungement Relief on Behalf of an Unnamed Person, signed by the unnamed person whose CRD record would be expunged;<sup>23</sup> and (2) a statement requesting expungement relief.<sup>24</sup> The signed form would represent an acknowledgement by the unnamed person that he or she agrees to be bound by the panel's decision on the request for expungement relief. If the party does not request expungement within the 60-day timeframe, the party would be required to file a motion seeking an extension to file the expungement request.

Second, if the Underlying Customer Case closes other than by award, FINRA would notify the unnamed person in writing that the case has closed. This milestone in the customer's case would start the one-year limitation period for the unnamed person to seek expungement of the customer dispute information against the firm at which he or she was associated at the time of the events giving rise to the customer dispute, in a separate action under the Industry Code (as discussed in further detail below).

Finally, if a party from the Underlying Customer Case does not request expungement relief on behalf of the unnamed person, the unnamed person would be permitted to file an expungement request under the Industry Code against the firm at which he or she was associated at the time of the events giving rise to the customer dispute, within one year of the Underlying Customer Case closure, provided the expungement request is not barred.<sup>25</sup>

## **II. Proposed Changes that Apply to All Requests for Expungement of Customer Dispute Information**

Currently, the Codes provide criteria that a panel must follow before it may decide an expungement request.<sup>26</sup> As explained in further detail below, under the proposal, the current requirements to hold a hearing session and to provide a basis for expungement in an arbitration award would be expanded to clarify the process and guide further the arbitrators' decision-making. The proposed changes would apply to all requests to expunge customer dispute information filed under the Codes.

### **A. Hold a Hearing Session**

Currently, the Codes require a panel that is deciding an expungement request to hold a recorded hearing session (by telephone or in person) regarding the appropriateness of expungement.<sup>27</sup> The proposed amendments would require that an associated person who is seeking to have his or her CRD record expunged appear at the expungement hearing, either in person or by videoconference; appearance by telephone would not be an option. As the associated person is requesting the permanent removal of information from CRD, FINRA believes that the associated person should be available in person or by videoconference to present his or her case and respond to questions from the panel.

### **B. Unanimity and Additional Finding Required to Grant Expungement of Customer Dispute Information**

Currently, the Codes require that the panel indicate in the arbitration award which of the Rule 2080 grounds for expungement serves as the basis for its expungement order and provide a brief written explanation of the reasons for its finding that one or more Rule 2080 grounds for expungement applies to the facts of the case.<sup>28</sup>

The proposed amendments would require that the panel agree unanimously to grant expungement and in the arbitration award: (1) identify at least one of the Rule 2080(b)(1) grounds for expungement that serves as the basis for expungement and provide a brief written explanation of the reasons for its finding that one or more Rule 2080(b)(1) grounds for expungement applies to the facts of the case; and (2) find that the customer dispute information has no investor protection or regulatory value.

The proposal would clarify for arbitrators that the standard for granting the permanent removal of customer dispute information from CRD is a finding that the customer dispute information has no investor protection or regulatory value. Since Rule 2080 has been in effect, FINRA has implemented policies and procedures to strengthen the expungement process. For example, in 2008, FINRA adopted Rule 12805 to require arbitrators to perform additional fact finding before granting expungement of customer dispute information.<sup>29</sup> After the approval of FINRA Rule 12805, FINRA staff updated the arbitrator training materials and all arbitrators were required to certify that they had familiarized themselves with the requirements of the expungement rules.<sup>30</sup> In 2013, in response to FINRA staff's concerns about the number of expungement requests granted after the Underlying Customer Case settles, FINRA published the Guidance for arbitrators to use when considering expungement requests.<sup>31</sup>

Based on FINRA's review of awards where expungement has been granted, arbitrators appear to be following the practices identified in the Guidance and have a heightened awareness that expungement is an extraordinary remedy. FINRA has noticed a marked improvement in the quality of the awards in which expungement is granted. Notwithstanding these positive results, FINRA believes that expanding the findings that arbitrators must make before granting expungement of customer dispute information would help FINRA maintain the accuracy of the data that appears in CRD by ensuring that only information that is not valuable to regulators and investors is expunged from CRD.<sup>32</sup>

### **III. Requests for Expungement of Customer Dispute Information Under the Industry Code and the Expungement Arbitrator Roster**

As explained above, if an expungement request is not decided during the Underlying Customer Case, the proposal would permit an associated person to file the expungement request as a new claim against the firm<sup>33</sup> at which he or she was associated at the time of the events giving rise to the customer dispute, provided the claim is not barred.<sup>34</sup> A three-person panel selected from the Expungement Arbitrator Roster would decide this new claim.

#### **A. Selection of Panel**

Under the proposal, the Neutral List Selection System<sup>35</sup> (NLSS) would randomly select three public chairpersons<sup>36</sup> from the Expungement Arbitrator Roster to decide an expungement request.<sup>37</sup> To be on the Expungement Arbitrator Roster, the public chairpersons would be required to have the following additional qualifications:

- (1) completed enhanced expungement training;<sup>38</sup>
- (2) admitted to practice law in at least one jurisdiction; and
- (3) five years' experience in any one of the following disciplines:
  - (a) litigation;
  - (b) federal or state securities regulation;
  - (b) administrative law;
  - (c) service as a securities regulator; or
  - (d) service as a judge.

The proposed changes to the expungement framework would help arbitrators on the Expungement Arbitrator Roster better understand the unique nature of this extraordinary remedy and the importance of maintaining the integrity of the public record. The proposed roster composition and the proposed additional requirements to grant expungement, taken together, should help FINRA maintain the integrity of its CRD records and ensure that expungement is only granted in appropriate circumstances.

### *B. Expungement Hearing*

Under the proposal, once the panel is selected from the Expungement Arbitrator Roster, it must hold a recorded hearing session regarding the appropriateness of the associated person's request for expungement of customer dispute information. With respect to the hearing session, the proposal provides that: (1) the associated person whose CRD record would be expunged must appear at the expungement hearing either in person or by videoconference;<sup>39</sup> (2) the Director would notify the parties from the Underlying Customer Case or the customer complaint of the time and place of the expungement hearing; and (3) all customers in the Underlying Customer Case or customers who filed a customer complaint are entitled to appear at the expungement hearing. At the customer's option, the customer may appear by telephone.

As discussed above in connection with expungement hearings in the Underlying Customer Case, FINRA believes that as the associated person is requesting the permanent removal of information from CRD, the associated person should be available in person to present his or her case and respond to questions from the panel. In addition, FINRA believes that allowing customers to appear by telephone would make it easier for them to participate in the expungement hearing and, therefore, could encourage them to participate.

### *C. Unanimity and Additional Finding Required to Grant Expungement*

Consistent with requests for expungement relief considered by a panel under the Customer Code, a panel selected from the Expungement Arbitrator Roster under the Industry Code may grant expungement of customer dispute information only if the panel agrees unanimously. In addition, in the arbitration award the panel must: (1) identify at least one of the Rule 2080(b)(1) grounds for expungement that serves as the basis for expungement and provide a brief written explanation of the reasons for its finding that one or more Rule 2080(b)(1) grounds for expungement applies to the facts of the case; and (2) find that the customer dispute information has no investor protection or regulatory value.

## **IV. Expungement Requests in Simplified Arbitrations**

Under the Codes, arbitrations involving \$50,000 or less are decided by a single arbitrator without a hearing, also referred to as a decision "on the papers," and are called simplified arbitrations.<sup>40</sup> The Codes provide that the requirement to hold a hearing to decide an expungement request applies to expungement requests made in simplified arbitrations.<sup>41</sup>

Under the proposal, an associated person or unnamed person would be required to file an expungement request under the Industry Code against the firm at which he or she was associated at the time of the events giving rise to the customer dispute, and only at the conclusion of the simplified case. Thus, a panel from the Expungement Arbitrator Roster would consider and decide the expungement request.<sup>42</sup>

The proposed amendments would address a concern raised by customers that when an associated person requests expungement during a simplified case, the arbitrator holds a hearing during the simplified case to decide the appropriateness of expungement. When the arbitrator conducts a hearing in this situation, the customer is forced to participate in a hearing that he or she did not request, which delays the customer's case and the rendering of an award in the customer's simplified case. The proposed amendments would ensure that expungement requests would not be heard during a simplified case.<sup>43</sup>

## **V. Preliminary Economic Impact Analysis**

### *A. Regulatory Need*

Associated persons can request expungement of customer dispute information from CRD. As discussed above, some critics have raised concerns about arbitration panels granting requests for expungement of customer dispute information when the panel has not heard the full merits of the Underlying Customer Case. Claimants and their counsel may not have the incentive to participate in expungement hearings. Panels, therefore, may receive information that is one-sided, which could favor the associated person seeking expungement. The proposed amendments would provide for an increased opportunity for customer participation in expungement decisions, make information regarding the Underlying Customer Case more readily available, make the expungement decision more timely relative to the Underlying Customer Case, and establish an Expungement Arbitrator Roster to decide expungement requests when expungement has not been decided as part of the Underlying Customer Case.

### *B. Economic Baseline*

The economic baseline for the proposed amendments is the current rules under the Codes that address the process for associated persons to expunge customer dispute information from CRD. The proposed amendments are expected to affect associated persons; firms; customers to complaints or arbitration cases; customers that publicly view CRD information through BrokerCheck; and the SEC, FINRA, state and other regulators that use CRD.

Associated persons have incentive to file for expungement relief to remove customer dispute information from CRD. By removing customer dispute information from CRD, associated persons would also remove customer dispute information from BrokerCheck. Customer dispute information on CRD and BrokerCheck may impact the business of associated persons and reduce their professional opportunities. Investors (including current and prospective customers) use BrokerCheck to learn about the professional background and conduct of associated persons. Current and prospective customers may be less likely to select or remain with associated persons who have customer dispute information on their records. Current and future employers can also consider customer dispute information when making employment decisions.

Although panels that decide expungement requests receive information related to the expungement request from associated persons, they may not receive such information from customers. Panels are likely to receive information from customers if the panel decides the expungement request during the Underlying Customer Case. Panels are less likely to receive such information if the Underlying Customer Case is settled or withdrawn. Panels may also not receive information from customers if associated persons file separate claims requesting expungement and the customers are unwilling or unable to participate. In these instances, customers and their counsel may not have the incentive to participate in the separate expungement hearing. Associated persons may also request expungement of customer dispute information long after the Underlying Customer Case closes, making it potentially more difficult for customers to participate and the panel to verify or validate the information provided.

One-sided information could favor the associated persons seeking expungement, which has the potential to reduce the integrity and reliability of the information on CRD and BrokerCheck. As noted above, investors use that information to make decisions about associated persons with whom they may wish to do business. The SEC, FINRA, state and other regulators use CRD information for licensing and regulatory activities. Accordingly, the integrity and reliability of CRD information is critical to the needs of these stakeholders.

FINRA staff is able to identify 5,482 customer claims in arbitration that were filed from 2014 to 2016, and that were closed as of June 30, 2017. FINRA staff is also able to identify 12,849 customer complaints that were filed against associated persons and closed during the same time period but did not result in an arbitration claim. These customer claims and complaints are available in the CRD system and disclosed through BrokerCheck and, therefore, could be the subject of an expungement request by an associated person.

FINRA staff is able to identify 2,232 customer arbitration cases involving an expungement request that were filed from 2014 to 2016 and closed as of June 30, 2017. Among the 2,232 cases, 1,738 (78 percent) were closed by settlement or mediation. Another 384 (17 percent) of the 2,232 cases were closed by hearing or on the papers; another 92 (4 percent) were withdrawn; and 18 (less than 1 percent) were closed by other means. In addition to the 2,232 customer arbitration cases, FINRA staff is also able to identify 183 intra-industry arbitration cases that involve an expungement request of customer dispute information.

Among the cases containing a request for expungement of customer dispute information that were filed from 2014 to 2016 and closed as of June 30, 2017, arbitrators made a determination regarding the expungement of customer dispute information in 808 of these cases. The 808 cases include decisions regarding expungement requests as part of the Underlying Customer Case as well as decisions regarding expungement requests when associated persons filed a separate claim for expungement following the close of the Underlying Customer Case.

Arbitrators recommended expungement for at least one associated person in 608 (75 percent) of the 808 cases. In another 213 (26 percent) of the 808 cases, arbitrators did not grant expungement for at least one associated person. In a few of the 808 cases where more than one associated person sought expungement relief, arbitrators both granted and did not grant expungement relief for at least one associated person. Among the 808 cases in which arbitrators made a determination regarding the expungement of customer dispute information, the Underlying Customer Case closed by settlement in 436 of the cases. Arbitrators recommended expungement for at least one associated person in 88 percent of these 436 cases.

If an arbitration panel grants expungement of customer dispute information, the associated person must obtain an order from a court of competent jurisdiction confirming the arbitration award containing expungement relief. In the experience of FINRA staff, courts typically confirm arbitration awards containing expungement relief. Associated persons that obtain a court order confirming the arbitration award must then serve the confirmed award on FINRA to have the customer dispute information expunged. Not all panel expungement recommendations result in the expungement of customer dispute information from CRD and BrokerCheck. Some associated persons may determine not to confirm the award in court. As of June 30, 2017, FINRA had expunged customer dispute information in connection with 391 (64 percent) of the 608 cases pursuant to a court order. As of that date, associated persons may have not yet sought or obtained a court order for the remaining 217 of the 608 cases. Other associated persons may have not yet served the confirmed award on FINRA.

Lastly, the current fee structure for filing a request to expunge customer dispute information provides incentives for associated persons to file a request separately from the Underlying Customer Case and add a small monetary claim, thus making it a simplified claim, to reduce the filing fee to \$50 from \$1,575 (*i.e.*, the filing fee for a non-monetary/ unspecified claim). Further, by making the request a simplified claim, the case can be heard by one arbitrator as opposed to the default of a three-arbitrator panel for non-monetary or unspecified claims.<sup>44</sup>

### *C. Economic Impacts*

The proposed amendments are designed, among other things, to improve the quality and timeliness of the information available to panels determining requests for expungement. The panels assigned to the Underlying Customer Case would be more likely to decide expungement requests, if any. In addition, expungement decisions would occur soon after the Underlying Customer Case closes or a member firm initially reports a customer complaint to CRD. The proposed amendments would therefore increase the opportunity for or likelihood that panels would receive information from customers when considering expungement requests. The information is therefore less likely to be one-sided and favor associated persons. The proposed amendments would also establish qualifications for those arbitrators on the Expungement Arbitrator Roster who decide expungement requests when customers are less likely to provide information in connection with an expungement request. With these additional qualifications, the arbitrators should be better able to evaluate the information they receive in a more judicious and discerning manner.

The proposed amendments would benefit investors, member firms, and regulators by helping to ensure that the customer dispute information on CRD and, therefore, BrokerCheck more accurately reflects those customer disputes that have investor protection or regulatory value. Stakeholders would be more confident in the reliability of the customer dispute information contained on CRD and BrokerCheck. The customer dispute information contained on CRD and BrokerCheck would also be more meaningful and valuable to stakeholders.

Customers would benefit from the proposed amendments that restrict the manner and timing of associated persons' requests for expungement of customer dispute information. Associated persons would have one year after a customer complaint was initially reported to CRD to request expungement of the information. For customer complaints that result in an arbitration claim, associated persons named in an Underlying Customer Case would be required to request expungement during the Underlying Customer Case. Associated persons whose expungement request is not determined during the Underlying Customer Case would then have one year following the close of the Underlying Customer Case to request expungement of the customer dispute information. Customers would therefore have a greater ability to participate in the expungement hearings, if they so choose. In addition, if a separate expungement case were filed, the associated person would no longer be able to name the customer as the opposing party. Customers would therefore no longer incur the costs and inconvenience to be a party to these claims. Lastly, expungement requests would not be heard during a simplified case. As a result, customer claimants in simplified cases would no longer experience delays in the resolution of their cases as a result of expungement hearings, and would not be forced to attend a hearing in a case that the customer chose to be decided on the papers.

The proposed amendments would impose costs on associated persons, primarily by restricting how and when they could file an expungement request and, in some cases, by increasing the cost of filing an expungement request. The stricter requirements for requesting expungement of customer dispute information are meant to improve the quality and timeliness of the information that the panel hearing the request receives. The information that panels receive is less likely to be one-sided from associated persons only. The information is therefore less likely to favor the associated persons requesting expungement.

The requirement that the decision be unanimous, rather than a majority decision, could also increase the difficulty for an associated person to obtain expungement. To the extent that customers and firms use customer dispute information to make business and employment decisions, if customer dispute information is not expunged as frequently, associated persons could experience a loss of business and professional opportunities, loss of employment at their current firm, and thus, decreased income.<sup>45</sup>

Associated persons could also incur additional fees to file expungement requests. The associated person would be required to pay a filing fee of \$1,425 or the applicable filing fee provided in Rule 12900(a)(1), whichever is greater. This aspect of the proposed amendments would end the practice of associated persons adding a monetary claim of less than \$1,000 to separately filed expungement requests to reduce their filing fee to the minimum of \$50.<sup>46</sup>

Associated persons would also be required to attend expungement hearings in person, either by traveling to the hearing location or by videoconference, depending on the method permitted by the arbitration panel. Traveling to the hearing location could significantly increase the cost of having their request heard, by increasing both transportation and room and board costs as well as lost time in transit. Attendance by videoconference would eliminate many of these costs.

The potential decrease in the frequency in which panels recommend expungement and the potential increase in costs to file and to attend hearings could reduce the incentive of associated persons to request expungement of customer dispute information. Associated persons could continue to request expungement relief if they believe that the request is likely to be granted and that any reduction to their income potential is greater than any costs that they could incur. Accordingly, the types of expungement cases that arbitration panels would consider under the proposed amendments would likely be more meritorious.

The proposed amendments would also impose additional costs on member firms. If associated persons file a separate claim for expungement, they would be required to file the claim against the firm at which he or she was associated at the time of the events giving rise to the customer dispute, rather than against the customer. To the extent that member firms would become a party to the expungement case more frequently, they could experience higher costs associated with those cases.

The magnitude of the benefits and costs of the proposed amendments depends on the change in the number of associated persons requesting expungement of customer dispute information, the number of arbitration awards that grant expungement, and the number of expungement awards confirmed by the courts. The extent to which awards granting expungement become more informed would enhance the integrity and reliability of the customer dispute information on CRD and, therefore, BrokerCheck and the ability of customers and regulators to rely on the information as an accurate description of the conduct of associated persons. The magnitude of the benefits and costs also depends on the extent to which the record of associated persons decreases their business or professional opportunities. A greater decrease in business or professional opportunities would result in a greater economic transfer between associated persons. The proposed amendments would have no effect on associated persons that do not have future customer claims or complaints.

*D. Alternatives Considered*

As noted above, FINRA staff has been working with NASAA on various expungement issues, including potential amendments to the existing regulatory review process. The proposed amendments in this *Notice* reflect just one approach. FINRA requests comment below to inform subsequent revisions to the proposed amendments, including other approaches that could reduce the potential that panels receive information that is one-sided, which may favor the associated person requesting expungement.

## Request for Comment

FINRA is interested in receiving comments on all aspects of the proposed amendments. In particular, FINRA seeks comment on the following questions:

1. FINRA Rules 12805 and 13805 provide, in relevant part that, in order to grant expungement of customer dispute information under Rule 2080, the panel must comply with the requirements stated in the rule. (Emphasis added.) FINRA notes, however, that if a panel issues an arbitration award containing expungement relief, the award must be confirmed by a court of competent jurisdiction and FINRA could decide to oppose the confirmation. Thus, as the associated person is required to complete additional steps after the arbitrators make their finding in the award before FINRA will expunge the customer dispute information, FINRA believes the word “grant” may not be an appropriate description of the panel’s authority in the expungement process. FINRA is considering changing the word to “recommend.” Please discuss whether the rule should retain “grant” or change to “recommend” or some other description to more accurately reflect the panel’s authority in the expungement process.
2. Would named associated persons request expungement in every case to preserve the right to have the expungement claim heard and decided, either in the Underlying Customer Case or as a new claim under the Industry Code? If so, what would be the potential costs and benefits of a named person requesting expungement in every case?
3. Should FINRA consider bifurcating the expungement request from the customer’s claim in all cases relating to customer disputes? What would be the costs and benefits of such an approach?
4. What are the costs and benefits of requiring the unanimous consent of a three-person panel to grant all requests for expungement of customer dispute information?
5. Is the one-year limitation on being able to request expungement of customer dispute information appropriate? Should the time period be longer or shorter? Please discuss.

6. Should the associated person who is requesting expungement be required to appear in person or by videoconference, rather than by phone, at the expungement hearing?
7. Should the arbitrators on the Expungement Arbitrator Roster have specific qualifications? If so, are the proposed additional qualifications appropriate or should FINRA consider other qualifications?
8. Should the arbitrators on the Expungement Arbitrator Roster be lawyers only or could the experience of serving on three arbitrations through award be a sufficient substitute?
9. How would the proposed amendments affect the granting or denying of expungement requests? Which aspect of the proposed amendments would have the largest impact on expungement determinations? Why?
10. The proposal would establish a one-year limitation period for associated persons to expunge customer dispute information that arose from a customer complaint. The limitation period would start on the date that the member firm initially reported the customer complaint to CRD. Should the one-year limitation period be based on a different milestone? If so, what should it be?
11. The proposal would clarify for arbitrators that the standard for granting the permanent removal of customer dispute information from CRD is a finding that at least one of the Rule 2080(b)(1) factors applies and that the customer dispute information has “no investor protection or regulatory value.” Are there specific factors that arbitrators should consider when making a finding that the customer dispute information has “no investor protection or regulatory value”?
12. In a simplified arbitration case, if a customer requests a hearing, should the single arbitrator be permitted to decide an expungement request, if a request is filed?

## Endnotes

1. On December 16, 2015, the FINRA Dispute Resolution Task Force (Task Force) issued its Final Report and Recommendations (Final Report). One of the recommendations was that FINRA create a special arbitrator roster to handle expungement requests in settled cases and in cases when a claimant did not name the associated person as a respondent. A list of the Task Force members is available at <http://www.finra.org/arbitration-and-mediation/finra-dispute-resolution-task-force>. The Final Report is available at <http://www.finra.org/sites/default/files/Final-DR-task-force-report.pdf>.
2. See Expanded Expungement Guidance (September 2017), available at <http://www.finra.org/arbitration-and-mediation/notice-arbitrators-and-parties-expanded-expungement-guidance>.
3. Persons submitting comments are cautioned that FINRA does not redact or edit personal identifying information, such as names or email addresses, from comment submissions. Persons should submit only information that they wish to make publicly available. See *Notice to Members 03-73* (Online Availability of Comments) (November 2003) for more information.
4. See Section 19 and rules thereunder. After a proposed rule change is filed with the SEC, the proposed rule change generally is published for public comment in the *Federal Register*. Certain limited types of proposed rule changes take effect upon filing with the SEC. See SEA Section 19(b)(3) and SEA Rule 19b-4.
5. FINRA operates the CRD system pursuant to policies developed jointly with NASAA. FINRA works with the SEC, NASAA, other members of the regulatory community, and member firms to establish policies and procedures reasonably designed to ensure that information submitted and maintained on the CRD system is accurate and complete. These procedures, among other things, cover expungement of customer dispute information from the CRD system in narrowly defined circumstances.
6. For example, broker-dealers use the Uniform Application for Securities Industry Registration or Transfer, referred to as Form U4, to register or transfer the registrations of, associated persons with self-regulatory organizations (SROs), and with states, commonwealths and territories. Also, broker-dealers use the Uniform Termination Notice for Securities Industry Registration, referred to as Form U5, to terminate the registrations of associated persons with SROs, and with states, commonwealths and territories.
7. See *Notice to Members 04-16* (March 2004).
8. FINRA Rule 2080 requires members or associated persons seeking expungement of customer dispute information to obtain an order from a court of competent jurisdiction directing expungement or confirming an arbitration award recommending expungement relief and requires the member or associated person to name FINRA as a party in any judicial proceeding seeking expungement relief. FINRA may, however, waive the requirement to name it as a party if it determines that the requested expungement relief is based on affirmative judicial or arbitral findings that: (1) the claim, allegation or information is factually impossible or clearly erroneous, (2) the associated person was not involved in the alleged investment-

- related sales practice violation, forgery, theft, misappropriation or conversion of funds, or (3) the claim, allegation, or information is false. In addition, FINRA has sole discretion “under extraordinary circumstances” to waive the requirement if the expungement request is meritorious and expungement would not have a material adverse effect on investor protection, the integrity of the CRD system, or regulatory requirements.
9. In 2009, Forms U4 and U5 were amended to add questions that required registered persons to report allegations of sales practice violations made in customer-initiated arbitrations even if they were not named as a respondent in the arbitration. *See* Securities Exchange Act Release No. 59916 (May 13, 2009), 74 FR 23750 (May 20, 2009) (Order Approving SR-FINRA-2009-008); *see also* [Regulatory Notice 09-23](#) (May 2009). Such persons may believe these allegations are unfounded and seek to have them expunged. Because they are not parties to the customer-initiated arbitration, they are unable to seek expungement relief in the Underlying Customer Case.
  10. FINRA Rule 12805 provides that a panel must comply with the following criteria before granting expungement: (1) hold a hearing to decide the issue of expungement; (2) review settlement documents, and consider the amount of payments made to any party, and any other terms and conditions of the settlement; (3) indicate in the award which of the grounds in FINRA Rule 2080 is the basis for expungement and provide a brief written explanation of the reasons for granting expungement; and (4) assess all forum fees for hearing sessions in which the sole topic is the determination of the appropriateness of expungement against the parties requesting expungement relief. *See also* FINRA Rule 13805.
  11. Under the Codes, a pleading is a statement describing a party’s causes of action or defenses (*e.g.*, statement of claim, answer, or counterclaim). *See* FINRA Rule 12100(v).
  12. A hearing session is any meeting between the parties and the arbitrator(s) of four hours or less, including a hearing or prehearing conference. *See* FINRA Rules 12100(p) and 13100(p).
  13. *See* FINRA Rule 12503.
  14. Currently, if an associated person requests expungement relief only in a claim filed separately, the filing fee would be the non-monetary/unspecified claim amount, or \$1,575. *See* FINRA Rules 12900(a) and 13900(a). Associated persons have been adding a monetary claim of less than \$1,000 to a request for expungement relief to reduce the filing fee to \$50. By converting the non-monetary/unspecified claim into a simplified claim, the associated person reduces the number of arbitrators who would hear and consider a complex matter like expungement from three to one. *See* FINRA Rules 12401 and 13401.
  15. A surcharge is assessed against each member that is named as a respondent in or employed, at the time the dispute arose, an associated person who is named as a respondent in a claim, counterclaim, cross claim, or third party claim filed and served under the Codes. *See* FINRA Rules 12901(a)(1)(B) and 12901(a)(1)(C) and FINRA Rules 13901(a)(2) and 13901(a)(3).
  16. Each member that is a party to an arbitration claim in which more than \$25,000 is in dispute is required to pay a process fee based on the amount of the claim. In addition, if an associated person of a member is a party, the member that employed the associated person at the time the dispute arose is charged the process fee, even if the member is not a party. *See* FINRA Rules 12903(a) and (b) and FINRA Rules 13903(a) and (b).

17. Under the Codes, no member is assessed more than a single surcharge or one process fee in any arbitration. *See* FINRA Rules 12901(a)(4) and 12903(b) and FINRA Rules 13901(d) and 13903(b).
18. The proposed amendments would not allow an associated person named in the Underlying Customer Case to file the claim requesting expungement relief against the customer from the Underlying Customer Case.
19. *See* proposed FINRA Rule 13805(a)(3).
20. A customer complaint can be reported to the CRD system via a Form U4 or Form U5. Pursuant to the requirements of FINRA Rule 1010, an associated person should be aware of the filing of a Form U4 by the associated person's member firm, as well as any amendments to the Form U4 to report a customer complaint involving that person. Article V, Section 3 of FINRA's By-Laws requires that a member firm provide an associated person a copy of an amended Form U5, including one reporting a customer complaint involving the associated person. Moreover, FINRA provides several methods for associated persons and former associated persons to check their records (e.g., by requesting an Individual Snapshot or by checking BrokerCheck).
21. *See* proposed FINRA Rule 12100(dd). *See also supra* note 9.
22. The term "Director" means the Director of the Office of Dispute Resolution. Unless the Codes provide that the Director may not delegate a specific function, the term includes staff to whom the Director has delegated authority. *See* FINRA Rules 12100(m) and 13100(m).
23. The text of the form can be found at [www.finra.org/notices/17-42](http://www.finra.org/notices/17-42).
24. Under the proposal, the party may include the request for expungement relief in an answer or pleading.
25. *See* proposed FINRA Rule 13805(a)(3). The unnamed person also would be prohibited from filing an expungement request against a customer.
26. *See supra* note 10.
27. *See* FINRA Rules 12805(a) and 13805(a).
28. *See* FINRA Rules 12805(c) and 13805(c).
29. *Id.*
30. In 2014, FINRA staff revamped the arbitrator training materials and amended them again in 2016.
31. *See supra* note 2.
32. *See* Securities Exchange Act Release No. 48933 (Dec. 16, 2003), 68 FR 74667, 74672 (Dec. 24, 2003) (Order Approving File No. SR-NASD-2002-168).
33. A firm, named as a respondent, would be assessed a member surcharge and process fee as provided under the Codes. *See supra* notes 15, 16 and 17.
34. *See* proposed FINRA Rule 13805(a)(3).
35. *See* FINRA Rule 13400.
36. A public arbitrator is an individual who does not have significant ties to the securities industry. *See* FINRA Rule 13100(x). Arbitrators are eligible to serve as chairpersons if they have completed chairperson training and: (1) have a law degree and are a member of a bar of at least one jurisdiction and have served as an arbitrator through award on at least one arbitration administered by an SRO in which hearings were held; or (2) have served as an arbitrator through award on at least three arbitrations administered by an SRO in which hearings were held. *See* FINRA Rule 13400(c).

37. The first arbitrator selected by NLSS would be the chairperson of the panel. The parties would not be permitted to strike any arbitrators selected by NLSS, but would be permitted to challenge any arbitrator selected for cause, pursuant to FINRA Rule 13410. If an arbitrator is removed, NLSS would randomly select a replacement subject only to a challenge for cause. The parties would not be permitted to agree to fewer than three arbitrators on the panel, and the parties would not be permitted to stipulate to the use of pre-selected arbitrators. Finally, if the associated person withdraws the claim after a panel is appointed, the case would be closed with prejudice, unless the panel decides otherwise. *See* proposed FINRA Rule 13806.
38. The Task Force suggested that the arbitrators be chair-qualified. In addition, it suggested that the arbitrators who would serve on the special arbitrator panel complete enhanced expungement training. FINRA agrees that the training for arbitrators selected for the Expungement Arbitrator Roster should be expanded. Thus, FINRA would create training for these arbitrators, which would emphasize that, if there is no party opposing the associated person's request for expungement relief, the panel would need to review more proactively the request and documentation and, if necessary, ask questions and for more information, before making a decision. The training would also focus on the need to identify one or more of the grounds for expungement in FINRA Rule 2080(b)(1) as the basis for expungement.
39. The panel would determine the method of appearance.
40. *See* FINRA Rules 12800(a) – (c); *see also* FINRA Rules 13800(a) – (c).
41. *See* FINRA Rules 12805(a) and 13805(a).
42. *See* proposed FINRA Rule 12800. FINRA Rule 13800 would also be amended to require that an associated person may only request expungement of customer dispute information under Rule 2080 by filing the request pursuant to Rule 13805(a) at the conclusion of the simplified arbitration case.
43. FINRA Rule 12800(c)(1) permits a customer to request a hearing. Under the proposal, if a customer requests a hearing, the arbitrator would decide the customer's case and at the conclusion of the customer's case, the associated person could file the expungement request against the firm and a panel from the Expungement Arbitrator Roster would decide the request. *See also* FINRA Rule 13800(c)(1).
44. Among the 2,232 customer arbitration cases and 183 intra-industry arbitration cases (mentioned above) that involve an expungement request of customer dispute information, 67 (3 percent) of the cases had an initial filing fee of \$50.
45. Researchers find a negative relationship between misconduct disclosures on CRD and the employment opportunities of associated persons. The misconduct disclosures in their analysis, however, include more than just customer allegations. *See* Mark Egan, Gregor Matvos, and Amit Seru, *The Market for Financial Adviser Misconduct*, 2016.
46. Among the 2,232 customer arbitration cases and 183 intra-industry arbitration cases (mentioned above) that involve an expungement request of customer dispute information, approximately one-fifth of the expungement filing fees would have increased to \$1,425 under the proposed amendments. The increase in fees would range from \$450, for claims greater than \$50,000 but less than or equal to \$100,000 which currently have a filing fee of \$975, to \$1,375, for claims with a monetary value of less than or equal to \$1,000 which currently have a filing fee of \$50.

**EXHIBIT 2b**

**Alphabetical List of Written Comments  
Regulatory Notice 17-42**

1. John B. Anzaldua (“Anzaldua”) (February 5, 2018)
2. Josh Barber, CRC Search (“Barber”) (December 12, 2017)
3. Walter Baumgardner, Esq. (“Baumgardner”) (December 27, 2017)
4. Ralph S. Behr, Esq. (“Behr”) (January 11, 2018)
5. Barbara Black (“Black”) (February 5, 2018)
6. Joseph Borg, North American Securities Administrators Association (“NASAA”) (February 5, 2018)
7. Juan Braschi, Merrill Lynch Global Wealth Management (“Braschi”) (January 25, 2018)
8. Scott Brookes (“Brookes”) (January 25, 2018)
9. Donna Burrill (“Burrill”) (January 25, 2018)
10. Michael Butt (“Butt”) (January 31, 2018)
11. Kevin Carroll, Securities Industry and Financial Markets Association (“SIFMA”) (February 5, 2018)
12. Steven B. Caruso, Maddox Hargett & Caruso, P.C. (“Caruso”) (January 30, 2018)
13. Peter Chepucavage (“Chepucavage”) (January 11, 2018)
14. Tony Christ (“Christ”) (January 25, 2018)
15. Roger B. Deal, Sequoia Wealth Partners, LLC (“Deal”) (February 1, 2018)
16. Dr. Kelly A. Decker (“Decker”) (January 27, 2018)
17. Benjamin Dell’Orto, Esmat Hanano, Alisa Radut & Nicole G. Iannarone, Georgia State University College of Law, (“Georgia State”) (February 5, 2018)
18. Michael J. Di Silvio, Di Silvio Financial Group (“Di Silvio”) (January 25, 2018)
19. G. Thomas Fleming III & Kevin K. Fitzgerald, Jones, Bell, Abbott, Fleming & Fitzgerald L.L.P. (“JonesBell”) (January 9, 2018)

20. Rick A. Fleming, Tracey L. McNeil, Office of the Investor Advocate, U.S. Securities and Exchange Commission (“The SEC Investor Advocate”) (February 15, 2018)
21. Kelly Frevele, Sigourney Norman & Christine Lazaro, St. John’s University School of Law (“St. John’s”) (February 5, 2018)
22. David W. Gamblin, Morgan Stanley Wealth Management (“Gamblin”) (January 26, 2018)
23. Stacey M. Garrett, Keesal, Young & Logan (“Keesal”) (February 1, 2018)
24. Edward A. Glenn, Morgan Stanley Wealth Management (“Glenn”) (January 31, 2018)
25. Gregory Gocek (“Gocek”) (December 7, 2017)
26. Tosh Grebenik, FA Expungement, LLC (“FA Expungement”) (January 29, 2018)
27. Jonathan Hagenstein (“Hagenstein”) (January 25, 2018)
28. Susan Harley & Remington A. Gregg, Public Citizen (“Public Citizen”) (February 5, 2018)
29. David Harmon, AXA Advisors, LLC (“Harmon”) (December 29, 2017)
30. Eric Harris (“Harris”) (December 9, 2017)
31. Robert L. Herskovits, Herskovits PLLC (“Herskovits”) (January 6, 2018)
32. Jay R. Higgenbotham, Merrill Lynch, Pierce, Fenner & Smith Incorporated (“Higgenbotham”) (February 1, 2018)
33. Jim Isola (“Isola”) (January 25, 2018)
34. William A. Jacobson, Esq. & Joshua N. Shinbrot, Cornell University Law School (“Cornell”) (February 5, 2018)
35. David Wm. James, Legacy Planning Group, Inc. (“James”) (February 2, 2018)
36. Catherine Joyce, Morgan Stanley Wealth Management (“Joyce”) (January 24, 2018)
37. Kristopher J. Kalkowski, Jacob Crawley & Omar Nagy, UNLV School of Law, (“UNLV”) (February 5, 2018)
38. William Leven, Private Banking and Investment Group (“Leven”) (January 25, 2018)

39. Dave Liebrader (“Liebrader”) (February 5, 2018)
40. John C. Lindsey, Lindsey & Lindsey (“Lindsey”) (February 25, 2018)
41. Patrick R. Mahoney, The Law Offices of Patrick R. Mahoney, P.C. (“Mahoney”) (February 5, 2018)
42. Mimi B. Osiason, LBO Consulting (“Osiason”) (December 7, 2017)
43. Andrew Penzell (“Penzell”) (February 1, 2018)
44. Leonardo Ramirez (“Ramirez”) (January 26, 2018)
45. Andy Rieger, Morgan Stanley Wealth Management (“Rieger”) (February 1, 2018)
46. David E. Robbins, Kaufmann Gildin & Robbins LLP (“Robbins”) (December 27, 2017)
47. Elena Rodriguez (“Rodriguez”) (December 9, 2017)
48. Virgil O. Rosser IV, Wells Fargo Advisors (“Rosser”) (January 25, 2018)
49. Armin Sarabi, AdvisorLaw, LLC (“AdvisorLaw”) (February 2, 2018)
50. Gary M. Saretsky, Jonathan M. Sterling & Collen M. Nickel, Saretsky Hart Michaels + Gould PC (“Saretsky”) (February 5, 2018)
51. Daniel A. Schlein, The Law Office of Daniel Schlein (“Schlein”) (February 3, 2018)
52. Gregory Scrydloff (“Scrydloff”) (January 31, 2018)
53. David Shields, Wellington Shields & Co. LLC (“Wellington”) (February 1, 2018)
54. Rod I. Skaf, SKAFCO (“Skafco”) (January 26, 2018)
55. Lance W. Slaughter, Wells Fargo Advisors (“Slaughter”) (January 26, 2018)
56. Barrick A. Smart, Smart Investments Advisory Inc. (“Smart”) (January 31, 2018)
57. Neil H. Smith (“Smith”) (January 26, 2018)
58. W. Alan Smith, Janney Montgomery Scott LLC (“Janney”) (February 5, 2018)
59. Jeff Speicher, Wells Fargo Advisor (“Speicher”) (January 26, 2018)
60. Denise M. Stephens, Princeton Financial Services, Inc. (“Stephens”) (February 1, 2018)

61. John D. Stewart, Baritz & Colman LLP (“Baritz”) (February 5, 2018)
62. Nancy Stewart (“Stewart”) (January 25, 2018)
63. Andrew Stoltmann, PIABA (“PIABA”) (February 2, 2018)
64. Jason S. Tinklenberg, LongView Financial Solutions (“Tinklenberg”) (July 5, 2018)
65. Robin Traxler, Financial Services Institute (“FSI”) (February 5, 2018)
66. Joe Tully, Commonwealth Financial Network (“Commonwealth”) (February 5, 2018)
67. Leslie M. Walter, JD (“Walter”) (February 5, 2018)
68. Stacie Weinerf, RBC Wealth Management (“Weinerf”) (February 1, 2018)
69. Brooks White (“White”) (January 15, 2018)
70. Greg Zanolli, Wells Fargo Advisors (“Zanolli”) (January 25, 2018)

**Exhibit 2c**

I had three complaints that were put in my U-4 all when I worked at Wells Fargo about 2 years after I left USBancorp Investments. I received a letter from A USBancorp Investments to notify me of my right to give input or show up in arbitration the very day that I received the letter. I talked to the attorney for B of A that defended Banc of America Investments. He settled because two of the three Guy Francis accounts were not marked aggressive. Even though I told my assistant to put down that they were all aggressive.

Two out of three complaints were strongly denied by the B of A as having no merit. I had a written record in the Francis file at B of A that confirmed that I had suggested more conservative options and strongly suggested that they make technology less than 10% of the portfolio because it was "way" overvalued. Guy Francis insisted that he wanted at least 40% in tech. At least three of the funds I was forced to sell if I wanted to "keep my job", were B of A mutual funds that were sued for fraud and they had no replacement broker for me in those approximate two years to guide clients in the 2000-2003 bear market. So of course B of A wanted to settle as they have many times done the same to other brokers. The person that alleged fraud was a "trust fund baby" that had as many as 10 bank accounts and actually made (about) 7% rate of total return. He complained because he was told by my eventual replacement at Banc Of America Investments that he had lost "a lot of money. This investment was in Ginnie Maes and according to the branch manager (Rob Pappani) this new broker told virtually everyone I had worked with that whatever they had was a terrible investment and should be sold so that they could "buy something good".

In summary I had no ability to defend myself in arbitration with any of the three complainants. I was given two complaints with zero merit that I was told could be expunged by (a female attorney that worked in the FINRA office in San Francisco at that time). I don't want to hire an attorney but two have offered to take these two zero merit cases to arbitration as they believe that they will be expunged in arbitration. Please look at my response on my u-4 for details on the three cases that are on my record. I think it will save us both time and money and it's not fair to have these two cases on my record as these two have unfairly hurt my ability to get new clients for myself and my family for these 15+ years.

Thanks for taking the time to read this.

John B. Anzaldua CRD # 2107126

I fully support and understand that we need to protect the investing public but when 8 out of 10 customer dispute disclosures are forced settlements by the advisor's firm because they don't want to spend the money to fight a costly legal battle, then who wins under the purposed rules that don't allow meritless claims to come off a record. The answer is pretty simple. Its all of the lawyers that know they can sue any advisor and 8 times out of 10 they know they will get a settlement. The expungement process, especially being able to expunge old meritless claims, gives some balance to the system. In the current environment, an advisor can have the claim removed when they have the money to get the work done whether that's 6 months from the allegation or 6 years. After reading through the proposed changes, the industry can live with most of proposed changes but please keep an open mind on allowing older disclosures that are meritless to have some rule to allow an advisor to get them removed. It seems like the rule changes were written by the lawyers that profit off of suing the advisors. That group has a lot of power and influence with FINRA but their approach is not to protect the investor. Its to sue as many advisors as possible to make a pay check. How about FINRA looks to ban the individual websites those attorney's run on advisors in almost every major market in the US where they name advisors by name and then use SEO to push that website high in the search results when the advisors name is typed into Google. Those sites are defaming advisors even when their claims are denied, closed no action, withdrawn yet they do a great job of drumming up more meritless claims on advisors. Again, we all want to see the bad apples removed from the business but it needs to be a fair system and the lawyers can't have all of the power. Somebody also needs to look out for the advisors that are being abused and part of that is giving them a mechanism to have fraudulent allegations removed from their public record.

My voice doesn't mean much but please consider a more balanced approach. Advisors need to be able to remove old claims that have no merit. Why force an advisor to live with a denied, closed no action or a withdrawn claim for their entire career. Maybe even look at the settlements where alleged damages are massive but the actual settlement is a small fraction of the amount. Those are so obvious what happened when you read them its silly that they cant get those removed.

Best regards,

*Josh Barber*

Managing Partner – Executive Recruiting  
719-445-8818



Dear Ms. Asquith: I have successfully expunged a record of a registered representative. With that as background, if FINRA is going to make it harder to expunge a complaint, then it must make it harder for complaints to appear on a registered representative record. The black mark should not appear until there has been an adjudication of the arbitration or the enforcement action.

A prime example of the mischief that can occur is the reporting of the limited partnership fraud committed by Prudential Securities in the sale of limited partnerships. While the company admitted the products were flawed and accepted responsibility for the fraud, the sale of the partnerships ended up on the registered representatives CRD.

Walter Baumgardner, Esq.

**RALPH S. BEHR**  
**ATTORNEY AT LAW**  
**12 SOUTHEAST 7<sup>TH</sup> STREET, SUITE 609**  
**FORT LAUDERDALE, FLORIDA 33301**  
**TELEPHONE 954-761-3444**

EMAIL: RB.BEHLAW@GMAIL.COM

January 11, 2018

**Sent Via U.S. Mail**

Financial Industry Regulatory Authority  
Attn: Marcia E. Asquith  
Office of the Corporate Secretary  
1735 K Street NW  
Washington, DC 20006-1506

Re: **FINRA Regulatory Notice 17-42**  
**(December 6, 2017)**

Dear Mrs. Asquith:

I write to endorse the cogent and prescient arguments contained in a comment submitted by the firm of Jones Bell dated January 9, 2018 and noted as received by FINRA on January 10, 2018.

I would only add the following comment:

The essence of Due Process is fundamental fairness. FINRA as an industry regulator must maintain both the appearance of fairness and effectuate processes that are fundamentally fair: fair to all parties.

The perceived and actual effect of the proposed amendments fails to meet even a casual due process review.

Accordingly, I urge FINRA to reject Regulatory Notice 17-42.

Very truly yours,

  
Ralph S. Behr, Esq.

cc: Jones, Bell, Abbott, Fleming & Fitzgerald, L.L.P.

## **Regulatory Notice 17-42**

### **FINRA Requests Comment on Proposed Amendments to the Codes of Arbitration Procedure Relating to Requests to Expunge Customer Dispute Information**

I served as Chair of the FINRA Dispute Resolution Task Force that was formed in June 2014 to consider possible enhancements to FINRA's arbitration and mediation forum, in order to ensure that the forum meets the evolving needs of participants. I am also a Chair-qualified public arbitrator who has participated in many arbitration cases, including expungement hearings. I submit these comments in my individual capacity, to provide background on the task force's recommendations on expungement and to express my personal support for the proposed amendments set forth in Regulatory Notice 17-42.

The task force set forth 51 recommendations in its final report, released in December 2015, including three important recommendations relating to expungement. During its deliberations, the task force was advised that FINRA and NASAA were in the process of discussions with regard to the expungement process, and consideration was being given to converting the process into a regulatory procedure. The task force took no position on whether a regulatory approach should eventually replace the current expungement process. Because of uncertainty about the ultimate outcome of the NASAA/FINRA discussions, the task force gave serious consideration to the creation of a special arbitration panel consisting of specially trained arbitrators to decide requests for expungement. Specifically, the task force recommended (1) the creation of a pool of trained, experienced arbitrators to conduct expungement hearings in settled cases and in all cases where claimants did not name the associated person as a respondent. The task force also recommended (2) development of enhanced arbitrator training with regard to the expungement process, including clearer guidance on the Rule 2080 grounds for expungement, which would be required of all chairpersons who conduct expungement hearings, and (3) review of procedures for notifying state regulators of expungement requests.

I support FINRA's proposed amendment to establish a roster of public arbitrators with additional qualifications (Expungement Arbitrator Roster) to decide expungement requests filed against a firm under the Industry Code, because it is similar to the task force's recommendation (1). In addition, I am pleased that FINRA recognizes the need for enhanced expungement training and commits to "create training for these arbitrators, which would emphasize that, if there is no party opposing the associated person's request for expungement relief, the panel would need to review more proactively the request and documentation and, if necessary, ask questions and for more information, before making a decision" (note 38). The task force's recommendation (2) would also extend required enhanced arbitrator training to chairpersons who conduct expungement hearings in cases decided after a hearing. The task force was of the view that, in all cases involving expungement, enhanced arbitrator training was of great importance. Because of the importance of maintaining the integrity of the CRD system, only information that is demonstrably unfounded, and thus of no investor protection or regulatory value, should be expunged.

Regulatory Notice 17-42 specifically asked for comment on certain aspects of the proposed amendment:

1. I agree that the rule should be amended from “grant” to “recommend” expungement, to reflect more accurately the process and the consequences of the arbitration panel’s decision. Simply stated, the arbitration panel does not “grant” expungement, as its decision must be confirmed by a court, and FINRA has the authority to oppose confirmation.

4. I strongly support the proposed amendment to require unanimous consent for panel decisions to recommend expungement. The existence of a customer’s complaint—regardless of its merits—is an accurate reflection of the historical record, so a strong argument can be made that expungement should rarely, if ever, be granted. Yet there has long been a tension between the importance of accurate historical information and the harm that can result to an associated person if a customer’s complaint is unfounded. Requiring unanimous consent to recommend expungement is an appropriate way to balance these competing tensions. It is similar to the rationale for other decisions that require unanimous consent (motions to dismiss, eligibility rule motions): these are decisions that involve an integral part of the arbitration process. It serves as an assurance that all members of the panel have found that one of the grounds of Rule 2080(b)(1) is present and that there is no investor protection or regulatory value to the complaint, allegation or information. As a chair, I strive for unanimity on all important decisions, and it is my understanding that this is the practice of many experienced chairs. Because of the importance of the integrity of the CRD system, I believe the benefit of assuring the integrity of the CRD system greatly exceeds the cost that in a divided decision an associated person will not be granted expungement.

(5) and (10) I support the proposed amendment to establish a one-year limitation period for filing expungement requests both in cases where the expungement request was not decided during the underlying customer case and in cases where the customer dispute information has not resulted in an underlying customer case within one year of the member firm initially reporting the customer complaint to CRD. It can be difficult for a panel to determine whether one of the grounds of Rule 2080(b)(1) exists without the investor’s testimony. With the passage of time it becomes less likely that investors will be available and willing to testify in a proceeding in which they have no financial stake. A one-year limitations period should allow for sufficient time for an associated person to file an expungement request.

(6) I strongly support requiring the associated person to testify in person; if that is not practical, then testimony via video conferencing may be acceptable. I have participated in expungement hearings where the associated person testified in person and in expungement hearings where the associated person testified via telephone. Based on my experience, telephonic testimony is not an adequate substitute when issues of intent and credibility are involved, as is typically the case in expungement hearings. The arbitration panel needs to look the associated person in the eye and observe the person’s demeanor.

(8) I do not oppose the proposed requirement that arbitrators on the Experienced Arbitrator Roster are attorneys with five years' experience in a relevant discipline, but the cost of these additional qualifications is that there will likely be fewer eligible arbitrators. The requirement of completed enhanced expungement training in lieu of additional qualifications may allow for more eligible arbitrators.

Thank you for providing the opportunity to comment on these proposed amendments.

Barbara Black

Professor of Law, University of Cincinnati College of Law (Retired)

Feb. 5, 2018



February 5, 2018

*Submitted electronically to [pubcom@finra.org](mailto:pubcom@finra.org)*

Marcia E. Asquith  
FINRA Office of the Corporate Secretary  
1735 K Street, NW  
Washington, DC 20006-1506

**RE: FINRA Regulatory Notice – 17-42 – Proposed Amendments to the Codes of Arbitration Procedure Relating to Requests to Expunge Customer Dispute Information**

Dear Ms. Asquith,

On behalf of the North American Securities Administrators Association (“NASAA”),<sup>1</sup> I hereby submit the following comments in response to FINRA Regulatory Notice 17-42 (“the Proposal”), issued on December 6, 2017.<sup>2</sup> NASAA has a long-standing interest in ensuring that there is no compromise in the integrity of the information housed on the Central Registration Depository (“CRD”) and its investment adviser equivalent, the Investment Adviser Registration Depository (“IARD”).<sup>3</sup> Each system contains the information filed with state securities administrators by applicants for registration as broker-dealers, investment advisers, and their representatives. In addition to using that information as part of licensing and ongoing oversight responsibilities,<sup>4</sup> state securities administrators are obligated under state securities and public records laws to ensure that records are maintained in accordance with those laws. These laws almost universally require the retention of all information filed as part of a registration application and amendments to the application. NASAA has gained a unique expertise in this area, as we have been involved in developing—and reforming—the expungement process since its inception, and are pleased to offer our comments on the Proposal.<sup>5</sup>

<sup>1</sup> NASAA is the association of the 67 state, provincial, and territorial securities regulatory agencies of the United States, Canada, and Mexico. NASAA serves as the forum for these regulators to work with each other in an effort to protect investors at the grassroots level and to promote fair and open capital markets.

<sup>2</sup> FINRA Regulatory Notice 17-42 – *Expungement of Customer Dispute Information – Proposed Amendments to the Codes of Arbitration Procedure Relating to Requests to Expunge Customer Dispute Information* (Dec. 6, 2017), available at [http://www.finra.org/sites/default/files/notice\\_doc\\_file\\_ref/Regulatory-Notice-17-42.pdf](http://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-17-42.pdf).

<sup>3</sup> FINRA, NASAA, and state securities regulators developed the CRD system collaboratively and jointly administer policies related to the jointly owned licensing information held on CRD. The IARD is an electronic filing system for investment advisers sponsored by the Securities and Exchange Commission and NASAA, with FINRA serving as the developer and operator of the system. See [www.iard.com](http://www.iard.com).

<sup>4</sup> E.g. completing broker-dealer and investment adviser examinations and bringing enforcement actions.

<sup>5</sup> Most recently, NASAA laid out its views regarding expungement in a letter to FINRA’s Arbitration Task Force. See Letter from William Beatty, NASAA President and Washington Director of Securities, to Barbara Black, FINRA Dispute Resolution Taskforce, Re, NASAA Comments on Expungement of Matters from the Central

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NASAA's position on expungement is clear: expungement is an extraordinary remedy to be granted solely in limited circumstances and the current process has failed to properly maintain the limited scope of this remedy.<sup>6</sup> In its 2015 letter, NASAA urged FINRA's Arbitration Taskforce, at a minimum, to endorse short-term solutions that would improve the existing expungement process, while regulators worked on more substantial reforms.<sup>7</sup> In the current Proposal, FINRA has taken a necessary first step towards those short-term solutions in meaningful expungement reform by proposing thoughtful amendments designed to mitigate some of the long-recognized issues with the existing expungement process. We appreciate and agree with the recognition that the Proposal is only a first step and reiterate our commitment to work with FINRA to implement more substantial regulatory reforms than those contemplated by the Proposal.

NASAA supports FINRA's efforts in the Proposal, but, along with FINRA, remains concerned with how far the current expungement process has strayed from the original intent of Rule 2080 and related arbitration rules. FINRA Rule 2080 and prior versions of the rule established a process designed to end the practice of arbitration panels granting expungement without clear criteria, regulatory participation, and court involvement.<sup>8</sup> The Proposal builds upon the original procedural framework by adding beneficial requirements and limitations related to the procedure of expungement. While NASAA supports the Proposal as an important first step, certain aspects of the proposed changes require further consideration.

#### Unanimity and In-Person Requirements

NASAA supports the proposed requirement that all expungement recommendations be made unanimously by a three-person arbitration panel. Given the extraordinary nature of expungement relief, it is inappropriate to recommend expungement without the agreement of the full arbitration panel. A divided panel indicates that there is doubt that the broker has met the

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Registration Depository, ("2015 Letter") (Aug. 31, 2015), available at <http://nasaa.cdn.s3.amazonaws.com/wp-content/uploads/2011/07/NASAA-Expungement-Letter-enclosure.pdf>.

<sup>6</sup> *Id.* See also, Letter from Joseph Borg, NASAA President, to Barbara Sweeney, Secretary NASD Regulation, Inc., Re, Request for Comments – 01-65 Proposed Rules and Policies Relating to the Expungement of Information from the Central Registration Depository (December 31, 2001) available at <http://www.nasaa.org/wp-content/uploads/2011/07/95-Letter.37262-47637.pdf> ("NASAA 2001 Letter"); Letter from Deborah Bortner, NASAA CRD Steering Committee Co-Chair, to Margaret H. McFarland, Deputy Secretary, U.S. Securities and Exchange Commission, Re, File No. SR-NASD-2002-168; Proposed Rule 2130 Concerning the Expungement of Customer Dispute Information from CRD (June 4, 2003) available at <http://www.nasaa.org/wp-content/uploads/2011/07/82-ProposedNASDRule-202130.37775-72237.pdf> ("NASAA 2003 Letter"); Letter from Karen Tyler, NASAA President, to Nancy M. Morris, Secretary, U.S. Securities and Exchange Commission, Re, Release No. 34-57572; File No. SR-FINRA-2008-010, Notice of Filing of Proposed Rule Change Relating to Amendments to the Codes of Arbitration Procedure To Establish New Procedures for Arbitrators To Follow When Considering Requests for Expungement Relief (April 24, 2008) available at <http://www.nasaa.org/wp-content/uploads/2011/07/31-Release-No34-57572SR-FINRA-2008-010NASAA.pdf> ("NASAA 2008 Letter"); Letter from Andrea Seidt, NASAA President, to Elizabeth M. Murphy, Secretary, U.S. Securities and Exchange Commission, Re, Release No. 34-71959, File No. SR-FINRA-2014-020 Notice of Filing of a Proposed Rule Change to Adopt FINRA Rule 2081 (Prohibited Conditions Relating to Expungement of Customer Dispute Information) (May 14, 2014) available at <http://www.nasaa.org/wp-content/uploads/2011/07/NASAA-Comment-Letter-Release-No-34-71959-File-No-SR-FINRA-2014-020.pdf> ("NASAA 2014 Letter").

<sup>7</sup> See NASAA 2015 Letter, *supra* note 4, at 6.

<sup>8</sup> See *id.* at 3-6 (discussing the original intent of Rule 2080 and its predecessor rule).

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higher burden attendant to eligibility for extraordinary relief, and thus should not merit an expungement recommendation. NASAA supports FINRA's recognition of the import of this decision and supports FINRA's corresponding proposal to eliminate the option to have a single arbitrator in a simplified arbitration proceeding make an expungement recommendation.

NASAA also supports the Proposal's requirement that a broker requesting expungement be present for an in-person hearing on his or her request. NASAA does not believe, however, that the proposed in-person requirement should be satisfied by appearing via video conference. Requiring a broker to be physically present during an expungement hearing is not an unreasonable burden given the extraordinary relief the broker is seeking.

As discussed in more detail below, however, NASAA opposes the inclusion of what it sees as a new "prong" to Rule 2080 by way of proposed changes to the expungement rules in the Code of Arbitration; namely, that arbitrators be required to make a finding that the customer dispute information that is the subject of the expungement petition has no regulatory or investor protection value. This "value" determination should be reserved for regulators.

#### Expungement-Only Arbitration Panels

NASAA also supports the Proposal's requirement that arbitration matters involving an expungement request that are not decided during the underlying customer case be heard by a specialized panel of arbitrators with particular expertise and training. In NASAA's experience, the majority of expungement requests are made in arbitration matters in which the underlying customer dispute is settled. As NASAA has noted previously, post-settlement expungement hearings often consist of a one-sided presentation of the facts, as investors and their counsel—the only other party in the case—have little incentive to participate after the investor's concerns have been resolved.<sup>9</sup> While an expungement-only arbitration panel does not fully address NASAA's concerns related to expungement recommendations based on one-sided proceedings, requiring such requests be heard by specially trained and experienced arbitrators is a good first step.<sup>10</sup>

In the Proposal, FINRA lays out the necessary qualifications for arbitrators on expungement-only panels.<sup>11</sup> NASAA supports the proposed additional qualifications.<sup>12</sup> NASAA generally agrees with FINRA's assessment that individuals meeting the proposed requirements would "better understand the unique nature of this extraordinary remedy and the importance of

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<sup>9</sup> *Id.* at 4-5. See also NASAA 2003 Letter, *supra* note 5.

<sup>10</sup> NASAA has previously advocated that an expungement-only panel is an important interim step in expungement reform. See 2015 NASAA Letter, *supra* note 4, at 7.

<sup>11</sup> See the Proposal, *supra* note 2, at 10 (requiring that the Expungement Arbitrator Roster only include public chairpersons that have completed advanced expungement training, licensed to practice law, and have at least five years of relevant experience).

<sup>12</sup> FINRA recently changed its definition of public arbitrators to exclude certain lawyers from serving as public arbitrators if their practice involves representing clients in certain investment related actions. In NASAA's view, this limitation could create an artificially shallow pool of arbitrators for expungement-only panels due to the requirement that these arbitrators be attorneys and potentially have regulatory experience. FINRA should consider allowing lawyers that represent clients in investment-related cases serve on expungement-only panels.

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maintaining the integrity of the public record.”<sup>13</sup> However, the extent to which these expungement-only panels truly appreciate the nuanced regulatory issues related to expungement largely depends on the content and effectiveness of the proposed “enhanced expungement training” and future substantive changes to the qualification prongs in Rule 2080. NASAA encourages FINRA to consult with state regulators when developing this new training program.

#### Requiring Named Brokers to Request Expungement during the Underlying Customer Case

If adopted, the Proposal would require brokers named as a party in a customer-initiated arbitration to request expungement in the course of the underlying dispute. NASAA supports this proposed change. As the Proposal notes, “some associated persons have filed requests seeking to expunge customer dispute information years after FINRA has closed the Underlying Customer Case.”<sup>14</sup> This lack of timeliness of expungement requests is a significant concern for NASAA and its members. As more time passes, evaluating the merits of a request for expungement becomes more challenging. When expungement requests lack timeliness, it can be difficult or impossible to locate relevant individuals or documents, as FINRA notes in the Proposal.<sup>15</sup> Requiring named brokers to bring their expungement requests during the underlying customer case goes a long way at closing a significant loophole in the current expungement process.

While this amendment, if adopted, would likely result in timelier expungement requests, it does not fully address—and nor do the other aspects of the Proposal—the problems created by the current Rule 2080’s procedural nature. Correcting these issues is a main focus of NASAA’s continued work to reform expungement. Further, because the Proposal does not fully address the shortcomings of the current Rule 2080 process due to its procedural nature, it is imperative that FINRA, as it has acknowledged in the Proposal, views the proposed changes as the starting point, not the finish line, for expungement reform.

#### Changes for Unnamed or “Subject of” Brokers

The Proposal would codify a FINRA-member firm’s ability, with the broker’s consent, to request expungement on behalf of a broker who is unnamed in a customer arbitration but is the “subject of” the dispute.<sup>16</sup> In the event that a firm does not request expungement on behalf of an unnamed broker, the unnamed broker would be required to bring a request for expungement within one year after the closing of the underlying customer case.<sup>17</sup> As further steps toward reforming the expungement process, NASAA supports this requirement along with the provision in the Proposal that would prevent an unnamed broker from filing an arbitration claim seeking expungement against an investor.

While NASAA supports the proposed changes related to expungement requests by unnamed or “subject of” brokers, particularly the one-year time limitation and prohibition on

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<sup>13</sup> See the Proposal, *supra* note 2, at 10.

<sup>14</sup> *Id.* at 5.

<sup>15</sup> *Id.*

<sup>16</sup> *Id.* at 7-8.

<sup>17</sup> *Id.* at 8.

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actions against investors, there are challenges in allowing firms to bring actions on behalf of brokers. Such an approach would require cooperation between the firms and the relevant brokers. This cooperation may not always exist, particularly in cases in which brokers are no longer associated with the relevant firm or the firm's and the broker's pecuniary interests diverge. As a result, the processes and procedures used by FINRA to notify unnamed brokers about closed matters is particularly important as that notice triggers the proposed one-year time limitation. If the Proposal is adopted, FINRA would be required to develop robust, mandated notification procedures to limit potential disputes regarding whether subsequent expungement requests are timely.<sup>18</sup>

### Increased Fees

The Proposal would also require brokers seeking expungement to pay additional fees. FINRA and the states expend significant resources in reviewing expungement requests. While the increase in fees does not directly offset those costs, the increased fees would at least in part reduce the costs FINRA incurs in responding and processing expungements. NASAA therefore supports this proposed change.

### Further Expungement Reform is Required

In 2003, NASAA agreed with the very limited expungement process for removing certain limited information from the CRD originally memorialized in the provisions of Rule 2130. At the time, Rule 2130 appeared to provide a better solution for expunging a broker's CRD records, as the then-NASD was expunging records solely based on recommendations from arbitrators without the standards of factual impossibility, lack of involvement, and false claims or allegations as set forth in the rule.<sup>19</sup> Unfortunately, this framework has failed, and is applied in a way that favors the interests of a single registrant over regulatory imperatives and the public interest. As indicated above, the Proposal, if implemented, would improve the existing expungement process, and NASAA applauds FINRA for this step towards meaningful expungement reform.

Expungement of a broker's CRD record is an extraordinary remedy. If the remedy remains commonplace and routine grants are not curtailed, the ongoing deletion of disclosure information from CRD will result in a loss of confidence in the CRD system.<sup>20</sup> Moreover, regularly expunging this information could lead to distrust in the other regulatory safeguards that rely on the information housed in the CRD. Without more significant reforms, the existing expungement process will continue to result in the deletion of critically valuable regulatory information from the

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<sup>18</sup> NASAA also notes the potential for workability complications related to brokers bringing actions against firms that are out of business and/or no longer FINRA members. This issue is also presented by the Proposal's formal expansion of the Rule 2080 process to mere customer complaints, which is addressed in more detail below. In this context, NASAA again sees practical concerns with the requirement that brokers bring claims against the firm they were associated with at the time of the customer complaint.

<sup>19</sup> Currently codified in Rule 2080(b)(1).

<sup>20</sup> In the Proposal, FINRA acknowledges that between 2014 and 2016 arbitrators granted 75% of the expungement requests they decided. See The Proposal, *supra* note 2, at 13-14. This makes clear that expungement is no longer an extraordinary remedy.

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CRD. If such information continues to be removed without meaningful consideration as to its regulatory value, regulators, industry, and investors can no longer trust that the data in the CRD contains all of the information necessary to make licensing and hiring decisions or to determine which financial professional to entrust with an investor's financial future.

The Proposal attempts to recognize the important regulatory value of customer complaint information by requiring arbitrators make a specific finding that information that is the subject of an expungement request has no regulatory or investor protection value before granting an expungement request.<sup>21</sup> NASAA appreciates FINRA's efforts to enhance its expungement rules by requiring arbitrators to make this important determination before granting an expungement request. However, this is a regulatory determination, which cannot be shifted to arbitrators selected to resolve a dispute pursuant to a contract between private parties. It would be inappropriate to deputize arbitrators and usurp a regulator's responsibilities.

In fact, regulators have already determined that customer complaint information has investor protection and regulatory value by requiring brokers to disclose it. By requiring the disclosure of this information on uniform registration forms, securities regulators—state and federal—have concluded that *all* customer complaint information within defined parameters is *presumptively* valuable. The presumptive value of this information underpins the premise that the expungement of any information is an extraordinary remedy.

NASAA, however, recognizes that there are certain very narrow situations in which customer complaint information should be expunged; namely, when, as the result of an error in responding to the questions on registration forms soliciting customer complaint information, such information is reported and subsequently disclosed publicly. Despite the intended rare recommendation contemplated by the original rules, expungement under the current Rule 2080 process is all too frequently recommended. NASAA can point FINRA to myriad examples where the current process has failed by recommending that valuable regulatory information be removed from the system, and is willing to provide these cases should FINRA find them useful. Because regulators have already determined the presumptive value of customer complaint information by requiring that it be disclosed, regulators have a responsibility to ensure such information is in fact disclosed and maintained. The expungement process cannot be used to routinely reverse these important regulatory disclosures.

Consequently, NASAA opposes the Proposal's expansion of the types of customer complaint information that would be subject to expungement under the Rule 2080 process. We recognize that there is increasing use of the expungement process beyond the scope originally intended with the rules now being used to address expungement requests related to customer *complaints* that were *not* the subject of arbitration. NASAA objects to expanding the scope of Rule 2080 to apply to all information related to customer complaints. Such an approach would further embed a flawed process that does not afford regulators the ability to preserve information already considered to have regulatory value and provide investor protection.

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<sup>21</sup> See *id.* at 3, 9-10.

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The Proposal would reward brokers who capitalize on the procedural nature of the rule and seek to expand its scope beyond arbitrated complaints. In NASAA's view, now is not the time to codify and expand an already broken process. Despite the Proposal's attempt to apply some limitations, formalizing a process to expunge customer *complaints* without a full vetting of the policy implications and collateral consequences of such a rule is not appropriate.<sup>22</sup> While this is an issue that FINRA and NASAA need to address as we continue to rework the expungement issue, expanding the scope of a flawed approach through this Proposal is not the appropriate approach to address this matter.

Finally, one of the primary areas that the amendments in the Proposal does not, and as a procedural proposal cannot, successfully address is the fact that more and more brokers are bypassing the Rule 2080 process entirely by going directly to court. Again, NASAA can point FINRA to many examples of cases purposely pursued in court to avoid the procedures—although flawed—in place in the arbitration expungement context. This is a significant concern for NASAA and its members, and for all the good ideas put forth by FINRA in the Proposal, none of them address this issue. Only substantive changes to broker's behavioral rules will curtail the rapid erosion of information from CRD and IARD. In its current form neither Rule 2080 nor the Proposal would prevent this unfortunate reality. In NASAA's view, such a mechanism is required, and its absence highlights the problems with Rule 2080's procedural nature. To truly fix the expungement process, wholesale reform is necessary.

### The Path Forward

As noted in the Proposal, NASAA and FINRA have been working together to explore potential amendments to the expungement process. NASAA appreciates the time and effort FINRA staff have dedicated to this important issue. While this work is ongoing and many issues must still be resolved, in NASAA's view, a workable expungement framework that truly preserves expungement as an extraordinary remedy would be built around the following core principles:

- Substantive standards that properly limit the scope of expungement requests, including a clearer presentation of new standards that replace the flawed and misapplied prongs outlined in Rule 2080;
- Mandatory process, meaning all expungement requests must be made pursuant to the new process, which would be designed to close loopholes in and avoid unintended outcomes of the current process;
- Increased regulatory participation, allowing for both a regulatory determination regarding the merits of an expungement request and the legal process to protect the data;
- Earlier notices to state regulators of an expungement request to better facilitate regulator involvement where appropriate;

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<sup>22</sup> Further, other means are available today for brokers to address their concerns related to customer complaints. When customer complaints are disclosed on the Form U4, brokers have the ability to provide their own responses to rebut the allegations in the complaints.

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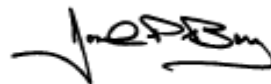
- Leverage the efficiencies of arbitration in fact finding, but limit the ability of arbitrators to “grant” expungement requests, instead only allowing factual, not legal, recommendations that are not considered awards;<sup>23</sup>
- Preserve the requirement that a court order the expungement of records prior to the removal of any information from the CRD.

NASAA has engaged FINRA with these core principles in mind, and pledges to work towards meaningful expungement reform.

### Conclusion

NASAA appreciates the opportunity to offer its comments in support of the Proposal, as it is a significant first step in meaningful expungement reform. The current expungement process is broken: a fact on which NASAA and FINRA agree. And as stated above, NASAA is prepared to provide and discuss with FINRA examples of expungement requests illustrating many of the problems unsolved by the changes in the Proposal. While NASAA looks forward to its continued dialog with FINRA on expungement, this dialog cannot continue indefinitely, while stop-gap fixes are applied to a fundamentally flawed expungement foundation. It is critical that a long-term solution to the expungement problem be reached, so as to stop the abuses that cannot be stopped by the Proposal. Should you have any questions regarding the comments in this letter, please do not hesitate to contact A. Valerie Mirko, ([vm@nasaa.org](mailto:vm@nasaa.org)), NASAA General Counsel, via email or by phone at 202-737-0900 or Melanie Senter Lubin ([mlubin@oag.state.md.us](mailto:mlubin@oag.state.md.us)), Maryland Securities Commissioner, Chair, NASAA’s CRD/IARD Steering Committee, via email or by phone at 410-576-6365.

Sincerely,



Joseph Borg  
Alabama Securities Director  
NASAA President

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<sup>23</sup> In the Proposal, FINRA specifically seeks comment on whether it should remove the concept of “granting expungement” in favor of “recommending expungement.” See the Proposal, *supra* note 2, at 17. In NASAA’s view, FINRA should make this change. As explained in prior comment letters, *supra* notes 4-5, the structure of Rule 2080 requires the confirmation of an arbitration award in a court of competent jurisdiction. This structure significantly limits a state regulator’s ability to present arguments opposing the merits of an expungement request during a confirmation proceeding in state court due to the deference courts are required to give arbitration awards under the Federal Arbitration Act. See Federal Arbitration Act, 9 U.S.C. § 10-11 (explaining the limited circumstances a court can vacate or modify an arbitration award).

In 31 years of service, I have seen the scale tilt from rogue brokers; to rogue clients and lawyers, to the abusive state in which we are now. Very few professions are as regulated as ours has become. In the meantime it has become easier and easier for rogue clients and lawyers to file suit and always gain a financial settlement on any kind of claim, meritless or not. Meritless and frivolous claim are being paid by the big firms because its easier and cheaper to settle, than the costs of going to court and defending their advisors!

In the meantime the advisor is left with a negative mark . His reputation threaten and trashed by a frivolous client and his lawyers , the regulators suffocating the innocent advisors and the big firms accepting their regulatory injustice because is cheaper and it helps them to tie up their advisors to the firm . The US system is based on Justice!!!! But where has it gone in this profession, when you are penalized even if you are innocent. Even if it's a meritless and frivolous case and is proven, you still have to pay thousands of dollars for an expungement for doing your job right ????? Where is the justice on that ? All the harm goes to the advisors no matter what; and they are left or force to fend for themselves.

It's like having a gun to your head and no matter what you say or do the trigger is going to be pulled, even if you are innocent!

I think it's time for our profession, professionals, firms and regulators(finra) to balance the scale again and stop the abuse that is growing to a monstrous scale and having innocent people who do their job well, fairly defended. Rouge clients and their layers need to become liable as well and should be put on a win, lose situation, penalized and fined. Not a win ,win which is where we are and making it easier for them. Anybody for any stupidity can file suit and they are assured by their layers that some financial reward will come out of this with zero downside or liability. It's become a great business for lawyers and their clients!!!!

In the meantime Finra keeps taking away the advisors rights and giving it to the core of the problem which is overregulating , giving more power to rogue clients and their lawyers as the firms are not taking a stance on this abuse.

Fair is fair and that is what justice is based on ! Finra should open their eyes and stop suffocating and overregulating advisors and make clients and their layers more liable . Finra needs to balance the scale. Penalize and make pay the liable party being the advisor or the client and his layers. This is where their efforts should be focused and stop the witch hunt with the advisors and the monetary bonanza gifts abuse given to the client. Making it easier and easier for them and ruining countless innocent carriers.

*Juan Braschi*

First Vice President  
Senior Financial Advisor

**LBDL Group**



*Merrill Lynch Global Wealth Management*  
*Millenium Park Plaza #15 Second Street, Suite 210*  
*Metro Office Park Guaynabo, PR 00968-1741*  
*T 787 294 3415 T 800 523 0663 F 787 294 3431*  
[www.fa.ml.com/lbdl\[fa.ml.com\]](http://www.fa.ml.com/lbdl[fa.ml.com])

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As an advisor who was unfairly saddled with a client's non-investment related complaint that was added to my record and never removed even though settled (it was settled as advised by my B/D at the time to avoid any legal fees – even though the legal counsel and they agreed the complaint was bogus)

I am still stinging from the fact that 10 years later, this is still on my record and that there is now consideration to permanently prevent the fair removal of meritless claims that are over a year old.

Please note my complaint that making it even harder for those who may be falsely accused without any recourse is a travesty and that FINRA has an obligation to protect both the consumer and the advisor equally....

Scott

Scott Brookes, AIF®

Director of Retirement Plan Services

720 S Colorado Blvd - Suite 600 South

Denver, CO 80246

I have held securities registrations since 1984.

I was the target of a former client accusation that I failed to disclose all pertinent information regarding an investment option she was considering. The claim was dismissed without action.

Yet, I have a record of that claim of "unscrupulous" behavior in BrokerCheck forever. No, that is wrong. There should be a method where upon investigation of a claim and the claim found to be without merit that the broker, such as I, won't have a black eye for the remainder of their careers. Careers that could be shortened because of the heightened promotion of using BrokerCheck, which is fine, IF BrokerCheck only contained claims found to be valid and action taken against the broker. Weed out the crooks. Of course. But I'll never know how many referred potential clients never hired me because they were told to look me up on BrokerCheck and found the claim. People don't understand that the claim was dismissed, what that meant.

I had been told that I could not expunge my record on BrokerCheck. Recently I learned I could. Now I'm learning that FINRA wants to take that away. NO. I want to clear my record because I have conducted my business ethically and by the book.

Thank you,  
Donna Burrill

The Constitution of the United States allows for innocent until proven guilty. However the reporting system under FINRA is guilty until proven innocent. Until you completely overhaul the entire system you must continue to allow expungement proceedings to exist.



February 5, 2018

**VIA EMAIL (pubcom@finra.org)**

Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

**Re: FINRA Regulatory Notice 17-42  
Proposed Amendments to the Codes of Arbitration Relating to  
Requests to Expunge Customer Dispute Information**

Dear Ms. Asquith:

The Securities Industry and Financial Markets Association (“SIFMA”)<sup>1</sup> appreciates the opportunity to provide this letter in response to the Financial Industry Regulatory Authority’s (“FINRA”) Regulatory Notice 17-42, proposing amendments to the Codes of Arbitration, including FINRA Rules 12805 and 13805, relating to requests to expunge customer dispute information (the “Notice” or the “Proposal”).

## **I. Executive Summary**

SIFMA continues to support the essential goals of the Central Registration Depository (“CRD”) and FINRA BrokerCheck public disclosure system, including that investors should have access to ***complete and accurate*** information about firms and individual registered representatives.<sup>2</sup> Given the general public’s increased use of and reliance upon BrokerCheck, the accuracy of reported

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<sup>1</sup> SIFMA is the voice of the U.S. securities industry. We represent the broker-dealers, banks and asset managers whose nearly 1 million employees provide access to the capital markets, raising over \$2.5 trillion for businesses and municipalities in the U.S., serving clients with over \$18.5 trillion in assets and managing more than \$67 trillion in assets for individual and institutional clients including mutual funds and retirement plans. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit <http://www.sifma.org>.

<sup>2</sup> See NASD Notice to Members 99-54, p. 2 (July 1999) stating that “NASD Regulation recognizes that the information on the CRD system has important investor protection implications, provided it is complete and accurate.” See also SIFMA April 2012 comment letter in response to Regulatory Notice 12-10 (February 2012) stating that “the information maintained in BrokerCheck must be accurate, clear, concise and relevant to the investor, and must be balanced against member firms’ and their employees’ legitimate privacy interests, and expectations of fairness and balance.” See also Notice to Arbitrators and Parties on Expanded Expungement Guidance (Updated September 2017) requiring that disclosures be “accurate and meaningful.”



information should be of paramount concern. No one benefits when a regulatory entity publishes, and thereby attaches its imprimatur to, potentially inaccurate or misleading information.

SIFMA believes that existing rules and FINRA's expanded expungement guidance provide sufficient safeguards for the expungement process. The proposed rules would establish inconsistent adjudicatory standards and procedures applicable only to expungement applications, and would increase the cost and burden on registered representatives seeking to protect their reputations and livelihoods from the harm caused by the disclosure of false or misleading customer complaint information.

The Notice asserts that by increasing the obstacles to expungement, including the costs and inconvenience to registered representatives, expungement filings would be fewer and more meritorious. However, the rule proposals and accompanying conclusions have been presented without any accompanying evidence that such changes are in fact necessary. Namely, the Proposal does not provide any cost-benefit analyses or empirical evidence that expungements are too numerous, are being improperly granted, or are being pursued in ways that are inconsistent with FINRA rules and regulatory guidance.<sup>3</sup> Anecdotal concerns from "critics of expungement" should not be the basis for wholesale changes to an essential remedy afforded to over 630,000 registered representatives to prevent the unfair dissemination of false or misleading information.

## **II. FINRA's Disclosure Regime Is Allegation-Driven And Expungement Is An Essential Remedy To Prevent The Dissemination Of False Or Misleading Information**

The CRD/BrokerCheck regulatory reporting regime presently requires the public disclosure of more information by registered persons than any other regulated profession. The broad reporting requirements related to customer complaints are "allegation-driven," rather than outcome-based, and require disclosure based on the "four corners" of a written customer complaint or pleading, even in the face of clear evidence to the contrary. Moreover, many complaints involve product-related allegations that in some cases unfairly result in disclosures against individual registered representatives.

FINRA's 2009 amendments to the Uniform Forms (Forms U4 and U5), especially those requiring disclosure of customer complaints against "unnamed" persons (See Reg. Notice 09-23), and the BrokerCheck Disclosure Rule (FINRA Rule 8312) have resulted in an increase in reportable disclosures, which can remain on a registered persons' public record for as long as they are in the industry and for several years thereafter.

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<sup>3</sup> See Framework Regarding FINRA's Approach to Economic Impact Assessments for Proposed Rulemaking (Sept. 2013) (detailing FINRA's cost-benefit analysis obligations), available at [http://www.finra.org/sites/default/files/Economic%20Impact%20Assessment\\_0\\_0.pdf](http://www.finra.org/sites/default/files/Economic%20Impact%20Assessment_0_0.pdf)



The Notice states that “[i]t has been FINRA’s long-held position that expungement of customer dispute information is an extraordinary measure, but it may be appropriate in certain circumstances.” However, expungement has long been recognized as a core part of an arbitrator’s power to award equitable relief. See NASD NTM 99-54, p. 3. Expungement serves one of the “three competing interests” of the CRD/BrokerCheck system, including, critically, the interests of over 630,000 registered representatives:

(1) the interests of NASD, the states, and other regulators in retaining broad access to customer dispute information to fulfill their regulatory responsibilities and investor protection obligations; **(2) the interests of the brokerage community and others in a fair process that recognizes their stake in protecting their reputations and permits expungement from the CRD system when appropriate**; and (3) the interests of investors in having access to accurate and meaningful information about brokers with whom they conduct, or may conduct, business.

NASD NTM 04-16, p. 2 (footnote omitted, emphasis added).

Based on these guiding principles, expungement is the *only* remedy available to registered representatives to remove false, inaccurate or erroneous information from their public disclosures. Contrary to expungement being an “extraordinary”<sup>4</sup> measure, expungement is an *essential* remedy to ensure the appropriate balance between the public disclosure of meritorious versus spurious complaints within the “three competing interests” of the CRD/BrokerCheck reporting regime.

### **III. Current Rules And Expanded Expungement Guidance Provide Substantial Safeguards For The Expungement Process**

Current FINRA rules ensure that expungement decisions are made only after a fact-based inquiry by competently trained arbitrators. In order for an expungement to be granted, Rule 2080(b)(1) requires a finding that (i) the claim or allegation is factually impossible or clearly erroneous; (ii) the registered person was not involved in the alleged sales practice violation, forgery, theft, misappropriation or conversion of funds, or (iii) the claim, allegation, or information is false. If the expungement award is based on any findings other than these three grounds, FINRA maintains the right to be named as a party and challenge any expungement award in a state court confirmation proceeding. (Rule 2080(b)(2)). Rules 12805 and 13805 require a recorded hearing along with a written explanation detailing the basis for the expungement relief. Rule 2081 prohibits conditioning settlements on non-opposition to requests for expungement relief. Additionally, the court confirmation requirements under FINRA Rule 2080 and relevant guidance (including those

<sup>4</sup> The “extraordinary remedy” language should not become part of the rule because the term is overly broad, vague and not susceptible to clear and consistent application as a legal term.



addressing waiver requests and preserving the rights of FINRA and state regulators to be made aware of and, if appropriate, challenge expungement awards) provide additional safeguards against inappropriate grants or potential abuses of the expungement process.

In 2013, FINRA began issuing “expanded” guidance to be followed by arbitrators when considering expungement requests. This guidance, updated as recently as September 2017, provides additional safeguards that increase the opportunity for customer participation, including requirements that: (i) allow a customer and his/her counsel to appear and testify at the expungement hearing; (ii) allow counsel for the customer or a pro se customer to introduce documents and evidence at the expungement hearing; (iii) allow counsel for the customer or a pro se customer to cross-examine the broker and other witnesses called by the party seeking expungement; and (iv) allow counsel for the customer or a pro se customer to present opening and closing arguments if the panel allows any party to present such arguments. Other expungement guidance requires arbitrators to review BrokerCheck Reports and prohibits the re-filing of expungement applications after a prior petition has already been made and adjudicated.<sup>5</sup>

Accordingly, FINRA already has in place a robust set of rules and expanded guidance to safeguard the expungement process, and there does not appear to be any empirical or other justification for many of the additional onerous regulations contained in the Proposal.

#### **IV. Comments to FINRA’s Proposed Amendments**

##### **A. Expungement Awards Should Not Require Unanimous Decisions By Mandatory Three-Member Arbitration Panels**

Since the advent of FINRA’s three-member panels, arbitration awards have been issued based on the determination of a majority of arbitrators. The Notice proposes a different and more stringent threshold for expungement decisions by requiring a unanimous decision in favor of expungement. Adoption of the proposed changes would result in a panel potentially applying a majority rules standard to the liability determination, but a unanimity standard to the expungement determination in the same case. The Proposal purports to assign greater value and scrutiny to expungements compared to other types of cases, but does not offer any explanation or empirical evidence as to why expungements warrant a higher threshold than a multi-million dollar customer or industry case. If implemented, this rule would impinge upon the fundamental fairness of the expungement process in providing an effective balance to the allegation-based complaint reporting regime and will have a significant impact on registered representatives’ ability to protect their livelihoods and reputations.

<sup>5</sup> See Notice to Arbitrators and Parties on Expanded Expungement Guidance (Updated Sept. 2017) available at: <https://www.finra.org/arbitration-and-mediation/notice-arbitrators-and-parties-expanded-expungement-guidance>



The proposal to increase arbitrator qualifications and training through a separate Expungement Arbitrator Roster (the “Roster”) consisting of practicing attorneys who have received advanced expungement training and have at least five years of experience in either litigation, securities regulation, administrative law, service as a securities regulator or service as a judge is commendable. More highly qualified and trained expungement arbitrators should lead to a more efficient and fair process, instill greater confidence in arbitrators by FINRA, customers, firms and registered persons and reduce the perceived need for unanimous decisions.

Current FINRA rules permit the parties, upon consent, to select a single arbitrator. However, as noted above, the Notice proposes a mandatory three-person panel that FINRA would randomly assign from the Roster for expungement cases. The Notice does not contain any discussion or evidence that a single arbitrator is unable to reach a just decision or that a three-person panel is more efficient or may reach a more accurate decision than a single highly qualified and trained arbitrator. If FINRA, customers, firms and registered persons can have confidence in a highly qualified and experienced single arbitrator through the Roster, there appears no compelling need to use three instead. This proposal will increase the financial burden on registered representatives seeking expungement.

SIFMA disagrees with the proposed process of FINRA randomly assigning arbitrators instead of permitting parties to rank and/or strike them, as is the current practice. Parties’ selection of neutral arbitrators is a hallmark of the arbitration process. FINRA’s random assignment of arbitrators removes the parties’ involvement and input, as well as the consensual nature of arbitration. Moreover, if implemented, the rule would treat expungement differently than any other arbitration proceeding, for which the parties could still select a single arbitrator or three-person panel. Accordingly, SIFMA supports continuing the arbitrator ranking system from the proposed Roster for expungement-only cases. However, to preserve arbitrator neutrality and foster greater transparency in arbitration education and assignment, SIFMA proposes that FINRA make the following publicly available relating to Roster arbitrators: (1) all training materials utilized; 2) all FINRA communications with Roster arbitrators regarding expungement; and (3) all documents related to the addition, removal or exclusion of any Roster arbitrators.

Additionally, current FINRA rules allow expungements to proceed in those cases resolved other than by award (*i.e.*, settlement) using the same arbitrators empaneled in the underlying case. The Proposal would instead require the filing of a new expungement matter for cases resolved other than by award, using a panel randomly assigned from the Roster. This proposal appears inefficient because often times the sitting panel involved in a case since inception is in the best position to know and assess a case’s facts and circumstances. Permitting a sitting panel to determine expungement in these cases would be most appropriate because it would provide for greater efficiency, lower costs and a quicker resolution. To address FINRA’s concern for greater training and increased qualifications for those arbitrators determining expungement, while also providing



for greater efficiency for a sitting panel to determine expungement, SIFMA proposes that at least one arbitrator on a three-person panel be selected from the Roster at each case's inception (or that all Chairs be Roster certified).

**B. Panels Should Not Be Required To Find That The Information To Be Expunged Has “No Investor Protection Or Regulatory Value”**

FINRA already imposes high standards in order for arbitrators to recommend expungement. FINRA Rule 2080(b)(1) requires a finding either that: (i) the claim or allegation is factually impossible or clearly erroneous; (ii) the registered person was not involved in the alleged sales practice violation, forgery, theft, misappropriation or conversion of funds, or (iii) the claim, allegation, or information is false. If the expungement award is based on any findings other than the above, FINRA maintains the right to be named as a party and challenge any expungement award in a state court confirmation proceeding. See Rule 2080(b)(2).

By proposing additional elements for expungement requiring interpretation and imposition of regulatory policy, the Notice suggests the current high standards of falsity, impossibility or non-involvement are somehow insufficient. However, the Notice appears to provide no evidence or argument as to why these high standards are insufficient or why they need to be bolstered.

In addition to the high standards imposed by FINRA Rule 2080(b)(1), the Notice proposes that a Panel must also find (and state in the Award) the customer dispute information has *no investor protection or regulatory value*. However, customer dispute information that satisfies one of the three grounds under Rule 2080(b)(1) simply cannot otherwise have any investor protection or regulatory value. Requiring a specific finding that the information has no investor protection or regulatory value would be redundant given the current high standards imposed under the rule. The imposition of these additional standards would appear to be largely symbolic and deterrent in nature, yet lack practical application.

Moreover, this proposed rule is already part of FINRA's expanded expungement guidance, which provides that “[c]ustomer dispute information should be expunged only when it has no meaningful investor protection or regulatory value.” Notice to Arbitrators and Parties on Expanded Expungement Guidance (Updated Sept. 2017). Such language has also been incorporated into FINRA's expungement script. However, these proposed rule changes reflect an overarching regulatory policy and should not be included as a factual finding required in an award. This proposed language may have the effect of discouraging otherwise meritorious expungement claims and stifling the process by increasing the burden on the registered representative with no attendant practical benefit.

The current expungement standards under Rule 2080(b)(1) require arbitrators to apply the specific facts of a case to determine whether expungement is warranted under the rule. Arbitrators are



further required to provide written factual findings in support of any expungement award. If implemented, this proposal would transform the traditional role of arbitrators as fact-finders and further require them to make a policy determination in each case. FINRA sets regulatory policy; it is not an arbitrator's role to interpret and implement regulatory policy on a case-by-case basis.

**C. The Proposed One-Year Limitations Period For Filing Expungement Should Be Modified Or Eliminated**

FINRA currently imposes no time limitation specific to expungement claims. To satisfy the laudable goal of preserving the integrity of customer complaint reporting by providing complete and accurate information to investors, false complaints should be expunged, no matter how old. The Notice proposes a one-year limitation commencing on the initial reportability of a customer complaint by the firm or one year after the conclusion of an arbitration in which the broker was not a named party. However, the Notice cites no basis for a one-year limitation for expungement claims and does not appear to provide any distinction as to why expungement limitations periods should be treated differently from all other limitations periods. Since FINRA Rules 12504 and 13504, which already provide a six-year eligibility period to file claims, ostensibly apply to expungements, there is no basis for a separate and significantly shorter time limitation for expungement-only matters.

There are also practical and procedural limitations of this proposed one-year limitations period. The proposed one-year limitation is insufficient for firms to properly investigate customer complaints and respond to customers. This would necessarily lead to the filing of expungements for pending or recently denied complaints that would then be stayed under recent expungement guidance that precludes concurrent actions. This would lead to registered representatives and firms devoting time, resources and capital to an inefficient regime created by an artificially short limitations period. In order to address this, SIFMA proposes that any such time limitation run from the close-out of the customer complaint on CRD (or the close of the arbitration), and not the initial reporting of the complaint on CRD.

Additionally, the Proposal does not address proposed time limitations for filing expungement actions for customer complaints that are disclosed before the implementation of the proposed rules. SIFMA requests further guidance on the extended time period that will be afforded registered representatives who have eligible claims for expungement that would become ineligible if the rule proposals were implemented. In any event, SIFMA proposes a one-year time period for registered representatives to file for expungement of previously disclosed customer complaints that were eligible for expungement prior to any rule change and requests that FINRA provide sufficient flexibility to address subsequent rule changes that may implicate limitations period by having retroactive effect.<sup>6</sup>

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<sup>6</sup> In 2010, FINRA amended Rule 8312, requiring the reportability of previously archived historical complaints. Sufficient safeguards and flexibility should be built into the proposed time limitations rules to address subsequent rule



**D. Other Important Proposed Changes Require Additional Consideration By FINRA**

**1. The Requirement For an In-Person or Video-Conference Expungement Hearing is Unnecessary and Inefficient**

Current FINRA Rules provide that an expungement hearing must be recorded, but that it may be held telephonically. The panel retains discretion to order an in-person hearing and exercises that discretion upon occasion when circumstances warrant. The Proposal would eliminate telephonic expungement hearings and would instead mandate in-person or video-conference expungements. However, the Proposal permits customers to testify by telephone. The Proposal offers no evidence concerning the efficacy of telephonic hearings or why expungements should require in-person hearings, while other cases, such as customer cases, could still be held telephonically. This Proposal would greatly increase the cost of expungement through attendant travel costs and loss of productivity. Additionally, permitting customers, but not registered representatives, to provide telephonic testimony reflects disparate witness standards. There appears no basis for requiring in-person testimony for a panel to better assess a registered representative's credibility, yet not requiring in-person testimony for a panel to better assess a complaining customer's credibility.

**2. The Proposed Increase in Filing Fees and Additional Member Fees are Burdensome and Punitive**

In pending arbitrations where a registered representative is named as a party, the Proposal would require the individual to pay an additional expungement filing fee of at least \$1425 and would assess an additional member surcharge and processing fee against the firm, in addition to the fees charged in the underlying arbitration. These additional fees are burdensome, punitive and will likely discourage registered representatives and firms from pursuing otherwise meritorious expungement claims. This could have an unfortunate impact of creating a tiered system where only registered representatives and firms that can absorb these additional costs will be able to pursue expungement, regardless of merit. The factual basis of each customer complaint should be the determining factor in expungement and not prohibitive costs that may deter otherwise meritorious expungement filings.

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changes that have retroactive effect, such as starting the limitations period from the time of the rule change having retroactive effect, as opposed to the initial reportability of the customer complaint.



### 3. **New Expungement Filings For All Cases Closed Other Than by Award are Unwarranted**

Currently, registered representatives may file for expungement in a customer case, even when that case is closed other than by award (*i.e.*, settlement). The Proposal would require registered representatives to file a new expungement matter, and would require registered representatives and member firms (that must now be named as a party), to pay the applicable filing, processing and member fees. As previously noted, the sitting panel is in the best position to determine expungement based on its involvement in the customer case. Such proposal would increase the costs, burden and time for resolution and may serve as a punitive measure for both the registered representative and the member firm, creating the unintended consequence of a tiered system described above.

Moreover, the proposed requirement to file for expungement 60 days prior to the first scheduled hearing date appears untenable and impractical. The proposal would require the registered representative and firm to pay separate expungement fees, even though a large portion of cases settle within 60 days of the hearing. Such fee structure is punitive in nature because it would essentially require triple payment by member firms (underlying customer arbitration, expungement during underlying arbitration, expungement in separate expungement matter) and double payment by registered representatives (expungement in underlying arbitration, expungement in separate matter). In addition to exponentially increasing the cost of expungement, this could also have the indirect effect of increasing the cost of settlement, potentially discouraging settlement in smaller cases due to the increased costs associated with expungement.

### 4. **New Procedures for Simplified Arbitrations (\$50,000 or less) Appear Inefficient and Not Simplified**

The current process for simplified arbitrations is for a single arbitrator to rule on liability first, then hold a hearing solely for the purpose of determining expungement. The Proposal would require the registered representative to file a *new* expungement claim, with FINRA randomly assigning three arbitrators from the Roster only *after* resolution of underlying arbitration on papers. FINRA would then assess additional fees against the registered representative and member firm. This proposal is inconsistent with the purposes of simplified arbitrations to reduce costs and resolve cases expeditiously. A simplified arbitration should be *simplified* for all parties involved, not just the customer. This change would make expungement in simplified arbitrations cost prohibitive and discourage meritorious expungement claims.

SIFMA proposes modification of the rules for simplified arbitrations by providing for the selection of a single arbitrator from the Roster to decide both liability and expungement. The arbitrator would issue a bifurcated order, first deciding the issue of liability on papers, then hold a hearing



solely to determine expungement. This would promote greater cost efficiency, a quicker resolution and greater customer participation.

SIFMA reiterates its general support for FINRA's desire to continuously improve the expungement process by providing complete and accurate customer complaint disclosure information on individual registered representatives and firms to the investing public. However, sufficient safeguards are already in place in the form of extensive rules and enhanced expungement guidance that are already onerous on registered representatives. The proposed rules establish inconsistent adjudicatory standards and procedures applicable only to expungement applications and would unfairly increase the cost and burden on registered representatives seeking to protect their reputations and livelihoods from the harm caused by the disclosure of false or misleading customer complaint information. These changes could potentially tip the balance between the allegation-based reporting regime and the need to provide only complete and accurate disclosure information. Many of the rule proposals will have a significant deterrent effect and stifle the expungement of otherwise meritorious expungement claims. SIFMA thanks FINRA staff for its willingness to consider the issues raised in this letter. We look forward to our next opportunity to comment on issues related to FINRA's expungement process.

If you have any questions or require further information, please contact me at 202-962-7300, [kcarroll@sifma.org](mailto:kcarroll@sifma.org), or our counsel, Mark D. Knoll and David Hantman, Bressler, Amery & Ross, P.C., at 212-510-6901 / 212-510-6912, [mknoll@bressler.com](mailto:mknoll@bressler.com) / [dhantman@bressler.com](mailto:dhantman@bressler.com).

Very truly yours,

A handwritten signature in dark ink, reading "Kevin M. Carroll". The signature is fluid and cursive, with a long horizontal stroke at the end.

---

Kevin Carroll  
Managing Director and Associate General Counsel

cc: Mark D. Knoll, Bressler, Amery & Ross (by electronic mail)  
David I. Hantman, Bressler, Amery (by electronic mail)

## MADDOX HARGETT & CARUSO, P.C.

Representing Investors

Mark E. Maddox<sup>1</sup>  
Thomas A. Hargett<sup>2</sup>  
Steven B. Caruso<sup>4</sup>  
Thomas K. Caldwell<sup>3</sup>

80 Broad Street  
Fifth Floor  
New York, NY 10004  
212.837.7908  
212.837.7998 fax

[www.investorprotection.com](http://www.investorprotection.com)

Indianapolis  
10150 Lantern Road  
Suite 175  
Fishers, IN 46037  
317.598.2040  
317.598.2050 fax

### VIA EMAIL SUBMISSION TO PUBCOM@FINRA.ORG

January 30, 2018

Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

Re: FINRA Regulatory Notice 17-42

Dear Ms. Asquith:

The purpose of this letter is to provide the Financial Industry Regulatory Authority, Inc. ("FINRA") with comments on the above referenced Regulatory Notice which was issued by FINRA on December 6, 2017.

I am an attorney whose practice is exclusively devoted to the representation of individual and institutional investors in their disputes with the securities industry. Moreover, I am the current Chairman of FINRA's National Arbitration and Mediation Committee ("NAMC") and a public member of the NAMC; the former Chairman of FINRA's Discovery Task Force Committee ("DTFC"); a former member of the Securities Investor Protection Corporation ("SIPC") Modernization Task Force; and a former President and current Director Emeritus of the Public Investors Arbitration Bar Association ("PIABA").

It is my understanding that the Regulatory Notice requests comment on proposed amendments to the FINRA Code of Arbitration Procedure ("FINRA Code") which are intended to help address the issues that are associated with requests to expunge customer dispute information from both the Central Registration Depository ("CRD") system and the FINRA BrokerCheck ("BrokerCheck") system.<sup>1</sup>

<sup>1/</sup> As a preliminary matter, it must be noted that the recently adopted process of issuing "Regulatory Notices" to seek comment on nearly every proposed rule change not only unduly delays consideration of the same, but of equal, if not greater importance, it provides an unfair and unnecessary advantage to industry participants who are the most likely constituency to be aware of and to comment on issued Regulatory Notices at this stage of their consideration.

Marcia E. Asquith  
January 30, 2018  
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The critical issue of expungements continues to be in desperate need of a viable and effective solution. Unfortunately, notwithstanding the fact that expungements have been widely recognized as an “extraordinary” measure with significant “regulatory” and “investor protection” implications, the historical monthly expungement data that I have personally maintained since January 1, 2013 indicates otherwise:

- Between January 1, 2013 and December 31, 2017, expungements were granted in 1,145 out of the 1,974 arbitration proceedings in which an expungement was requested which equates to an expungement approval rate of 73.20%; and
- With respect to post-settlement arbitration awards (awards which followed the settlement of the underlying customer arbitration proceeding), between January 1, 2013 and December 31, 2017, expungements were granted in 981 out of the 1,117 settled arbitration proceedings in which an expungement was requested which equates to an expungement approval rate of 87.83%.

The troubling nature of this latter statistic is further evidenced by a review of the FINRA Rule 2080 predicates which served as the basis for the expungements in these post-settlement arbitration proceedings between January 1, 2013 and December 31, 2017.

In fact, 44.48% of the awards associated with post-settlement arbitration proceedings in which expungements were granted were predicated on a finding, under FINRA Rule 2080(3), that “the claim, allegation or information [was] false.”

This statistic – 44.48% of the awards associated with post-settlement arbitration proceedings in which expungements were granted having been predicated on a finding, under FINRA Rule 2080(3), that “the claim, allegation or information [was] false,” is belied by the fact that a substantial majority of settlements are effectuated by the payment of monetary compensation.

With respect to the questions presented for specific comment in the Regulatory Notice, I would offer the following comments and observations.

- Should the expungement rule retain “grant” or change to “recommend” or some other description to more accurately reflect the panel’s authority in the expungement process?

In view of the fact that arbitrators do not have the power to “grant” an expungement request, it is clear that the language should be changed to “recommend” as this

Marcia E. Asquith  
January 30, 2018  
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would insure that it is both 100% clear and accurate.

- What are the costs and benefits of requiring the unanimous consent of a three-person panel to grant all requests for expungement of customer dispute information?

In view of the fact that expungements have been widely recognized as an “extraordinary” measure with significant “regulatory” and “investor protection” implications, it is clear that requiring the unanimous consent of a three-person panel to recommend the expungement of customer dispute information must be adopted. Moreover, given the historical fact that more than 99% of prior expungement awards have been decided on a unanimous basis, this proposed rule amendment would not have any material cost impact on the expungement process and would simply codify existing reality.

- Is the one-year limitation on being able to request expungement of customer dispute information appropriate?

It is my opinion that a one-year limitation on being able to request expungement of customer dispute information is appropriate in view of the fact that this time limitation would encourage more customers to potentially participate in the expungement hearing and to provide information and documentation that would be material to the consideration of whether or not a recommendation of expungement would be appropriate.

- Should an associated person who is requesting expungement be required to appear in person or by videoconference, rather than by phone, at the expungement hearing?

It is my opinion that an associated person who is requesting expungement should be required to appear in person or by videoconference so that the arbitrators can assess the associated person’s demeanor and credibility.

- Should the arbitrators on the Expungement Arbitrator Roster have specific qualifications and, if so, are the proposed additional qualifications appropriate or should FINRA consider other qualifications?

It is my opinion that it is necessary for arbitrators to have specific qualifications to be included on the Expungement Arbitrator Roster so that the integrity of the CRD and BrokerCheck systems can be maintained. Moreover, the proposed additional qualifications appear to be fair and reasonable.

Marcia E. Asquith  
January 30, 2018  
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· The proposal would clarify for arbitrators that the standard for granting the permanent removal of customer dispute information from CRD is a finding that at least one of the Rule 2080(b)(1) factors applies and that the customer dispute information has “no investor protection or regulatory value.” Are there specific factors that arbitrators should consider when making a finding that the customer dispute information has “no investor protection or regulatory value”?

The predicate issue in connection with this question is whether it is appropriate for FINRA to download the responsibility for the determination of “investor protection” and/or “regulatory value” to arbitrators? Based on the available historical data for expungements, is my opinion that the answer to this question is clearly no. Arbitrators in the FINRA forum have signed on for the determination of disputes – that is what they are trained to do and that is what they should be solely asked to do. In order for arbitrators to now be asked to determine “investor protection” and/or “regulatory value” considerations would require not only a tremendous amount of specific training, but there would also need to be ongoing oversight of their determinations so as to insure that this critical function achieves its goals.

In the event that you should have any questions with respect to the preceding, please do not hesitate to contact me.

Very truly yours,

Maddox Hargett & Caruso, P.C.

*s/ Steven B. Caruso*

Steven B. Caruso

Steven B. Caruso, Esq.  
Maddox Hargett & Caruso, P.C.  
80 Broad Street, 5th Floor  
New York, N.Y. 10004  
www.investorprotection.com  
(212) 837-7908

## FINRA DISPUTE RESOLUTION ARBITRATION AWARD REVIEW - 2013

| MONTH ENDED | POST-SETTLEMENT |        | CLAIMANT AWARD |        | RESPONDENT AWARD |        | BD/AP v. CUSTOMER AWARD |        | RULE 2080(b)(1) PREDICATE |        |        |
|-------------|-----------------|--------|----------------|--------|------------------|--------|-------------------------|--------|---------------------------|--------|--------|
|             | GRANTED         | DENIED | GRANTED        | DENIED | GRANTED          | DENIED | GRANTED                 | DENIED | A                         | B      | C      |
| Jan. 2013   | 20              | 0      | 1              | 1      | 7                | 2      | 2                       | 0      | 12                        | 12     | 15     |
| Feb. 2013   | 20              | 2      | 1              | 5      | 7                | 1      | 2                       | 0      | 9                         | 8      | 18     |
| Mar. 2013   | 31              | 1      | 2              | 0      | 5                | 2      | 6                       | 0      | 22                        | 14     | 24     |
| Apr. 2013   | 34              | 4      | 1              | 1      | 7                | 4      | 3                       | 0      | 23                        | 14     | 27     |
| May. 2013   | 39              | 4      | 2              | 4      | 8                | 3      | 2                       | 0      | 26                        | 21     | 28     |
| Jun. 2013   | 25              | 2      | 2              | 9      | 11               | 3      | 4                       | 0      | 20                        | 17     | 20     |
| Jul. 2013   | 35              | 3      | 1              | 2      | 6                | 3      | 1                       | 0      | 22                        | 14     | 30     |
| Aug. 2013   | 24              | 1      | 0              | 4      | 9                | 3      | 2                       | 0      | 22                        | 14     | 30     |
| Sept. 2013  | 20              | 1      | 1              | 3      | 3                | 2      | 3                       | 0      | 14                        | 9      | 14     |
| Oct. 2013   | 26              | 3      | 1              | 3      | 11               | 1      | 2                       | 1      | 22                        | 10     | 24     |
| Nov. 2013   | 26              | 3      | 1              | 4      | 11               | 2      | 2                       | 1      | 22                        | 10     | 24     |
| Dec. 2013   | 23              | 6      | 0              | 6      | 3                | 4      | 2                       | 0      | 12                        | 12     | 13     |
|             | 323             | 30     | 13             | 42     | 88               | 30     | 31                      | 2      | 226                       | 155    | 267    |
|             | 91.50%          |        | 23.64%         |        | 74.58%           |        | 93.94%                  |        | 49.67%                    | 34.07% | 58.68% |

TOTAL EXPUNGEMENTS GRANTED IN CALENDAR YEAR 2013: 455 OUT OF 559 = 81.40%

Steven B. Caruso, Esq.  
Maddox Hargett & Caruso, P.C.  
80 Broad Street, 5th Floor  
New York, N.Y. 10004  
www.investorprotection.com  
(212) 837-7908

## FINRA DISPUTE RESOLUTION ARBITRATION AWARD REVIEW - 2014

| MONTH ENDED | POST-SETTLEMENT |        | CLAIMANT AWARD |        | RESPONDENT AWARD |        | BD/AP v. CUSTOMER AWARD |        | RULE 2080(b)(1) PREDICATE |        |        |
|-------------|-----------------|--------|----------------|--------|------------------|--------|-------------------------|--------|---------------------------|--------|--------|
|             | GRANTED         | DENIED | GRANTED        | DENIED | GRANTED          | DENIED | GRANTED                 | DENIED | A                         | B      | C      |
| Jan. 2014   | 28              | 3      | 0              | 4      | 4                | 1      | 1                       | 0      | 13                        | 10     | 23     |
| Feb. 2014   | 13              | 3      | 0              | 1      | 6                | 2      | 1                       | 0      | 10                        | 7      | 11     |
| Mar. 2014   | 18              | 1      | 1              | 7      | 5                | 5      | 4                       | 0      | 10                        | 13     | 15     |
| Apr. 2014   | 19              | 4      | 0              | 3      | 6                | 0      | 1                       | 0      | 8                         | 9      | 17     |
| May. 2014   | 17              | 3      | 0              | 5      | 4                | 3      | 5                       | 0      | 8                         | 10     | 18     |
| Jun. 2014   | 24              | 2      | 1              | 5      | 8                | 4      | 3                       | 1      | 17                        | 12     | 26     |
| Jul. 2014   | 24              | 4      | 0              | 4      | 1                | 3      | 2                       | 2      | 10                        | 10     | 17     |
| Aug. 2014   | 15              | 3      | 1              | 8      | 2                | 3      | 2                       | 1      | 11                        | 9      | 9      |
| Sept. 2014  | 13              | 0      | 0              | 0      | 4                | 2      | 4                       | 0      | 10                        | 8      | 15     |
| Oct. 2014   | 25              | 6      | 1              | 2      | 7                | 2      | 6                       | 1      | 15                        | 14     | 29     |
| Nov. 2014   | 15              | 0      | 0              | 4      | 1                | 3      | 2                       | 0      | 6                         | 4      | 12     |
| Dec. 2014   | 20              | 2      | 0              | 5      | 7                | 5      | 4                       | 0      | 15                        | 11     | 18     |
|             | 231             | 31     | 4              | 48     | 55               | 33     | 35                      | 5      | 133                       | 117    | 210    |
|             | 88.17%          |        | 7.69%          |        | 62.50%           |        | 87.50%                  |        | 28.91%                    | 25.43% | 45.65% |

TOTAL EXPUNGEMENTS GRANTED IN CALENDAR YEAR 2014: 325 OUT OF 442 = 73.53%

Steven B. Caruso, Esq.  
Maddox Hargett & Caruso, P.C.  
80 Broad Street, 5th Floor  
New York, N.Y. 10004  
www.investorprotection.com  
(212) 837-7908

## FINRA DISPUTE RESOLUTION ARBITRATION AWARD REVIEW - 2015

| MONTH ENDED | POST-SETTLEMENT |        | CLAIMANT AWARD |        | RESPONDENT AWARD |        | BD/AP v. CUSTOMER AWARD |        | RULE 2080(b)(1) PREDICATE |        |        |
|-------------|-----------------|--------|----------------|--------|------------------|--------|-------------------------|--------|---------------------------|--------|--------|
|             | GRANTED         | DENIED | GRANTED        | DENIED | GRANTED          | DENIED | GRANTED                 | DENIED | A                         | B      | C      |
| Jan. 2015   | 7               | 1      | 1              | 2      | 6                | 1      | 0                       | 0      | 5                         | 5      | 9      |
| Feb. 2015   | 14              | 3      | 0              | 2      | 6                | 2      | 2                       | 0      | 7                         | 9      | 13     |
| Mar. 2015   | 20              | 2      | 0              | 5      | 4                | 5      | 5                       | 1      | 11                        | 10     | 19     |
| Apr. 2015   | 15              | 2      | 0              | 6      | 2                | 5      | 5                       | 0      | 11                        | 6      | 14     |
| May. 2015   | 14              | 4      | 0              | 9      | 7                | 3      | 4                       | 0      | 12                        | 8      | 19     |
| Jun. 2015   | 19              | 2      | 0              | 7      | 2                | 2      | 1                       | 0      | 8                         | 6      | 16     |
| Jul. 2015   | 9               | 7      | 3              | 8      | 3                | 0      | 1                       | 0      | 6                         | 6      | 12     |
| Aug. 2015   | 16              | 2      | 0              | 4      | 4                | 2      | 0                       | 1      | 13                        | 8      | 10     |
| Sept. 2015  | 15              | 2      | 0              | 2      | 4                | 3      | 1                       | 0      | 7                         | 5      | 15     |
| Oct. 2015   | 17              | 1      | 2              | 7      | 2                | 1      | 1                       | 0      | 15                        | 4      | 16     |
| Nov. 2015   | 14              | 1      | 0              | 6      | 7                | 2      | 1                       | 0      | 7                         | 5      | 17     |
| Dec. 2015   | 15              | 4      | 1              | 5      | 8                | 1      | 3                       | 0      | 13                        | 11     | 18     |
|             | 175             | 31     | 7              | 63     | 55               | 27     | 24                      | 2      | 115                       | 83     | 178    |
|             | 84.95%          |        | 10.00%         |        | 67.07%           |        | 92.31%                  |        | 30.59%                    | 22.07% | 47.34% |

TOTAL EXPUNGEMENTS GRANTED IN CALENDAR YEAR 2015: 261 OUT OF 384 = 67.969%

Steven B. Caruso, Esq.  
Maddox Hargett & Caruso, P.C.  
80 Broad Street, 5th Floor  
New York, N.Y. 10004  
www.investorprotection.com  
(212) 837-7908

## FINRA DISPUTE RESOLUTION ARBITRATION AWARD REVIEW - 2016

| MONTH ENDED | POST-SETTLEMENT |        | CLAIMANT AWARD |        | RESPONDENT AWARD |        | BD/AP v. CUSTOMER AWARD |        | RULE 2080(b)(1) PREDICATE |        |        |
|-------------|-----------------|--------|----------------|--------|------------------|--------|-------------------------|--------|---------------------------|--------|--------|
|             | GRANTED         | DENIED | GRANTED        | DENIED | GRANTED          | DENIED | GRANTED                 | DENIED | A                         | B      | C      |
| Jan. 2016   | 6               | 3      | 0              | 3      | 5                | 0      | 1                       | 0      | 4                         | 2      | 8      |
| Feb. 2016   | 9               | 2      | 0              | 4      | 7                | 2      | 1                       | 0      | 6                         | 6      | 12     |
| Mar. 2016   | 8               | 3      | 0              | 3      | 1                | 2      | 0                       | 0      | 3                         | 2      | 7      |
| Apr. 2016   | 11              | 0      | 2              | 2      | 5                | 2      | 4                       | 0      | 8                         | 5      | 16     |
| May. 2016   | 13              | 4      | 0              | 4      | 4                | 1      | 1                       | 0      | 10                        | 7      | 10     |
| Jun. 2016   | 13              | 1      | 2              | 4      | 6                | 4      | 1                       | 0      | 8                         | 9      | 15     |
| Jul. 2016   | 13              | 0      | 0              | 9      | 2                | 4      | 1                       | 0      | 6                         | 8      | 10     |
| Aug. 2016   | 9               | 2      | 1              | 1      | 9                | 2      | 2                       | 0      | 7                         | 5      | 17     |
| Sept. 2016  | 6               | 4      | 0              | 2      | 4                | 4      | 0                       | 0      | 3                         | 3      | 6      |
| Oct. 2016   | 12              | 1      | 1              | 4      | 6                | 2      | 1                       | 0      | 6                         | 5      | 13     |
| Nov. 2016   | 6               | 1      | 1              | 5      | 8                | 0      | 1                       | 0      | 9                         | 2      | 12     |
| Dec. 2016   | 18              | 2      | 0              | 2      | 3                | 1      | 0                       | 0      | 9                         | 6      | 14     |
|             | 124             | 23     | 7              | 43     | 60               | 24     | 13                      | 0      | 79                        | 60     | 140    |
|             | 84.35%          |        | 14.00%         |        | 71.43%           |        | 100.00%                 |        | 28.32%                    | 21.51% | 50.18% |

TOTAL EXPUNGEMENTS GRANTED IN CALENDAR YEAR 2016: 204 OUT OF 294 = 69.388%

Steven B. Caruso, Esq.  
Maddox Hargett & Caruso, P.C.  
80 Broad Street, 5th Floor  
New York, N.Y. 10004  
www.investorprotection.com  
(212) 837-7908

## FINRA DISPUTE RESOLUTION ARBITRATION AWARD REVIEW - 2017

| MONTH ENDED | POST-SETTLEMENT |        | CLAIMANT AWARD |        | RESPONDENT AWARD |        | BD/AP v. CUSTOMER AWARD |        | RULE 2080(b)(1) PREDICATE |        |        |
|-------------|-----------------|--------|----------------|--------|------------------|--------|-------------------------|--------|---------------------------|--------|--------|
|             | GRANTED         | DENIED | GRANTED        | DENIED | GRANTED          | DENIED | GRANTED                 | DENIED | A                         | B      | C      |
| Jan. 2017   | 6               | 2      | 1              | 2      | 4                | 3      | 1                       | 0      | 4                         | 4      | 4      |
| Feb. 2017   | 8               | 0      | 0              | 1      | 4                | 5      | 2                       | 0      | 9                         | 3      | 7      |
| Mar. 2017   | 9               | 2      | 1              | 5      | 6                | 6      | 2                       | 0      | 9                         | 7      | 12     |
| Apr. 2017   | 17              | 3      | 0              | 5      | 0                | 1      | 2                       | 0      | 11                        | 7      | 8      |
| May. 2017   | 12              | 1      | 0              | 3      | 9                | 2      | 2                       | 1      | 11                        | 8      | 15     |
| Jun. 2017   | 12              | 2      | 0              | 6      | 2                | 3      | 3                       | 0      | 7                         | 5      | 12     |
| Jul. 2017   | 7               | 2      | 0              | 5      | 5                | 0      | 0                       | 0      | 5                         | 3      | 7      |
| Aug. 2017   | 13              | 0      | 1              | 3      | 4                | 2      | 1                       | 0      | 6                         | 6      | 13     |
| Sept. 2017  | 7               | 2      | 0              | 1      | 2                | 3      | 2                       | 0      | 8                         | 3      | 8      |
| Oct. 2017   | 11              | 3      | 2              | 4      | 2                | 1      | 4                       | 0      | 5                         | 8      | 14     |
| Nov. 2017   | 11              | 3      | 1              | 6      | 2                | 2      | 1                       | 0      | 9                         | 4      | 10     |
| Dec. 2017   | 15              | 1      | 1              | 4      | 4                | 0      | 1                       | 0      | 10                        | 7      | 12     |
|             | 128             | 21     | 7              | 45     | 44               | 28     | 21                      | 1      | 94                        | 65     | 122    |
|             | 85.91%          |        | 13.46%         |        | 61.11%           |        | 95.45%                  |        | 33.45%                    | 23.13% | 43.42% |

TOTAL EXPUNGEMENTS GRANTED IN CALENDAR YEAR 2017: 200 OUT OF 295 = 67.797%

This proposal should include employer weaponized U-5 comments which can be significantly more unfair and harmful than customer complaints. I included a detailed analysis of this issue in my response to the 360 notice which I incorporate herein.

[https://www.finra.org/sites/default/files/notice\\_comment\\_file\\_ref/SN-32117\\_Chepucavage\\_comment.pdf](https://www.finra.org/sites/default/files/notice_comment_file_ref/SN-32117_Chepucavage_comment.pdf) .

FINRA has long ignored the issue of employers making untrue and unfair comments on Form U-5 and now has an opportunity to partially rectify that problem which may be more common than the customer complaint issue. While expungement may not be the best characterization it does include expunging the offending/unfair words and replacing them with a fair and complete description of the reasons a person was terminated. Including such actions will allow FINRA to learn how often this occurs because today its too expensive to challenge such unfairness in arbitration. Finally, such descriptions are often related to customer complaints where there is an incentive for the firm to blame the individual as opposed to the firm's management.

Peter Chepucavage- [202-364-3804](tel:202-364-3804)  
3705 Corey Pl.N.W.  
Washington, D.C.20016

FINRA,

I have been a broker since 1984. I applaud FINRA requiring disclosure of all bond commissions on the confirm. I think customers should know what they paid. However making it harder to expunge meritless complaints o a brokers record is improper. The complaint was not determined to be wrong by a court process. However it registers as wrong with everyone who views it. I think 60,000 brokers would wrongly be affected by stiffening the expungement process.

Be well,  
Tony Christ

I am writing this email during the comment period regarding Regulatory Notice 17-42. We live in a society where we are supposed to be considered innocent until proven guilty. The current process for expungement already allows for a complaint to remain on an advisor's record even if the case is found to be frivolous and even not true entirely. Then we, as advisors, as required to spend time and money proving again that we are innocent of all claims. I personally have an existing example of how this is unfair to the advisor. A claimant testified in his deposition that he did not believe I did anything wrong nor was I guilty of any of the claims filed against me...but rather that his attorney told him he had to name me (along with the Broker Dealer) in the lawsuit in order to get the best claim and most recompense. While I am confident that this claim will be expunged from my record, how could it be right that I have to spend time and money to prove what the client stated under oath. Now, you are proposing to raise the cost and make the decision more difficult to prove that I am innocent when the claimant testified to such under oath?? Again...where is the innocent until proven guilty status we are all guaranteed under the law??

Please reconsider the proposals under Regulatory Notice 17-42 and provide a more fair process for cases to be heard simultaneously with the original complaint. That would seem to save everyone time and money...while being more fair to all involved.

**Roger B. Deal**

Managing Executive & Financial Advisor

**Sequoia Wealth Partners, LLC**

**3154 18th Avenue, Suite #7**

**Columbus, Nebraska 68601**

**402-563-1210 – Phone**

**402-562-7801 – Fax**

**9375 Burt Street, Suite 102**

**Omaha, NE 68114**

**402-504-1414 – Phone**

**402-502-5482 – Fax**



*Standing Strong For Your Financial Future*

[Roger@SequoiaWealthPartners.com](mailto:Roger@SequoiaWealthPartners.com)

[www.SequoiaWealthPartners.com](http://www.SequoiaWealthPartners.com)[\[sequoiawealthpartners.com\]](http://sequoiawealthpartners.com)

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To Whom It May Concern;

I am writing to express my sincere concern in how agents and advisors due process rights are constantly being violated.

Almost 10 years ago I received a bogus complaint by a consumer. This consumer actually solicited me ..she came to me for help with "rolling over" her IRA. She initiated the sale and she told me what she wanted done. I was somewhat a new agent at the time and going through a separation with my ex ..who happened to also be an agent. I was not aware of the FINRA process of a consumer complaint..but my ex was! And my ex was actually the one who set me up for the complaint!! My company settled for "in the best interests of consumer relations". Which I was told that is standard so consumers who are disgruntled can go along on their merry way. My E&O settled in favor for me, the agent, as I did nothing wrong. It wasn't until years later that I even knew about "Brokercheck" and that I had this bogus complaint still on my record. I was shocked that it was there...and shocked that I wasn't even aware of being able to "share my voice" about this bogus complaint. I went back to my company about this and to put my "voice" attached to this complaint a few yrs ago. However, it still had to "read" a certain way based upon "company policy"...or so I was told.

This all is so unfair (and criminal in my opinion) that an agents/advisors reputation is at stake..which is how we make our living..on our reputation... While a consumer can engage in wrongful doing or intended deception to result in financial or personal gain with a financial institution. This is called fraud folks! In addition, defamation of a person's character is also a civil wrong.

Bottom line ...We as agents and advisors need a fair system in place that protects the rights of people..whether they are an advisor or a consumer. I understand that we've come a long way from "buyer beware" and there should be agencies to protect consumers rights for being violated. But we also need systems and processes in place to equally protect the agent/advisors rights too. If we don't we will cultivate an industry that becomes "seller beware" and compromise the very integrity of what FINRA has intended.

Thank you,  
Kelly

sent from; Dr. Kelly A. Decker

**Center for Clinical Programs**

**Mailing Address:**

PO BOX 4037  
Atlanta, GA 30302-4037  
Phone: (404) 413-9270  
Fax : (404) 413-9229

**In Person:**

85 Park Place  
Atlanta, GA 30303



February 5, 2018

**VIA EMAIL to [pubcom@finra.org](mailto:pubcom@finra.org)**

Ms. Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

Re: Comments Concerning FINRA Regulatory Notice 17-42  
Expungement Process of an Associated Person

To whom it may concern:

Thank you for the opportunity to comment on Regulatory Notice 17-42 and its proposed changes to the expungement process. We work in the Georgia State College of Law's Investor Advocacy Clinic where we represent small investors who cannot afford legal representation. Because we work closely with investors, we understand how essential complete and accurate BrokerCheck records are. Investors rely upon this information to choose a financial professional, and they can be harmed when records are incorrect or incomplete. Our clients do not bring their claims lightly and are shocked when a well-founded claim draws a request for expungement, suggesting that their concerns are without merit.

We submit this comment in support of the proposal with some modifications. First, the one-year limitation period permits fair and equal investor participation in the process. Second, the heightened qualifications for the expungement arbitrator roster will result in reliable and informed decisions. Third, the in-person or videoconference requirement will ensure that decisions are based on the merits and involve all parties. Finally, we support language revisions to clarify the expungement process.

**A. The One-Year Limitation Period Facilitates Investor Participation.**

An associated person should bring any expungement within one year of the closing of the underlying customer case, as suggested in the proposal.<sup>1</sup> The one-year limitation ensures that relevant evidence is available and increases investors' ability to participate. Moreover, one year is more than a sufficient time in which to bring expungement proceedings for true error or fraud. Absent a reasonable time limit, associated persons could strategically wait years until witnesses and documents are no longer available. A one-year time limit on expungement claims balances

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<sup>1</sup> See FINRA, REGULATORY NOTICE 17-42, EXPUNGEMENT OF CUSTOMER DISPUTE INFORMATION 5 (2017) ("For the expungement request to be considered after the Underlying Customer Case closes other than by award, the associated person would be required to file the request within one year after FINRA closes the Underlying Customer Case, provided the expungement request is not barred.")

the interests of investors with those of associated persons by continuing to formalize the expungement process and ensuring fair resolutions.

**B. The Heightened Qualifications for the Expungement Arbitrator Roster Will More Result in Reliable and Informed Decisions.**

We support the requirement of additional qualifications for an arbitrator to be included on the Expungement Arbitrator Roster. Arbitrators experienced in securities, administrative law, or litigation will have the background necessary to engage in thorough deliberation over the details of an expungement request. Expungement requests are extraordinary in that there are very narrow grounds upon which they should be granted. Creating a roster with diverse backgrounds and a wealth of legal and securities knowledge will equip the panel with the necessary tools to provide the high-level scrutiny required for an expungement hearing.

We also support the proposition that the panel's decision be unanimous.<sup>2</sup> When an investor receives a positive outcome in a hearing, whether through award or settlement, he feels vindicated, satisfied that the wrong has been corrected. However, when the associated person still is able to expunge the issue from his CRD, the investor is essentially labeled a liar. Allowing a simple majority of the panel to remove the complaint from the associated person's record where the associated person or firm still had to pay a claim should require additional scrutiny. The requirement of a unanimous decision will ensure that scrutiny is present.

**C. The In-Person or Videoconference Requirement Makes It More Difficult for an Associated Person to Receive a One-Sided Decision.**

We support requiring an associated person who seeks expungement to appear personally at the hearing, whether the process takes place as part of the underlying case or not.<sup>3</sup> An expungement is a significant prize to an associated person, and as such the associated person should be required to attend a hearing in person to demonstrate their commitment to that prize. The permanent removal of customer complaints from an associated person's record allows the associated person to continue operating as if the complaint had never occurred. The magnitude of such a reward should mandate that an associated person appear in person at an expungement hearing. Accordingly, we believe that the option for an associated person to appear by videoconference should be permitted, if at all, in those simplified cases where a hearing did not take place.<sup>4</sup>

Additionally, we support bifurcating expungement requests from the merits of all customer cases. Doing so will facilitate an independent and thorough expungement hearing overseen by a

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<sup>2</sup> See FINRA, REGULATORY NOTICE 17-42, EXPUNGEMENT OF CUSTOMER DISPUTE INFORMATION 9 (2017) ("The proposed amendments would require that the panel agree unanimously to grant expungement . . .").

<sup>3</sup> *Id.* at 11 (" . . . FINRA believes that as the associated person is requesting the permanent removal of information from CRD, the associated person should be available in person to present his or her case and respond to questions from the panel.").

<sup>4</sup> Not all simplified arbitrations proceed only on the papers. A hearing may be held in a simplified arbitration upon the customer's request. FINRA R. 12800(c)(1). In any such cases, an associated person seeking an expungement should appear in person, with the expungement process mirroring the underlying proceeding. In those cases where the customer does not seek a hearing, holding the entire customer proceeding hostage to an in-person hearing requirement for the expungement request does not advance justice and should not be permitted.

separate, qualified panel. Separating expungement requests from customer cases will make the expungement process more rigorous and require a greater commitment by the associated person while maintaining the integrity of the CRD. At the same time, it will allow the merits to proceed more expeditiously. We recommend that this change be coupled with additional notifications to the investor about the expungement hearing to incentivize his or her participation in such hearings.

For expungement requests related to non-simplified cases, we support limiting the request to one opportunity during a bifurcated portion of the underlying case. Once an expungement request is made in the underlying case, a separate panel selected from the Expungement Arbitrator Roster should decide whether the request will be granted.

#### **D. FINRA Should Clarify the Expungement Process.**

In response to Question 1, we recommend clarifying the language regarding how information is expunged and by whom. As the notice describes, Rules 12805 and 13805 currently suggest that the arbitration panel can grant an expungement, when only a court can do so. Changing the language to “recommend” rather than “grant” will better describe the role of the panel versus the court in arbitration proceedings. This clarification should assist courts and parties in understanding the court’s role.

#### **Conclusion**

In conclusion, from our vantage point of working with aggrieved investors, we support changes to the expungement process to ensure that BrokerCheck remains a valuable resource and investors are treated fairly. An expungement should be limited to extraordinary circumstances, and adding requirements such as the one-year limitation, in-person hearings, and specially-qualified panels will ensure that expungement is granted only in cases where it is appropriate.

Thank you for this opportunity to share our comments to ensure the expungement process is not abused and regular investors have access to complete and correct information concerning their financial adviser.

Best regards,

*Benjamin Dell'Orto*

*Esmat Hanano*

*Alisa Radut*

Benjamin Dell'Orto  
Student Intern  
Student Reg. No. SP001565\*

Esmat Hanano  
Student Intern  
Student Reg. No. SP001567\*

Alisa Radut  
Student Intern  
Student Reg. No. SP001351\*

*Nicole G. Iannarone*

Nicole G. Iannarone  
Assistant Clinical Professor

\*All student interns in the Investor Advocacy Clinic, including these signatories, perform all work under the Georgia Student Practice Rule contained in Rules 91-95 of the Rules of the Supreme Court of Georgia as registered law students under the supervision of a licensed Georgia attorney.

I respectfully request that FINRA provide a swift and affordable process for advisors to expunge meritless claims off their records.

*Michael J. Di Silvio*

Managing Director - Investments

Financial Advisor

Di Silvio Financial Group

of Wells Fargo Advisors

# JONESBELL

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G. THOMAS FLEMING III\*  
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WILLIAM M. TURNER\*  
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KASUMI T. RODDICK  
NEIL M. KATSUYAMA  
KAYLA S.S. BETBOUT  
AUSTIN D. SCHAEFER  
ARSALAN IBRAHIM NASIR

\*A PROFESSIONAL  
CORPORATION

January 9, 2018



OF COUNSEL

MICHAEL J. GILL\*  
ELIZABETH T. PIERSON\*  
TRENTON J. HILL  
USMAN S. MOHAMMED

MAURICE JONES, JR.  
(1902-1987)  
EUGENE W. BELL  
(1926-1996)  
MICHAEL J. ABBOTT  
(1944-2015)

*Via Federal Express*

Financial Industry Regulatory Authority  
Attn: Marcia E. Asquith  
Office of the Corporate Secretary  
1735 K Street NW  
Washington, DC 20006-1506

Re: **FINRA Regulatory Notice 17-42**  
**(December 6, 2017)**

Dear Ms. Asquith:

We write in response to the request for comment on the proposals concerning “expungement of customer dispute information” as set forth in FINRA’s Regulatory Notice 17-42, which was dated December 6, 2017 (hereinafter, the “Proposal”).

Since 1977, this law firm has been actively involved in the representation of clients having legal matters concerning the financial services industry in general, and arbitration proceedings before FINRA Dispute Resolution (formerly NASD arbitration) in particular. In our view it is essential that FINRA Dispute Resolution be viewed by all as a neutral forum where both public customers, and industry members and their registered representatives can receive a fair and impartial resolution of their disputes. Over the past decades, many changes to FINRA’s Code of Arbitration (the “Code”) have enhanced FINRA’s reputation as a fair and impartial forum; unfortunately, that is not the case with respect to the changes to the procedures for expungement, as set forth in the Proposal.

This topic is of great importance to registered persons, given the relatively recent evolution of industry rules concerning the reporting of customer complaints. Today, most customer complaints against a registered person, including false and even defamatory claims, must immediately be reported on their CRD registration record; and there they must remain, publicly available on the Internet to be viewed by their customers, potential customers and anyone else, unless and until “expunged” from the CRD system. Traditional notions of basic fairness and due process demand that the right to seek expungement of false claims not be subjected to unreasonable conditions, restrictions and excessive fees; unfortunately, the Proposal would do just that, and thereby would diminish FINRA’s reputation as a fair and neutral forum. In our view, the proposed amendments to FINRA’s Codes of

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Arbitration Procedure relating to requests to expunge customer dispute information from the securities industry registration records of associated persons, as set forth in the Proposal, are ill-advised and should not be implemented, for the reasons set forth below. For ease of reference, we address the proposed changes in the order set forth in the Proposal.

***“All Requests for Expungement of Customer Dispute Information”***

FINRA proposes to require that, for all requests for expungement, the associated person seeking that relief must appear at the hearing, and that *“to grant expungement, a three-person panel of arbitrators must unanimously agree that expungement is appropriate . . . .”* (emphasis ours.) We believe this aspect of the Proposal is both inappropriate and unfair, for several reasons. First, under Section 12410 of the Code all rulings and determinations of the panel concerning customer disputes are to be made “by a majority of the arbitrators . . . .” (An identical rule is applicable to industry disputes under Section 13414 of the Code.) We can conceive of no good-faith basis for treating an associated person’s expungement request differently than a decision on the merits of a customer complaint. Any duly-appointed FINRA panel has the authority, by a majority vote, to enter an Award which could be financially and/or professionally disastrous for a registered person; such an Award by a majority of an arbitration panel would be final, and non-appealable (except on the very limited grounds applicable to a motion to vacate the award). If a determination by a majority of a FINRA arbitration panel is sufficient to financially or professionally destroy a registered representative who appears as a respondent before that panel, why should a unanimous decision of a FINRA arbitration panel be required to remove a false or erroneous claim from that associated person’s registration record?

To require a unanimous decision on any expungement request obviously would give a single individual sitting on a three-member arbitration panel the power to prevent, for improper reasons or no good reason at all, a meritorious request that a false or erroneous claim be removed from a representative’s CRD record. The Proposal to require a unanimous decision for expungement reflects a bias in favor not just of customer claimants, but of the claimants’ bar, and an antipathy toward registered persons seeking to maintain their good name and reputation in the industry. If FINRA truly desires to maintain “the integrity of the public record,” then its rules should facilitate – not complicate – the removal from the CRD record of claims that are false. We strongly urge that this aspect of the Proposal be rejected.

***“Expungement Arbitrator Roster”***

Under the Proposal, a new roster of “expungement arbitrators” would be culled from the “public chairperson” panel. To be included on that new panel, an individual would be required to (1) complete “enhanced expungement training,” (2) be admitted to practice law in at least one jurisdiction, and (3) have “five years’ experience in litigation, state or federal securities regulation, administrative law, or as a judge.” Conspicuously *absent* from this list, of course, is anyone having five or more years’ experience in the securities industry (from which substantially all customer arbitration claims arise).

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Conspicuously *included* within the requisite “disciplines” for inclusion on the expungement arbitrator roster would be members of the claimants’ bar, whose business is the litigation of customer complaints against associated persons and member firms. The claimants’ bar, of course, has a strong financial interest in having *all* customer complaints remain available on the CRD system; and claimants’ lawyers would certainly populate the proposed “expungement arbitrator roster.” This fact, coupled with the Proposal’s requirement of “unanimity” concerning any expungement request, would virtually guarantee that most, if not all, expungement requests made following adoption of the Proposal would be denied.

We believe that any FINRA arbitrator who is qualified to fairly decide the merits of a customer complaint should be equally capable of “understanding the unique nature of a request for expungement.” The creation of a new “expungement arbitrator roster” will neither promote a fair and impartial resolution of expungement requests, nor serve to the “maintain the integrity of the public record.”

***“Expungement Requests In Simplified Arbitration Cases”***

The Proposal would require in simplified cases that a registered person “wait until the conclusion of a customer’s simplified arbitration case to file an expungement request, which . . . would be heard by a panel selected from the expungement arbitrator roster.” For all the reasons set forth above, there should *not* be a separate “expungement arbitrator roster” created to consider expungement requests, and this is especially so with regard to “simplified” cases, for several reasons. First, there is no person more qualified to consider an expungement request than the arbitrator who hears all the evidence in the customer’s “simplified arbitration” case. Second, the additional time, effort, and expense required of an associated person to bring a *new* expungement proceeding after the conclusion of a “simplified arbitration” would make the process anything *but* “simplified” for the associated person. Once again, this aspect of the Proposal suggests an antipathy toward registered persons, and to expungement requests in general.

***“Expungement Requests Relating to Customer Complaints That Do Not Result in an Arbitration Claim”***

The Proposal would also require that an associated person seeking expungement of a customer complaint do so “within one year of the member firm initially recording the customer complaint to CRD.” In our view, a one-year window of eligibility for a registered representative to make an expungement request would be unreasonably short, arbitrary, and unfair, for several reasons.

First a one-year eligibility window is inconsistent with other provision of the Code. For many years, Section 12206 of the Code has provided a *six (6) year period of eligibility* for customers to file an arbitration claim following the “occurrence or event giving rise to the claim.” There is no basis for a one (1) year eligibility period for a registered representative to file an expungement request, other

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than to create a trap for an unwary registered representative, and to cause well-founded expungement requests to be forever time-barred.

Also, a one-year eligibility period for expungement requests would, as a practical matter, lead to inequitable results. In our experience, it sometimes happens that a registered representative may be unaware, for a variety of business or personal reasons, that a member firm (perhaps his or her previous employer) has reported a customer complaint on his or her CRD. Under the Proposal, the expiration of one-year from the date of the initial CRD report would be a bar to him or her making an expungement request, regardless of how ill-founded and meritless the customer complaint may have been.

This aspect of the Proposal once again reflects antipathy toward registered persons, and a bias in favor of the claimants' bar. For these reasons, we strongly urge that the "eligibility period" for expungement requests, if such a limitation is to be added to the Code, be the same as the eligibility period for customer complaints of Section 12206 of the Code, i.e. six (6) years.

***"Requesting Expungement Relief in the Underlying Customer Case (Where an Associated Person Is Named as a Party)"***

We would have no objection to a rule that would require an associated person, who has been named as a party *and has appeared in the underlying customer case*, to make his or her expungement request during the course of the underlying customer case. As stated above, we believe the arbitration panel assigned to resolve the underlying customer case is best situated to resolve a request that a claim be expunged from the associated person's record. However, we have the following objections and comments regarding specific aspects of this part of the Proposal:

- Where the registered person has (for whatever reason) not appeared as a respondent in the underlying customer case, no such limitation should apply; in that case, he or she should have the otherwise-applicable eligibility period in which to bring an expungement request. (As also set forth above, the "eligibility period" of such requests should be the same as the eligibility period for customer complaints, i.e., 6 years.)
- The Proposal would require that the expungement request be made by the individual respondent "no later than 60 days before the first scheduled hearing session." There is no good-faith basis for such a limitation, other than to create a potential trap for the unwary; and, such a limitation is inconsistent with Section 12503 of the Code, which provides that "a party may make motions in writing, or orally during any hearing session." Basic fairness requires that an individual respondent in the arbitration be permitted to make a motion for expungement at any time, up to an including closing argument in the underlying customer case.

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- The Proposal also would impose an additional “filing fee” for the making of an expungement motion: “along with the expungement request, the associated person would be required to pay a filing fee of \$1,425 or the applicable filing fee provided in Rule 12900(a)(1), whichever is greater.” Clearly, the only purposes of this amendment would be to financially punish the associated person for making an expungement request, and to generate additional (but unwarranted) revenue for FINRA. The presentation of an expungement request by a registered person who is a party to the underlying customer case does not require any additional administrative time or effort, either by FINRA, or by the arbitrators; thus, there is no good-faith basis for charging this new fee. Here again, the Proposal reflects an antipathy on the part FINRA both toward registered persons and toward expungement requests, and has an adverse effect on FINRA’s reputation as a fair and neutral forum.
- The Proposal specifies that although the panel would be required to agree unanimously to grant expungement, “in deciding the customer’s claims, however, a majority agreement of the panel would continue to be sufficient.” Again, there is no good-faith basis for allowing a final award to be rendered on a customer complaint by a majority of the arbitration panel, but requiring unanimity to grant the associated person’s expungement request.
- We strongly object to the Proposal’s requirement that, where a customer complaint has been resolved by settlement, the panel appointed in the underlying customer case “would not decide the associated person’s expungement request.” Once again, there is no good-faith basis for requiring an associated person to forfeit all of the time, effort and expense incurred in the underlying customer case, and to begin a new FINRA proceeding in order to make an expungement request. It is common for customer cases to settle, sometimes on the eve of the hearing, or even after several days of hearing on the merits. By that point, the associated person and/or his or her member firm will have incurred substantial attorneys’ fees, forum fees, and costs, in the defense of the customer’s claims; in addition, by that point, huge amounts of time and energy will have been devoted to the defense of the case, the selection of an arbitration panel, motion practice, and so on. There is no good-faith reason why all of that time, energy and money should be forfeited by requiring the associated person to commence a new FINRA proceeding for the purpose of making an expungement request. The arbitration panel selected to preside over the arbitration since its inception is clearly best suited to hear the associated person’s expungement request; this is perhaps best demonstrated by other parts of the Proposal, which bemoan the occasional instance where an expungement request is made to an arbitration panel that does not have the benefit of hearing from the claimant. Where a customer case is

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settled or dismissed before the completion of the hearing on the merits, the arbitration panel in that case has the advantage of having considered all of the pleadings, evidence and argument which the claimant and his or her lawyers have offered up to and including the point of settlement, or dismissal. The requirement that a new proceeding be initiated in this circumstance once again reflects an antipathy toward registered persons and expungement requests, which diminishes FINRA's reputation as a neutral forum.

- The Proposal also would prohibit a registered person who is *not* named as a respondent from intervening in the arbitration. This part of the Proposal is both unfair, and unnecessary. It is not uncommon for claimants' lawyers to name a member firm, but *not* name the associated person responsible for the alleged investment-related claim; this presents a tactical advantage for the claimants' bar, as the un-named associated person is less likely to participate vigorously in defense of the claim. In many cases, the un-named associated person may no longer be registered with the member firm when the customer complaint is filed, or when it goes to hearing; a registered person in this circumstance rightly may wish to intervene in the arbitration proceeding, and to protect his or her reputation by seeking expungement. The Proposal, however, "would foreclose the option for an un-named person to intervene in the underlying customer case." Once again, it is difficult to imagine any good-faith basis to "foreclose" a registered representative's right to intervene in an arbitration which concerns his or her alleged sales practice violations. Clearly, allowing intervention would be the most economical way to resolve both the customer's claims, and the associated person's request for expungement; to prohibit intervention in this circumstance serves no purpose, other than to allow the claimants' bar to make sure that the associated person does not participate in the defense of the customer's claims. Once again, this aspect of the Proposal would not enhance FINRA's reputation as a fair and neutral forum.

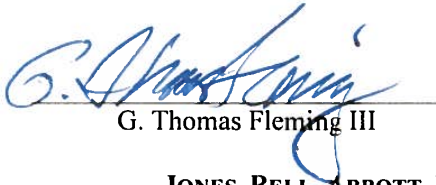
### ***Conclusion***

Registered persons seeking expungement of a customer claim that appears on their CRD Registration Record should be entitled to the same treatment under the FINRA Code as a customer bringing an arbitration claim: a fair hearing by a qualified panel of arbitrators, under procedural rules that are neither biased in favor of, nor prejudiced against, either side. Unfortunately, a plain reading of the Proposal contained in Regulatory Notice 17-42 leads to the conclusion that FINRA, bowing to pressure from the claimants' bar, is biased in favor of allowing ill-founded claims to remain on an individual's CRD Registration Record, and is prejudiced against the notion that a registered person should be given a fair opportunity to protect his or her reputation, and to have false claims expunged from his or her CRD Record.

Attn: Monica E. Asquith  
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For all of the reasons set forth above, we urge that the Proposal set forth in Regulatory Notice 17-42 be rejected.

Very truly yours,

  
G. Thomas Fleming III

of

  
Kevin K. Fitzgerald

**JONES, BELL, ABBOTT, FLEMING & FITZGERALD L.L.P.**

GTF:mmd



OFFICE OF THE  
INVESTOR ADVOCATE

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549**

February 15, 2018

**Submitted Electronically**

Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, CA 20006-1506

**RE: Regulatory Notice 17-42**

Dear Ms. Asquith:

The Office of the Investor Advocate<sup>1</sup> at the Securities and Exchange Commission (“Commission” or “SEC”) appreciates this opportunity to provide comments in regard to the issues raised in the Financial Industry Regulatory Authority, Inc.’s (“FINRA”) Regulatory Notice 17-42 (the “Notice”).<sup>2</sup> As described in the most recent Annual Report on Activities from our Office,<sup>3</sup> the SEC Office of the Investor Advocate and the SEC Ombudsman have a strong interest in proposed rule changes involving broker-dealer information contained in the online Central Registration Depository (“CRD”) because it plays such a key role in protecting investors. Securities industry regulators rely on data in CRD for licensing and enforcement activities and much of the information in CRD is ultimately made available to the public through BrokerCheck, a free research tool available on FINRA’s website.

**I. Introduction**

The Notice describes potential changes to the process for expunging records from the CRD. The notable changes could include, among many changes discussed in the Notice: (1) creating a limitations period for brokers and firms to request expungement from FINRA; (2) establishing a roster of attorney arbitrators with specialized experience; (3) requiring arbitrator panels to unanimously agree to award

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<sup>1</sup> Pursuant to Section 4(g)(4) of the Securities Exchange Act of 1934, 15 U.S.C. § 78d(g)(4) (2012), the Office of the Investor Advocate at the Securities and Exchange Commission is responsible for, among other things, analyzing the potential impact on investors of proposed rules of self-regulatory organizations. In furtherance of this objective, we routinely review and examine the impact on investors of proposed rulemakings of SROs, including those issued by FINRA, and make recommendations to the SROs proposing those rulemakings. As appropriate, we make formal recommendations and/or utilize the public comment process to help ensure that the interests of investors are fully considered as rules are adopted.

<sup>2</sup> FINRA, REG. NOTICE 17-42, PROPOSED AMENDMENTS TO THE CODES OF ARB. PROC. RELATING TO REQUESTS TO EXPUNGE CUSTOMER DISP. INFO. (Dec. 2017), <http://www.finra.org/industry/notices/17-42> [hereinafter NOTICE 17-42].

<sup>3</sup> SEC, OFF. OF THE INV. ADVOC., REP. ON ACTIVITIES, FISCAL YEAR 2017 (2017), at 27-30, <https://www.sec.gov/advocate/reportspubs/annual-reports/sec-investor-advocate-report-on-activities-2017.pdf>.

expungement; (4) potentially increasing the fees that brokers or firms must pay when requesting expungement; and (5) requiring the arbitrator panel to unanimously find and attest that the case has no investor protection or regulatory value. We understand that this proposal is one in a series of regulatory initiatives that FINRA is considering with respect to the expungement process and that FINRA staff has been working with the North American Securities Administrators Association (“NASAA”) on various expungement issues, including potential amendments to the existing regulatory review process.

The Office of the Investor Advocate has reviewed the Notice and the comments received to date. In brief, we believe that FINRA’s existing expungement framework, the standard of which is laid out in FINRA Rule 2080, needs substantive improvements and additional regulatory input in order to better serve the interests of retail investors. As a first step in a larger review, we commend FINRA for proposing procedural changes that should benefit retail investors. We are hopeful that the proposed changes will help expungement become the extraordinary remedy it was meant to be, and we encourage FINRA to continue working with NASAA and other interested parties on further refining and improving the expungement process.

That said, we are concerned that the proposed enhancements to the expungement process may cause brokers to seek to avoid the Rule 2080 process entirely, and instead request expungement of their records directly from a court of competent jurisdiction. We would not want to see significant forum-shopping in response to this rulemaking, and we recommend FINRA evaluate, as part of this rulemaking, whether there are ways to prevent brokers from going outside the enhanced expungement framework.

Further, we must note our concerns regarding the proposed requirement that, in order to recommend expungement, the arbitrators must also unanimously attest that the dispute has no investor protection or regulatory value. We believe that “investor protection” and “regulatory value” are relatively vague terms that could be interpreted differently and applied inconsistently by arbitrators. In particular, it is not clear from the Notice how FINRA arbitrators will appropriately assess regulatory value. We believe the proposal could be strengthened by providing greater clarity with respect to these terms, and FINRA should provide a framework for how these terms should be interpreted and applied by arbitrators.

Similarly, we are concerned that it may be premature to apply the expungement process to customer complaints that did not proceed to arbitration. In our view, FINRA should assess whether its many proposed modifications to the expungement process work as intended before expanding its process to this class of customer complaints.

## **II. Background**

Prior to the 1980s, there was no centralized electronic database for broker-dealer registration. FINRA’s predecessor, the National Association of Securities Dealers (“NASD”), originally developed the CRD database in conjunction with NASAA to centralize registration for the broker-dealer industry.<sup>4</sup>

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<sup>4</sup> See, e.g., NASAA, CRD & IARD, <http://www.nasaa.org/industry-resources/investment-advisers/crd-iard> (last visited Feb. 8, 2018).

When implemented in 1981, CRD consolidated a multi-state, paper-based registration process into a single, nationwide filing process and computer system.<sup>5</sup> Information in CRD is obtained through forms that registered representatives, broker-dealers, and regulators complete as part of the securities industry registration and licensing process.<sup>6</sup> In 1988, the NASD established its first public disclosure program to provide investors with important information about the professional background, business practices, and the conduct of NASD members and their associated persons.<sup>7</sup> This information about securities professionals, now distributed through FINRA's BrokerCheck program, was and continues to be derived from the CRD database.

Prior to 1999, arbitrators could order expungements of records from CRD without criteria and without a court order.<sup>8</sup> As applied by the NASD, arbitrator-ordered expungement of information from CRD was afforded the same treatment as a court-ordered expungement.<sup>9</sup> NASAA disagreed with this application, asserting that information in CRD constitutes state records and, due to state recordkeeping requirements, only a court of competent jurisdiction has the authority to order the destruction of state records. As a result of these discussions, in January 1999, NASD imposed a moratorium on arbitrator-awarded expungement of customer dispute information from CRD unless confirmed by a court of competent jurisdiction.

In 2001, NASD sought public comment on proposed safeguards and procedures for its expungement process, including what minimum criteria would need to be present for arbitrators to determine that expungement was appropriate, such as a finding that the customer's claim was without legal merit.<sup>10</sup> Building on this, in 2003, NASD received Commission approval to adopt Rule 2130 (now FINRA Rule 2080), which established procedures guiding the expungement process.<sup>11</sup> Since 2003, the procedures have been further refined through FINRA guidance, interpretations, and rulemakings.

At the time of Rule 2130's adoption, expungement was envisioned as an extraordinary remedy.<sup>12</sup> As currently applied, it appears that expungement is far from extraordinary, necessitating the changes in this proposal. Analysis conducted by FINRA<sup>13</sup> and the Public Investors Arbitration Bar Association

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<sup>5</sup> See OFF. OF INV. EDUC. & ADVOC., STUDY & RECOMMENDATION ON IMPROVED INV. ACCESS TO REGISTRATION INFO. ABOUT INV. ADVISERS & BROKER-DEALERS (Jan. 2011), at 13-14, <https://www.sec.gov/news/studies/2011/919bstudy.pdf>.

<sup>6</sup> See *id.*

<sup>7</sup> See FINRA NOTICE TO MEMBERS 02-74 (Nov. 2002), at 799, <http://www.finra.org/sites/default/files/NoticeDocument/p003441.pdf>.

<sup>8</sup> See NASD NOTICE TO MEMBERS 99-09 (Feb. 1999), at 47, <https://www.finra.org/sites/default/files/NoticeDocument/p004582.pdf>.

<sup>9</sup> *Id.*

<sup>10</sup> NASD NOTICE TO MEMBERS 01-65 (Dec. 2001), at 563, <http://www.finra.org/sites/default/files/NoticeDocument/p003745.pdf>.

<sup>11</sup> See Order Granting Approval to Amendment No. 2 to Proposed NASD Rule 2130, Exchange Act Release No. 48,933, 68 Fed. Reg. 74,667 (Dec. 24, 2003), <https://www.gpo.gov/fdsys/pkg/FR-2003-12-24/pdf/03-31646.pdf> [hereinafter Rule 2130 Order].

<sup>12</sup> See Comment Letter from Karen Tyler, President, NASAA, to Nancy M. Morris, Sec'y, SEC (Apr. 24, 2008), <http://www.nasaa.org/wp-content/uploads/2011/07/31-Release-No34-57572SR-FINRA-2008-010NASAA.pdf>.

<sup>13</sup> NOTICE 17-42, *supra* note 2, at 14.

(“PIABA”)<sup>14</sup> shows that the vast majority of expungement requests are granted. Over the years, FINRA has adopted procedural rules, published articles in *The Neutral Corner* to educate arbitrators, created the publicly available Expanded Expungement Guidelines page on its website, and has taken other steps, none of which have stemmed the high percentage of expungements granted by arbitrators. In 2015, NASAA expressed why, in its view, the current expungement framework does not work:

It is critical that arbitration panels—or whomever else is determining the merits of an expungement request—consider the regulators’ perspective in weighing whether a customer complaint should be expunged. The process, as designed, effectively charged the arbitrators with standing in the regulators’ shoes when assessing an expungement request. In practice, however, this does not happen. The parties involved in an expungement hearing are usually the broker requesting expungement and the arbitration panel. The expungement hearings rarely involve any customer testimony, which is often the only source of information that may contradict the evidence presented by a broker . . . . While a customer theoretically can testify or otherwise participate in an expungement hearing, the hearing often occurs after the customer dispute has been settled, leaving the customer and his or her counsel little incentive to oppose or otherwise object to the expungement. Precisely because a customer cannot be expected to adequately present and advocate a regulator’s view in whether an arbitration or customer complaint has regulatory value . . . the arbitration panel was given that role under Rule 2080. Unfortunately, despite changes to the process optimistically adopted to bolster that role, the process has failed.<sup>15</sup>

### III. Analysis

The Exchange Act requires that the rules of a registered securities association such as FINRA be designed to protect investors and the public interest.<sup>16</sup> In our view, several of the proposed amendments will enhance investor protection and we welcome their inclusion.<sup>17</sup> It makes sense to require the three arbitrators to unanimously agree to recommend expungement, to have FINRA codify the rights of investors to participate in expungement hearings, and to create a special panel to review customer complaints where the underlying arbitration was not decided on the merits.

We are also encouraged that FINRA staff has been working with NASAA on expungement issues. The states, as co-owners of CRD and advocates for investor protection, should be viewed as primary stakeholders in the expungement process. Thus, as FINRA works to finalize these

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<sup>14</sup> See, e.g., PIABA Report: Data Show That FINRA Efforts to Slow Expungement of Broker Misconduct Has Failed (Oct. 20, 2015), <https://piaba.org/sites/default/files/newsroom/2015-10/PIABA%20Press%20Release,%20Expungement%20Study%20Update.pdf> [hereinafter PIABA Report].

<sup>15</sup> See Comment Letter from William Beatty, President, NASAA, to FINRA Dispute Resolution Task Force (Aug. 31, 2015), at 4-5, <http://nasaa.cdn.s3.amazonaws.com/wp-content/uploads/2011/07/NASAA-Expungement-Letter-enclosure.pdf> [hereinafter NASAA Letter].

<sup>16</sup> See 15 U.S.C. § 78o-3(b)(6) (2010).

<sup>17</sup> From our review it appears that some changes, at least as currently proposed, may have little to no direct impact on investor protection, such as the increased filing fees for brokers seeking expungement. Therefore, we will limit our discussion to the matters most likely to impact investors.

enhancements, we recommend that FINRA give further consideration to the policies and procedures outlined by NASAA in its August 2015 letter to the FINRA Dispute Resolution Task Force, namely pre-notice to state regulators during an ongoing arbitration or a standardized protocol for states when FINRA waives its role as a party.<sup>18</sup>

With respect to the current proposal, we believe there are a few ways in which FINRA can enhance its proposed rule to better serve investors. We believe the proposal can be strengthened to prevent avoidance and promote consistent application of the rule. We also caution against immediately extending the expungement process to customer complaints that did not result in arbitration.

#### Unanimity of Rule 2080(b)(1) Finding

Proposed Rules 12805(b) and 13805(b) state that when deciding a request for expungement of customer dispute information, the arbitrators on an expungement panel must agree unanimously to grant expungement. The current process only requires a majority of arbitrators. In our view, this proposal will positively impact investor protection because it will provide a greater assurance that only meritless complaints are expunged, and we are hopeful that this requirement will encourage brokers to only seek expungement when the underlying customer dispute information is meritless. We are also hopeful that the percentage of cases that result in a recommendation of expungement will decline.

#### Codifying Expanded Expungement Guidance

FINRA's Expanded Expungement Guidance webpage provides guidance to arbitrators on the importance of allowing investors and their counsel to participate in the expungement hearing. It enumerates that arbitrators should: (1) allow the investor and their counsel to appear at the expungement hearing; (2) allow the investor to testify (telephonically, in person, or other method) at the expungement hearing; (3) allow the *pro se* investor or the investor's counsel to introduce documents and evidence at the expungement hearing; (4) allow the *pro se* investor or the investor's counsel to cross-examine the broker and other witnesses called by the party seeking expungement; and (5) allow the *pro se* investor or the investor's counsel to present opening and closing arguments if the panel allows any party to present such arguments.<sup>19</sup>

Proposed Rule 13805(c) codifies the first two enumerated items from the Expanded Expungement Guidance webpage. Specifically, it states that the investor may appear at the expungement hearing, and the investor may appear at the expungement hearing by telephone if the customer chooses to do so. Since expungement hearings in FINRA's forum are typically one-sided with no party arguing against expungement, we strongly support this provision because it signals to arbitrators that investors are critical stakeholders in FINRA's expungement process. This is especially important because FINRA's attempts to educate arbitrators about its regulations, policies, and

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<sup>18</sup> NASAA Letter, *supra* note 15, at 7.

<sup>19</sup> Notice to Arbitrators and Parties on Expanded Expungement Guidance, FINRA, <https://www.finra.org/arbitration-and-mediation/notice-arbitrators-and-parties-expanded-expungement-guidance> (last updated Sept. 2017).

procedures, including the importance of allowing retail investors to participate in the expungement process, have not always been heeded.<sup>20</sup>

We suggest that FINRA amend proposed Rule 13805(c) to include all five of the rights of investors and their counsel as identified on the Expanded Expungement Guidance webpage, as well as any other rights that FINRA considers important for investors to exercise when participating in expungement hearings. At a minimum, investors and their counsel should have the following rights added to proposed Rule 13805(c):

- Introduce evidence at the expungement hearing;
- Cross-examine the broker and witnesses introduced by the broker in the expungement hearing; and
- Present opening and closing arguments if the panel allows any party to present such arguments.

Codifying all five investor rights enumerated on the Expanded Expungement Guidance webpage will ensure that the remaining three investor rights are not misinterpreted by arbitrators as mere suggestions rather than as FINRA mandates.

#### Special Panel Review of Cases That Do Not Close On the Merits

Pursuant to proposed Rules 12805(a) and 12806, if a customer-initiated arbitration ends before the hearings on the merits concludes, any expungement request will be decided by a new three-person panel selected from the Expungement Arbitration Roster. The arbitrators on this roster will be provided expanded training that would emphasize that the panel “would need to review more proactively the request and documentation and, if necessary, ask questions and [ask] for more information, before making a decision.”<sup>21</sup>

We support this proposed amendment because FINRA’s data shows that for customer complaints where there was an arbitration not decided on the merits, the expungement rate is 88 percent,<sup>22</sup> which is simply too high for an *extraordinary* remedy. As FINRA states in the Notice, the special arbitrator roster may be able to “better understand the unique nature of this extraordinary remedy and the importance of maintaining the integrity of the public record.”<sup>23</sup> We believe that a more proactive, engaged arbitration panel may be able to conduct a more robust review of the facts before deciding whether one of the Rule 2080 prongs are present. As a result, we believe the creation of the special

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<sup>20</sup> See, e.g., *Royal Alliance Associates v. Liebhaber*, 206 Cal. Rptr. 3d 805, 808 (Cal. Ct. App. 2016). In that case, the retail investor was not permitted to participate in the underlying expungement hearing. When the investor objected, the arbitrators on the panel errantly concluded that the proper process was followed. The California appellate court ruled that investors have a right, as a matter of fairness, to challenge a broker’s efforts to seek expungement.

<sup>21</sup> NOTICE 17-42, *supra* note 2, at 22 n.38.

<sup>22</sup> *Id.* at 14.

<sup>23</sup> *Id.* at 10.

panel with additional training and a proactive fact-finding approach is an improvement to the current expungement process.

#### Simplified Arbitration Expungement Requests

Proposed Rule 13800(f) provides that a broker may only request expungement of customer dispute information at the conclusion of a simplified arbitration, and that a panel from the Expungement Arbitrator Roster would consider and decide the expungement request. FINRA states that holding the expungement hearing during the arbitration “delays the customer’s case and the rendering of an award in the customer’s simplified case” and the proposal would “ensure that expungement requests would not be heard during the simplified case.”

We support this proposed amendment, and we applaud FINRA’s efforts to make the arbitration process faster and more efficient for retail investors. Although most investors and their counsel may not have an incentive to participate in expungement hearings, some may want to do so, including investor participants in FINRA’s simplified arbitration forum. Accordingly, it is critical that FINRA inform the investor about the pending expungement request and permit the investor to participate in that matter.

Regulatory Notice 17-42 asks whether the single arbitrator in a simplified arbitration should be permitted to decide an expungement request in lieu of the panel of three arbitrators. In our view, the arbitrator in a simplified arbitration should not be permitted to decide an expungement request alone because it will be easier for a broker to convince one arbitrator, rather than a panel of three arbitrators, to recommend expungement. We recognize that the arbitrator who conducts the simplified arbitration may be able to provide valuable insights to an expungement panel related to the same customer dispute and, as such, we have no objection to the addition of this arbitrator to the panel.

#### Broker Avoidance of FINRA Rule 2080 Expungement

Regulatory Notice 17-42 asks whether commenters believe that named associated persons would request expungement in every case to preserve the right to have the expungement claim heard and decided. As noted above, we believe that this proposal could have an unintended, almost opposite effect: brokers may choose to avoid the newly enhanced FINRA expungement process and instead file their request for expungement directly with a court of law. Accordingly, we recommend that FINRA amend its Code to prohibit brokers from sidestepping its dispute resolution forum by filing a request for expungement directly with a court of competent jurisdiction.

Under the current expungement framework, brokers who request expungement from FINRA may expect a one-sided hearing and an award of expungement most of the time. This arbitration award is then submitted to a court of law, often with FINRA waiving its right to oppose the expungement request and without the participation of the investor who initiated the complaint. The award is usually granted deference by the court pursuant to the Federal Arbitration Act. Thus, it would appear that the current arbitration-based framework results in decisions tilted in the broker’s favor.

Because this proposal raises the bar for brokers seeking Rule 2080 expungement, some brokers may seek to avoid FINRA’s new process altogether. If the proposed rules go into effect, brokers seeking an expungement award from FINRA will face heightened requirements: (a) a potentially higher

fee; (b) new procedural requirements, including time limitations; and (c) the unanimous decision to recommend expungement. Then, after the broker satisfies these requirements, the broker must still file a request for expungement with a court of competent jurisdiction. NASAA's comment notes that, even under the current rules that tend to work in brokers' favor, "more and more brokers are bypassing the Rule 2080 process entirely by going directly to court."<sup>24</sup> We believe this trend is likely to continue or accelerate under the new rules because a broker may prefer to simply proceed directly to the courthouse with their request, rather than attempt to meet these enhanced standards. Therefore, to avoid unintended outcomes, FINRA should consider ways that its rules may discourage brokers from sidestepping its dispute resolution forum by filing requests for expungement directly with a court.

### Unanimity of "No Investor Protection or Regulatory Value" Finding

Proposed Rules 12805(b) and 13805(b) provide that when deciding a request for expungement of customer dispute information, the arbitrators on an expungement panel must make a finding in the award that the dispute has no investor protection or regulatory value. We appreciate the apparent intent behind this rule – to raise the bar and make expungement a more extraordinary remedy than it already is in practice.

As noted above, however, we believe this requirement could be strengthened by FINRA providing greater clarity regarding the terms "investor protection" and "regulatory value" because they are relatively vague terms that could be interpreted differently and applied inconsistently by arbitrators. We are especially concerned about how arbitrators will assess the term "regulatory value" because arbitrators are not regulators and they are not guided by regulatory concerns.<sup>25</sup> We recognize that these terms have been used by FINRA in communications with arbitrators in the past,<sup>26</sup> but that does not mean that arbitrators fully understand what they mean as terms of art. Because of this, FINRA should also provide a framework for how these terms should be interpreted and applied by arbitrators.<sup>27</sup>

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<sup>24</sup> Comment Letter from Joseph Borg, President, NASAA, to Marcia E. Asquith, FINRA (Feb. 5, 2018), at 7, [http://www.finra.org/sites/default/files/17-42\\_NASAA\\_comment.pdf](http://www.finra.org/sites/default/files/17-42_NASAA_comment.pdf).

<sup>25</sup> All customer dispute information has presumptive *de facto* investor protection and regulatory value because firms are required to report this data to FINRA via the uniform registration forms.

<sup>26</sup> See, e.g., FINRA, *THE NEUTRAL CORNER, A Closer Look at Expungement: Asking the Right Questions* (Vol. 4, 2013), at 6, <http://www.finra.org/sites/default/files/Publication/p410646.pdf>.

<sup>27</sup> Our concerns have a historical basis. In 2003, FINRA's predecessor, the NASD, dismissed concerns that Rule 2130 (Rule 2080) would make expungement easier to obtain because, as noted in the SEC order approving the rule, "arbitrators will know the standards for expungement relief under proposed Rule [2080], because they will have received appropriate training, and . . . arbitrators will only grant expungement relief based on those standards." Rule 2130 Order, *supra* note 11, at 74,670. This assessment has subsequently proven to be misguided. As NASAA noted in their August 2015 letter to the FINRA Dispute Resolution Task Force, arbitrators have been empowered under the Rule 2080 framework to serve as a substitute for direct regulator involvement in the expungement process, but they are third-parties who "routinely elevate the individual broker's concerns above regulatory imperatives." NASAA Letter, *supra* note 15, at 4. Just last year, FINRA observed the "practice of brokers continually being granted expungement of their disciplinary histories from industry databases," an observation supported by FINRA and PIABA data that show that arbitrators grant expungement in the vast majority of cases. Antoinette Gartrell, *FINRA to Address Expungement Issues, Arbitration Chief Says*, BNA (Mar. 21, 2016), <http://www.bna.com/finra-address-expungement-n57982068766>; NOTICE 17-42, *supra* note 2; PIABA Report, *supra* note 14.

### Complaints That Do Not Result In an Arbitration Claim

Under the proposal, FINRA permits the expungement of customer complaints reported to FINRA that did not result in an arbitration claim.<sup>28</sup> The proposal requires a broker to file an expungement request: (a) within one year from the date that the firm initially reported the customer complaint to CRD; or (b) if the firm reported the complaint to FINRA before the effective date of the proposal, within six months from the effective date of the proposal.<sup>29</sup>

We do not believe that now is the time to expand the Rule 2080 expungement process to claims that did not result in arbitration. With this proposal, FINRA is taking substantial steps at refining the expungement process. We would prefer to see the results of the new process before introducing an entirely new class of complaints to the mix. We recommend that FINRA first assess whether the Expungement Arbitrator Roster is performing as expected with arbitrated complaints that do not conclude on the merits, and whether further modifications to the roster's training program are necessary.


### **IV. Conclusion**

While we commend FINRA for proposing procedural changes that should benefit retail investors, we are concerned that the proposal could incentivize brokers to avoid the Rule 2080 expungement process entirely and instead file requests for expungement directly with the courts. We encourage FINRA to consider how to best mitigate this risk and limit the circumstances where a broker can circumvent the Rule 2080 process. We are also concerned that arbitrators, as non-regulator third-parties, will not understand the regulatory terms "investor protection" and "regulatory value" as terms of art. We encourage FINRA to provide greater clarity with respect to these terms and develop a framework to guide how these terms should be interpreted and applied by arbitrators. On the whole, however, we are largely supportive of the proposed procedural changes contained in the Notice and we wish to see FINRA, after reviewing all the comments and consulting with NASAA, move quickly in seeking Commission approval for these rules.

Should you have any questions, please do not hesitate to contact either of us, or Senior Counsel Adam Moore, at (202) 551-3302.



Rick A. Fleming  
Investor Advocate



Tracey L. McNeil  
Ombudsman

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<sup>28</sup> NOTICE 17-42, *supra* note 2, at 7.

<sup>29</sup> *Id.*



Securities Arbitration Clinic  
St. Vincent DePaul Legal Program,  
Inc.

8000 Utopia Parkway  
Queens, NY 11439  
Tel (718) 990-6930  
Fax (718) 990-6931  
www.stjohns.edu

February 5, 2018

Via email to [pubcom@finra.org](mailto:pubcom@finra.org)  
Ms. Marcia E. Asquith  
Officer of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 2006-1506

Re: **FINRA Regulatory Notice 17-42**  
**Expungement of Customer Dispute Information**

Dear Ms. Asquith:

Thank you for the opportunity to comment on the issue of expungement of customer dispute information. We are writing this comment on behalf of the Securities Arbitration Clinic at St. John's University School of Law (the "Clinic"). The Clinic is part of the St. Vincent De Paul Legal Program, Inc., a not-for-profit legal services organization. The Clinic represents small aggrieved investors and is committed to investor education and protection. Accordingly, the Clinic has a strong interest in the rules governing the information that may be available to customers when deciding with whom to invest.

Generally, the Clinic is supportive of the proposed changes to the rules governing when and how an associated person may seek expungement of customer complaint information from the CRD, and by extension, BrokerCheck.

The Clinic supports the creation of an Expungement Arbitrator Roster. The Clinic supports the proposal that arbitrators eligible for the Expungement Arbitrator Roster be chair-qualified attorneys. Expungement of customer complaint information is an extraordinary remedy, which requires a different determination than whether a firm or associated person is liable to the customer for damages. We believe enhancing the

training and qualifications of public chairpersons to serve on an Expungement Arbitrator Panel will help ensure greater integrity of the expungement process.

Consonant with FINRA's goal of maintaining the accuracy of the data in the CRD and, therefore BrokerCheck, the Clinic supports requiring the standard for granting expungement be a finding that the customer dispute information has no investor protection or regulatory value. This will help strengthen investor protection by improving confidence in the accuracy of the CRD and BrokerCheck.

The Clinic strongly agrees with requiring associated or unnamed persons to wait until the conclusion of a customer's case to file an expungement request. We believe that the result of the customer's case will assist the arbitrator panel in determining whether or not the customer dispute information has any investor protection or regulatory value. The Clinic suggests that associated persons be prohibited from seeking expungement if there has been a finding of liability in the underlying arbitration.

Additionally, the Clinic supports separating the expungement request from the underlying arbitration to allow for consistency in how expungement requests are considered. In cases under \$100,000, a single arbitrator considers the merits of the case. The arbitrator will be a public chair-qualified arbitrator; however, the arbitrator may or may not be on the Expungement Arbitrator Roster. In cases in excess of \$100,000, three arbitrators consider the merits of the case, however, it is possible that none of the arbitrators will be from the Expungement Arbitrator Roster. In addition, in cases under \$100,000, a single arbitrator will consider the expungement request, while three arbitrators must reach a unanimous decision for cases where the customer complaint requested damages in excess of \$100,000. To ensure uniformity in how expungement requests are considered, all expungement requests should be heard by a panel of three arbitrators from the Expungement Arbitrator Roster. To the extent an arbitrator in the underlying customer dispute is qualified as an Expungement Arbitrator, we would have no objection in that arbitrator being retained on the new panel to consider the expungement request.

In addition, by separating the expungement request from the underlying customer case, customers should receive faster decisions in simplified cases. Currently, if an associated person requests expungement in a simplified case, the arbitrator must hold a hearing to consider the request, notwithstanding that the customer did not request a hearing on the underlying dispute. This delays the process, as the arbitrator may only hold the hearing once he has made a determination on the merits of the case. However, that decision is not relayed to the parties, because the award may not be finalized until all outstanding issues (expungement) are decided. The Clinic thanks FINRA for recognizing and attempting to address these issues by proposing that expungement requests will be bifurcated from simplified arbitrations.

In addition, we support allowing the proposed expungement process to proceed without the customer having to be named a party to the request. We do believe that customers must have notice of the expungement request and the right to appear.

In addition, if the customer does wish to appear in connection with an expungement request, we support continuing to allow the various forms of appearance contemplated by FINRA in its guidance to the parties and arbitrators: (i) the customer and their counsel may appear at the expungement hearing; (ii) the customer may testify (telephonically, in person, or other method) at the expungement hearing; (iii) counsel for the customer or a pro se customer may introduce documents and evidence at the expungement hearing; (iv) counsel for the customer or a pro se customer may cross-examine the broker and other witnesses called by the party seeking expungement; and (v) counsel for the customer or a pro se customer may present opening and closing arguments if the panel allows any party to present such arguments.<sup>1</sup> The Clinic represents individuals, at no cost to the customer, who cannot otherwise obtain representation. Our clients are often elderly, with health issues which may make appearing for a hearing difficult. Therefore, we support FINRA's belief that customers should be able to participate in an expungement hearing without having to appear in person. By allowing the customer flexibility, customers may be better able to participate in the expungement request.

Given the reported problems associated with the current expungement process, the Clinic supports the proposed changes to the expungement process. Thank you for your consideration of this matter.

Very truly yours,

/s/  
Kelly Frevele  
Legal Intern

/s/  
Sigourney Norman  
Legal Intern

/s/  
Christine Lazaro  
Director of the Securities Arbitration Clinic  
and Professor of Clinical Legal Education

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<sup>1</sup> See FINRA, "Notice to Arbitrators and Parties on Expanded Expungement Guidance," September 2017, available at <http://www.finra.org/arbitration-and-mediation/notice-arbitrators-and-parties-expanded-expungement-guidance>.

I do not agree with FINRA changing the rules on Expungement. I had a meritless claim from a beneficiary of the account. The account was profitable and the lawyer settling the estate was so upset that he wrote the retraction letter for the client. The client was told by another broker to file a complaint and that she would get the losses back. There were no losses.

David W. Gamblin  
Vice President  
Financial Advisor

NMLS ID 1285388

**Morgan Stanley Wealth Management**

8150 N. Wickham Rd Melbourne, FL 32940

Direct Line 321-253-6844

Office 321-255-2400

Toll free 800-949-2001

Fax 321-751-2060

Email [David.W.Gamblin@morganstanley.com](mailto:David.W.Gamblin@morganstanley.com)

Research on any stock is available upon request

**KEESAL, YOUNG & LOGAN**

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(562) 436-7416

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HERBERT H. RAY, JR.\*†  
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PHILIP R. LEMPRIERE\*‡

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STACEY MYERS GARRETT  
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GLEN R. PIPER  
SANDOR X. MAYUGA  
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MELANIE L. RONEN‡  
AUDETTE PAUL MORALES  
BENTLEY P. STANSBURY III‡  
DAVID A. TONG‡  
STEFAN PEROVICH  
TARA B. VOSS  
NATHAN R. JASKOWIAK  
JENNIFER M. PORTER

MOLLY J. HENRY†  
AILAN LIU  
MICHAEL T. WEST  
RYAN S. LEAN  
KRISTY H. SAMBOR  
ELYSE W. WHITEHEAD  
ERIN WEESNER-MCKINLEY  
IAN ROSS  
SAMANTHA W. MAHONEY‡  
HILLARY A. DARNELL  
JOSHUA NORTON  
FRANCESCA M. LANPHER  
VALERIE I. HOLDER†  
IGOR V. STADNIK†  
SIMON M. LEVY

BRYCE CULLINANE  
ASHLEY E. IMPELLITTERI  
ALEXANDER J. BUKAC  
CURTIS V. ABRAM  
JARED W. SPEIER  
CHERYL S. CHANG  
KATHERINE L. HANDY  
TAYLOR J. ALTMAN  
ZACHARY T. BERNE\*  
CASSIDY A. WALLACE  
ANDREW B. MASON  
JAMES L. KRITENERINK  
SAMANTHA D. PARRISH  
NATALIE M. LAGUNAS

February 1, 2018

OF COUNSEL  
ROBERT H. LOGAN  
DOUGLAS R. DAVIS\*†  
RICHARD A. APPELBAUM+  
REAR ADMIRAL, U.S.C.G. (RET.)  
ELIZABETH A. KENDRICK  
DAVID W. TAYLOR‡  
WILLIAM MCC. MONTGOMERY

\* ADMITTED IN ALASKA  
† ADMITTED IN WASHINGTON  
‡ ADMITTED IN WASHINGTON & CALIFORNIA  
§ ADMITTED IN ALASKA & CALIFORNIA  
+ ADMITTED IN DISTRICT OF COLUMBIA & FLORIDA  
° REGISTERED FOREIGN LAWYER WITH THE LAW SOCIETY  
OF HONG KONG & ADMITTED IN NEW YORK  
± SOLICITOR ADMITTED IN ENGLAND, WALES AND NORTHERN  
IRELAND

ALL OTHERS ADMITTED IN CALIFORNIA

**Via E-Mail – pubcom@finra.org**

Ms. Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, D.C. 20006-1506

Re: **Comments regarding FINRA Regulatory Notice 17-42 (12/6/2017)**

Dear Ms. Asquith:

We write in response FINRA's request for comment on the proposed rule changes concerning expungement of customer dispute information set forth in FINRA's Regulatory Notice 17-42 (December 6, 2017).

Since 1970, Keesal, Young & Logan has represented companies and individuals associated with the financial services industry. Our attorneys have appeared in securities arbitration proceedings conducted by the Financial Industry Regulatory Authority (FINRA), the New York Stock Exchange, Pacific Stock Exchange, American Stock Exchange, National Association of Securities Dealers, American Arbitration Association, Judicial Arbitration and Mediation Services (JAMS), National Futures Association and the Municipal Securities Rulemaking Board. We also have significant experience handling regulatory proceedings initiated by the Securities and Exchange Commission, FINRA and state regulators, and frequently speak on topics related to the securities industry in general and FINRA procedure generally. The opinions and views expressed in this letter are solely those of Keesal, Young & Logan, P.C.

**Introduction**

Associated persons' livelihoods depend on their reputations. The overwhelming majority of associated persons work diligently to serve investors' needs with integrity and professionalism. Nevertheless, most customer complaints against associated persons must be reported on the associated persons' Central Registration Depository ("CRD") records and also appear on the associated persons' publicly-available BrokerCheck records regardless of whether

SAN FRANCISCO OFFICE  
450 PACIFIC AVENUE  
SAN FRANCISCO, CA 94133  
(415) 398-6000  
FACSIMILE:  
(415) 981-0136 • (415) 981-7729

ANCHORAGE OFFICE  
SUITE 650  
1029 WEST THIRD AVENUE  
ANCHORAGE, AK 99501-1954  
(907) 279-9696  
FACSIMILE: (907) 279-4239

SEATTLE OFFICE  
SUITE 3300  
1301 FIFTH AVENUE  
SEATTLE, WA 98101  
(206) 622-3790  
FACSIMILE: (206) 343-9529

HONG KONG OFFICE  
SUITE 1603  
299 QUEEN'S ROAD CENTRAL  
HONG KONG  
(852) 2854-1718  
FACSIMILE: (852) 2541-6189

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the complaints are timely, justified or meritorious. There is no “gatekeeper” function to weed out false, factually impossible or even defamatory complaints before they are publicly reported on an associated person’s CRD record. Rather, the only tool associated persons have to restore their professional reputations and good names after the filing of such unmeritorious claims is the expungement process.

FINRA and its predecessor organizations have a long history of recognizing the importance of a fair expungement process. In 2001, FINRA’s immediate predecessor, the National Association of Securities Dealers Regulation (“NASD”), noted that “individuals in the brokerage community have an interest in securing a fair process that recognizes their stake in protecting their reputations and permits expungement from the CRD system when appropriate....” (NASD Notice to Members 01-65, p. 565 (2001)). NASD Regulation likewise recognized that “in some cases, allegations of misconduct may be without merit or may falsely or mistakenly accuse associated persons of engaging in misconduct...” and that those types of allegations “may unfairly tarnish the reputations of those associated persons....” (*Id.*, p. 566.) In our opinion, it is critical that the CRD record-keeping system and FINRA Dispute Resolution treat all involved—the investing public, broker-dealer firms, and associated persons—in a fair and neutral manner. We agree with and commend FINRA’s goal of providing a fair and neutral forum for public investors; of course, that goal also should embody the equally important goal of providing a fair and neutral forum for associated persons.

Although some of the changes proposed by Regulatory Notice 17-42 are relatively minor, others unfairly skew the expungement procedures against associated persons and will result in an unfair, and unfairly administered, forum. While investor protection and overall transparency are imperative, many of the proposed rule changes do not advance those goals. In the end, the changes serve mainly to punish associated persons who are trying to serve their clients honestly and professionally. That does not protect investors. We therefore urge FINRA’s Board of Governors to reject most of the changes proposed by Regulatory Notice 17-42 and to decline to submit the proposed amendments to the Securities and Exchange Commission for adoption. The reasons for our views are discussed below.

### **Comments on Regulatory Notice 17-42**

**1. Regulatory Notice 17-42 asks whether the word “grant” in FINRA Rules 12805 and 13805 should be changed to “recommend” or some other description to more accurately reflect the panel’s authority in the expungement process.**

We agree that the word “grant” in FINRA Rules 12805 and 13805 should be changed to “recommend.” This is a clarifying change that accurately reflects the scope of the panel’s authority.

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**2. Regulatory Notice 17-42 proposes that associated persons who are named parties in an arbitration be required to seek expungement relief in the “Underlying Customer Case” or else they will be barred from seeking expungement relief at a later date. (Regulatory Notice 17-42, I.A.1.)**

If an associated person *does not appear* in the “Underlying Customer Case” (perhaps because he or she was not properly served with the claim and had no notice of it, or because he or she is no longer subject to FINRA’s jurisdiction), we believe it would violate principles of fairness and due process to bar the associated person from seeking expungement relief at a later date.

By making it *mandatory* for associated persons to seek expungement relief in the Underlying Customer Case at the risk of being barred from seeking that relief at a later date, Regulatory Notice 17-42 virtually ensures that every associated person will assert a claim for expungement in every case in which they are named. This will result in increased expense to every associated person and to every member firm that employed the associated person during the time of the events alleged in the Underlying Customer Case. In addition, it will increase the cost and expense associated with arbitration, which perversely could impede the goals of protecting investors and ensuring that FINRA arbitration remains an expedient and cost-effective forum.

To address this very real concern, we suggest that where an associated person’s request for expungement relief is granted under Rule 2080 as part of the Underlying Customer Case, the arbitrators be specifically authorized to assess, in appropriate cases, any additional filing fees or costs associated with the expungement to the associated person (and against the customer who initiated the unmeritorious claim).

**3. To seek expungement relief as part of the resolution of the “Underlying Customer Case,” Regulatory Notice 17-42 proposes that associated persons be required to (1) file the expungement request no later than 60 days before the first scheduled hearing session (or obtain an extension of that deadline) and (2) pay a filing fee of \$1,425 or the filing fee provided in Rule 12900(a)(1), whichever is greater, and further contemplates the assessment of a “member surcharge” and a “process fee.” (Regulatory Notice 17-42, I.A.2.)**

If an associated person has been named in *and has appeared* in an Underlying Customer Case, we agree that it is reasonable to require the associated person to state his or her intent to seek expungement relief at least 60 days before the first scheduled hearing date (or to seek relief from that deadline by way of a

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motion). This process ensures that all participants in the Underlying Customer Case are on notice of the issues to be addressed and determined at the evidentiary hearing.

We urge FINRA to reject the proposed \$1,425 filing fee that an associated person would be required to pay to restore his or her good name under the expungement procedures in the Underlying Customer Case, as well as the related “member surcharge” that would be charged to the associated person’s employer and/or former employer(s).<sup>1</sup> Regulatory Notice 17-42 does not explain the rationale for imposing these additional filing fees on an associated person, nor does Regulatory Notice 17-42 justify imposing a “member surcharge” and “process fee” on the associated person’s employer during the time of the events at issue, *regardless of whether that member is a named party to the arbitration*. Since Regulatory Notice 17-42 would *require* an associated person to seek expungement relief in the Underlying Customer Case (where the associated person appears in the Underlying Customer Case), the expense of empaneling and compensating arbitrators and administering the case should be handled as part of the Underlying Customer Case. Any additional administrative or processing burden as a result of the expungement request would be *de minimis*.

Additionally, we are concerned about Regulatory Notice 17-42’s proposal that all member firms who employed the associated person during the time of the events giving rise to the dispute would be subject to a member surcharge. The proposal fails to recognize at least three realities:

First, Regulatory Notice 17-42 neither defines nor provides any guidelines regarding the meaning of the phrase “during the time of the events giving rise to the dispute.” Frequently, an “occurrence or event” that is the basis for a customer’s claim occurred years ago, but the customer contends that he or she is entitled to damages up to and including the date of the hearing, in some instances based on the argument that there exists a “continuing duty” or “continuing harm.” Does the “time of the events giving rise to the dispute” refer to simply the date of the event or occurrence that gave rise to the dispute? Or does it refer to the entire time period that the customer contends is at issue (frequently a hotly contested issue).

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<sup>1</sup> By way of comparison, the cost to file a complaint in Los Angeles County Superior Court is \$435 (unlimited civil cases). Cal. Gov. Code §§70611, 70602.5, 70602.6.

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Second, where an associated person changes employers during the events alleged in the claim, the former firm may not wish to pay a member surcharge and “process fee” for the former employee; likewise, the new employing firm may not wish to pay a member surcharge and “process fee” relating to conduct that arguably occurred long before the associated person was hired. The imposition of these fees (whether mandatory or voluntary) on the former and current member firms creates an obvious tension between the associated person and his or her former and current employer(s). This tension may deter an associated person from pursuing meritorious requests for expungement relief simply because of unrelated economic pressure.

Third, an associated person’s employment may change as a result of a broker-dealer firm being sold or acquired by another firm. In that instance—where the associated person does not voluntarily change jobs but instead the employing firm changes names or owners around the associated person—will both Firm 1 and Firm 2 (the *former* member firm and the *new* member firm) be assessed “member surcharges”? Regulatory Notice 17-42 does not address this.

Regulatory Notice 17-42 should not be approved without further clarification and guidance to member firms and associated persons on these important issues.

**4. Regulatory Notice 17-42 proposes that a three-person panel of arbitrators must unanimously agree that expungement is appropriate. (Regulatory Notice 17-42, I.A.3 and II.B.)**

Imposing a unanimity requirement on expungement decisions is unfair to associated persons and effectively imposes a higher burden of proof (unanimity) on associated persons than on customers in the same case (where a majority of arbitrators may decide the merits of a claim). Under Rule 12410, all rulings and determinations of the panel concerning customer disputes are to be made “by a majority of the arbitrators . . .” Rule 13414 pertaining to industry disputes is identical. There exists no reasonable basis for treating an associated person’s expungement request materially differently from a decision on the merits of the underlying customer complaint. The same rules that apply to a determination of the merits of a customer case should apply to determining whether expungement relief is warranted under Rule 2080. We urge FINRA to reject this proposed component of Regulatory Notice 17-42.

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**5. Regulatory Notice 17-42 proposes that in order to grant expungement relief, the arbitrators must (1) identify at least one of the Rule 2080(b)(1) grounds for expungement that serves as the basis for expungement and (2) find that the customer dispute information has no investor protection or regulatory value. (Regulatory Notice 17-42, I.A.3 and II.B.)**

This is a material change to Rule 2080 that serves only to unnecessarily complicate and confuse the expungement process to the detriment of associated persons with no corresponding investor protection value. Current FINRA Rule 2080 sets forth the circumstances under which expungement of customer complaint information from an associated person's CRD record would be appropriate. Expungement relief is appropriate under Rule 2080(b)(1) where the arbitrators find that:

- (A) the claim, allegation or information is factually impossible or clearly erroneous;
- (B) the registered person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation or conversion of funds; or
- (C) the claim, allegation or information is false.

If the expungement relief is based on judicial or arbitral findings other than those described above, expungement relief can be granted under Rule 2080(b)(2) where the arbitrators conclude that:

- (A) the expungement relief and accompanying findings on which it is based are meritorious; and
- (B) the expungement would have no material adverse effect on investor protection, the integrity of the CRD system or regulatory requirements.

Regulatory Notice 17-42 proposes to remove the arbitrators' ability to grant expungement relief based on judicial or arbitral findings "other than" those listed in Rule 2080(b)(1). We urge FINRA to reject this component of the proposal. Customer disputes arise in a myriad of ways and under countless circumstances. Arbitrators must be empowered to restore balance and the status quo of an untarnished professional reputation in circumstances where they determine such relief is warranted under the alternate grounds identified in Rule 2080(b)(2).

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Regulatory Notice 17-42 also proposes to treat Rule 2080(b)(2) as an *additional* requirement for expungement relief instead of as an *alternate* basis for expungement relief. This additional burden is not justified and simply will confuse the proceedings. For instance, if the arbitrators find that a claim is “factually impossible,” “clearly erroneous,” “false,” or that the registered representative was “not involved in the alleged investment-related sales practice violation” (under Rule 2080(b)(1)), the claim by definition has no investor protection value. What “investor protection” interest could be served by the continued reporting of a false, factually impossible, or clearly erroneous claim? The requirements of Rule 2080(b)(2) are already satisfied by definition when any of the grounds of Rule 2080(b)(1) has been established. There is plainly nothing more for the arbitrators determine, and FINRA should not suggest that arbitrators must make additional findings as a prerequisite to granting expungement relief.

**6. Regulatory Notice 17-42 discusses expungement relief in the context of two possible resolutions to customer cases: closing by award and closing by “other than award” (e.g., the parties settle the arbitration). (Regulatory Notice 17-42, I.A.3 and I.A.4.)**

Regulatory Notice 17-42 proposes that, if the case is resolved by an award, the arbitrators must consider and decide the expungement request during the Underlying Customer Case. If the case closes “other than by award” (such as by settlement), Regulatory Notice 17-42 proposes that the panel in the Underlying Customer Case would not decide the associated person’s expungement request. In that situation, the associated person would be permitted to file the expungement request as a new claim under the Industry Code against the firm at which he or she was associated at the time of the events giving rise to the customer dispute. (Regulatory Notice 17-42, I.A.3 and I.A.4.) This component of Regulatory Notice 17-42 raises but does not address the following important issues:

If a case closes as a result of an order dismissing the case under Rule 12206 or Rule 12504, will the request for expungement relief be determined by the same arbitrators who ruled on the motion in the Underlying Customer Case? What if the motion to dismiss is granted *before* the associated person has made a request for expungement? Will the associated person have the right to seek expungement relief before the same arbitrators who determined the Underlying Customer Case?

If a case closes by settlement, Regulatory Notice 17-42 proposes that the panel in the Underlying Customer Case would *not* decide the associated person’s expungement request. In that situation, the associated person would be permitted

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to file the expungement request as a new claim under the Industry Code against the firm at which he or she was associated at the time of the events giving rise to the customer dispute. If the settlement occurs late in the case (perhaps even after the commencement of or during the presentation of evidence in the merits hearing), does the associated person have the right to request that the panel in the Underlying Customer Case continue to serve, for the purpose of resolving the related request for expungement relief? Clearly at that point the arbitrators would be familiar with the issues and at least some of the evidence; it would seem to be a waste of time, effort and resources to require the associated person to initiate a *new* request for expungement relief before a *new* panel of arbitrators under the Industry Code. Further, if the associated person has already paid the filing fee for expungement contemplated by Regulatory Notice 17-42 in the Underlying Customer Case, will the associated person be required pay *another* filing fee upon the filing of a new expungement request under the Industry Code?

If FINRA wishes to pursue possible modifications to the expungement rules and procedures, we urge FINRA to reject the Regulatory Notice 17-42 in its current form and to consider these issues and ramifications before recommending any proposed rule changes.

**7. Regulatory Notice 17-42 proposes a one-year limitation on an associated person's right to request expungement of customer dispute information where the dispute did not result in an arbitration claim. (Regulatory Notice 17-42, I.A.5.)**

Regulatory Notice 17-42 proposes that an associated person seeking expungement of a customer complaint that does not result in an arbitration claim be required to file a request for expungement relief "within one year of the date that a member firm initially reported a customer complaint to CRD." In our opinion, the one-year period is unreasonably short and unfair for at least the following reasons.

First, a one-year eligibility requirement on expungement requests is inconsistent with other provisions of the FINRA Rules. For example, Rule 12206 allows customers to file an arbitration claim within six years after the occurrence or event giving rise to the claim. Regulatory Notice 17-42 fails to justify the disparity in allowing customers six years to bring a claim while restricting associated persons to just one year to seek expungement relief.

Second, Regulatory Notice 17-42 proposes that, if the customer complaint did not result in an arbitration, the one-year limitation on an expungement request would begin to run from the date that a member firm initially reported the

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customer complaint to CRD. Due to the six-year eligibility period for customer complaints under Rule 12206, this will lead to inequitable and inconsistent results. It is entirely possible, for instance, that a customer might submit a complaint to a firm (resulting in the complaint being reported on the associated person's CRD and BrokerCheck) but allow the complaint to remain dormant, without initiating an arbitration claim, for a period of three, four or five years. If, in the fifth year, the customer initiates an arbitration claim, the customer's claim may be eligible for arbitration under Rule 12206 but the associated person's request to expunge that very same claim would be time-barred. That is an inequitable result that should be avoided.

Third, instead of decreasing expungement requests, the proposed one-year limitation on expungement relief claims likely would increase the frequency of those requests. Under the proposal in Regulatory Notice 17-42, an associated person would be obligated to seek expungement relief within one year of the date a customer complaint is first reported on the associated person's CRD. An associated person could timely initiate and obtain expungement relief, only to find that three, four or five years later the customer initiates an arbitration based on the complaint that was previously expunged. Assuming that the customer's initiation of the dispute in arbitration would be reported anew on the associated person's CRD, the associated person would be required to initiate a second request for expungement relief of the same complaint that had been expunged years earlier. This obviously results in an undue burden on associated persons and member firms, as well as an undue consumption of arbitral (and, in some instances, judicial) resources.

In our opinion, if FINRA ultimately imposes an eligibility period on expungement relief, the period should be six years (the same period of time as the eligibility for customer complaints under Rule 12206), and the six-year period should commence one year after the member firm's filing of the "closing event" Form U4 or Form U5 amendment and Disclosure Reporting Page (reporting the resolution of the claim). Further, similar to Rule 12206(b), if the arbitrators in a FINRA arbitration determine that the associated person's request for expungement relief is ineligible for arbitration because it was initiated more than six years after the "closing event" on the associated person's Form U4 or Form U5 (and correlating CRD), the associated person should have the right to withdraw the request for expungement relief from arbitration, without prejudice, and pursue expungement relief in court.

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**8. Regulatory Notice 17-42 proposes eliminating the ability of unnamed associated persons to intervene in the Underlying Customer Case for the purpose of seeking expungement relief. (Regulatory Notice 17-42, I.B.2.)**

This component of Regulatory Notice 17-42 is unnecessary. Customers frequently name member firms as the respondent in arbitration but avoid naming the individual associated person who is accused of various sales practice violations. Regardless of whether the associated person is named as a respondent, the claim may nevertheless be one that requires reporting on the associated person's CRD. In that instance, the associated person may have an interest in intervening in the Underlying Customer Case for the purpose of seeking expungement relief. This approach often can be economical, given that the evidence on the merits (or lack thereof) of the customer's complaint will be presented at the evidentiary hearing and that same evidence will provide the basis for expungement relief. Regulatory Notice 17-42 does not explain the reason for eliminating the rights of unnamed associated persons in this circumstance. We urge FINRA to reject this component of the proposal.

**9. Regulatory Notice 17-42 proposes requiring associated persons seeking expungement relief to appear in person or by videoconference, rather than by telephone. (Regulatory Notice 17-42, II.A.)**

Again, this proposal reflects a disparity in FINRA's treatment of customers who seek awards of money damages and associated persons who seek expungement relief. No rule requires customers seeking monetary awards to appear in person or by video conference in order to initiate or pursue a claim. Arbitrators frequently allow customers and other witnesses to appear by telephone. In certain circumstances, an associated person's appearance by telephone in an expungement relief proceeding is both efficient and appropriate. The associated person is available and can answer questions from the arbitrators, if necessary. Associated persons should not be subject to more stringent burdens on their requests for expungement relief than customers have in their requests for damages.

**10. Regulatory Notice 17-42 proposes a special "Expungement Arbitrator Roster" for use in cases where the expungement relief is not decided as part of the "Underlying Customer Case." (Regulatory Notice 17-42, III.A.)**

We commend FINRA for providing expungement training to its arbitrators, but we find at least three shortcomings with the proposed "Expungement Arbitrator Roster" process and suggest that it should be rejected.

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First, Regulatory Notice 17-42 provides that in cases where expungement relief is not sought as part of the Underlying Customer Case, FINRA will randomly select three public chairpersons to decide an expungement request. This appears to suggest that three — and only three — arbitrators will be imposed on the associated person, meaning that the associated person would not have the right to strike or rank proposed arbitrators for the expungement relief hearing. Again, this imposes an unfair restriction on associated persons, and is a restriction that is absent from customer dispute cases. We suggest that FINRA randomly select a minimum of 12 proposed arbitrators to serve on an expungement relief case, from which the associated person and anyone else involved in the case can rank and strike the proposed panelists.

Second, Regulatory Notice 17-42 proposes a specialized “Expungement Arbitrator Roster.” To be included on the “Expungement Arbitrator Roster,” an arbitrator must be admitted to practice law in at least one jurisdiction and have at least five years’ experience in “litigation” (not necessarily securities litigation). The “Expungement Arbitrator Roster” does not include non-lawyers who have five or more years’ experience in the securities industry. We believe that non-lawyers who have five or more years’ experience in the securities industry bring valuable experience and practical perspective to securities arbitrations. FINRA shares this belief, which is why it permits non-lawyers with five or more years’ experience in the securities industry to serve as arbitrators in the resolution of customer disputes. We believe that the qualifications of arbitrators in expungement relief cases should mirror the qualifications of arbitrators in customer dispute cases.

Third, as noted above, non-lawyers who have five or more years’ experience in the securities industry are permitted to serve as arbitrators in customer disputes. Therefore, it is likely that in cases where the request for expungement relief is sought as part of the Underlying Customer Case, the associated person’s request for expungement relief may be decided by a panel that includes a non-lawyer arbitrator; but in cases where the request for expungement is not decided as part of an Underlying Customer Case, non-lawyer arbitrators would not be eligible to participate. FINRA obviously believes that non-lawyer arbitrators are capable of “understanding the unique nature of a request for expungement,” because FINRA permits non-lawyer arbitrators to decide expungement requests in the context of Underlying Customer Complaints. These same non-lawyer arbitrators should be permitted to serve on arbitration panels where expungement is the only relief sought. There is no rational basis to create a two-tiered system for the resolution of requests for expungement relief depending

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on whether the requests are part of an Underlying Customer Complaint or brought as a stand-alone claim.

**11. Regulatory Notice 17-42 proposes use of the “Expungement Arbitrator Roster” in simplified cases. (Regulatory Notice 17-42 IV.)**

Regulatory Notice 17-42 proposes that an associated person would not be permitted to request expungement relief as part of the Underlying Customer Case in “simplified arbitrations” (typically arbitrations involving \$50,000 or less, which are resolved by a single appointed arbitrator). Instead, under the proposal, the associated person would be required to file an expungement request under the Industry Code against the firm at which he or she was associated at the time of the events giving rise to the customer dispute, and only at the conclusion of the simplified case. Regulatory Notice 17-42 proposes that a three-member panel from the “Expungement Arbitrator Roster” would consider and decide the expungement request.

For the reasons discussed at item 10 above, we urge FINRA to reject the proposed “Expungement Arbitrator Roster.” In addition, we believe that the arbitrator who is most qualified to determine a request for expungement relief in any particular case is the same arbitrator who heard and considered the evidence and merits (or lack thereof) of the underlying customer case which is the basis for the request for expungement. If that evidence has been reviewed and considered by a single arbitrator pursuant to the simplified arbitration rules, then that arbitrator, acting alone, should likewise have the authority to determine the associated person’s correlating request to expunge information about that complaint from his or her CRD. It is unfair to impose the burden of a second arbitration and its attendant added expense, delay and effort on the associated person in this circumstance. Further, requiring the associated person to initiate a new arbitration for expungement relief under the Industry Code (rather than seek expungement relief as part of the Underlying Customer Case in the simplified arbitration) risks inconsistent results between the two proceedings. FINRA should simplify the process, not make it more complicated.

**12. Additional comment regarding Regulatory Notice 17-42 and Expungements.**

In addition to the foregoing comments, we urge FINRA to consider the following:

a. Guidance to Associated Persons Regarding Registration Requirements and Expunged Claims. We request that FINRA provide clarity and

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guidance to associated persons and registration personnel regarding the meaning and effect of an expunged claim in the context of licensing and registration questionnaires.

For instance, the Uniform Application for Securities Industry Registration or Transfer (Form U4 (Rev. 5/2009)) asks applicants a number of questions regarding whether they have ever been named as a respondent in or the subject of an *investment-related*, consumer-initiated arbitration or civil litigation which alleged that the associated person was *involved* in one or more *sales practice violations* and the resolution of those claims. (See Form U4 Questions 14.I(1)-(5).) Must applicants answer “Yes” to these questions if the customer claim asserted against them has been determined to be “false,” or “factually impossible,” or a panel of arbitrators or court determined that the associated person was “not involved” in the alleged conduct, and therefore the complaint has been duly expunged from the associated person’s CRD record? The instructions for completing the Form U4 do not answer this question, and we have found no guidance from FINRA on this issue.

We urge FINRA to expressly inform associated persons that they may confidently answer these questions “No” with respect to claims that have been expunged from their records.

b. Explicitly Recognizing Orders From Other Arbitration Forums For Expungement Relief.

In an effort to provide public customers with a choice of alternative dispute resolution forums, member firms frequently allow public customers to elect arbitration before FINRA, the American Arbitration Association, and other providers. If a public customer elects arbitration before an arbitration forum other than FINRA, the arbitral findings should be recognized and afforded the same weight as arbitral findings of arbitrators in a FINRA-administered arbitration, provided that (1) the arbitrators make written, factual findings as the basis for expungement under Rule 2080, and (2) the requirements of Rule 12805 are satisfied. Arbitrators in these alternate forums are qualified to determine whether, after a recorded hearing, the evidence supports a finding that a claim is “factually impossible or clearly erroneous,” or that the associated person was “not involved” in the alleged wrongdoing, or that the claim is “false,” or that a claim for expungement is meritorious and expungement would have no material adverse effect on investor protection.

Ms. Marcia E. Asquith  
February 1, 2018  
Page 14

Re: Comments regarding FINRA Regulatory Notice 17-42 (12/6/2017)

Currently, FINRA Rules 2080 and 12805 refer to "arbitration awards seeking expungement relief" and "confirming an arbitration award containing expungement relief" without specifying that the Award must be a FINRA Award. FINRA states that it will accept expungement orders issued by a court of competent jurisdiction (without an underlying arbitration award). We suggest that FINRA explicitly state that orders from other respected arbitral tribunals, validated by judicial confirmation, will be accorded comity. By doing so, FINRA will encourage member firms to continue providing public customers with their choice of arbitration forum (not restricting that choice to FINRA, simply because it is the only arbitration forum in which expungement relief can be obtained), and FINRA likewise will encourage associated persons to seek expungement relief as part of the "Underlying Customer Case" where the arbitrators will be familiar with the evidence from that proceeding.

### **Conclusion**

As securities attorneys, we value FINRA's desire to provide a fair, neutral, and transparent forum for public investors; however, the rights and interests of associated persons must not be trampled in the process. To reiterate, we agree that misconduct by associated persons towards investors should not be swept under the rug. However, the mechanism for expunging false, defamatory or factually impossible claims from honest associated persons' records should not be made so onerous that it hurts the very associated persons who share FINRA's concern for helping the investing public. Thank you for FINRA's continued recognition that associated persons have an interest in protecting their professional reputations from false or mistaken claims through the expungement process, and for the opportunity to comment on the proposals in Regulatory Notice 17-42.

For the reasons set forth above, we urge FINRA's Board of Governors to reject the proposal in Regulatory Notice 17-42 with the few exceptions noted herein and work towards drafting proposed rules concerning expungement with the goal of fairness and expediency in mind for all participants in the FINRA arbitral process.

Very truly yours,



Stacey M. Garrett  
stacey.garrett@kyl.com

I wish to state my firm opposition to the rule changes that FINRA is proposing. I have been subject to two frivolous claims in thirty-five years. One complaint was submitted by a woman who in fact had me mistaken for someone else! This was absolutely ludicrous, yet it was attached to my record. Now, FINRA proposes to remake the rule governing expungements of frivolous claims to make them permanent if not expunged within 12 months; this absurdity is so manifest that it actually -- and ironically -- reduces FINRA's standing as a regulator. Cicero said: 'True law is right reason in agreement with nature.' There is nothing that can claim either reason or natural agreement in these proposed changes. They would be laughable if only they had no impact on the livelihood of people who have families to support.

E. A. Glenn

Edward A. Glenn  
Portfolio Manager Director  
Senior Vice President  
Morgan Stanley Wealth Management  
888.213.0415  
[edward.a.glenn@morganstanley.com](mailto:edward.a.glenn@morganstanley.com)

For information on current economic or market topics, visit our web-site:

[www.morganstanleyfa.com/glenn\\_burns/](http://www.morganstanleyfa.com/glenn_burns/)

For information on any company mentioned herein a report is available

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Dear FINRA Office of Dispute Resolution:

Being a longtime FINRA arbitrator and upon receiving today the December, 2017 FINRA Dispute Resolution Update, I noticed in it a call for comments on proposed expungement rule changes, detailed in FIRNA Regulatory Notice 17-42. Having served recently on several expungement matters and scheduled to participate in more in 2018, I wanted to offer my related comments to address the 12 specific areas for which guidance is sought on pp. 17-18 of the notice. My comments are provided in the attached Word file.

One thing I would say here, assuming you adopt the requirement that only licensed and highly experienced attorneys as qualified for any new expungement panels, as a non-attorney I would thus automatically be rejected as qualified and would find that highly discriminatory. It is bad enough that you have arranged the system to exclude any non-attorneys from serving as mediators, regardless of their talents or capabilities for performing in such a capacity. Now apparently someone is proposing the same for expungement, which beyond the certainty of adding to the complexity, cost, and the time required to arrive at an expungement decision, doesn't seem to offer any obvious advantage in contrast to making a less radical adjustment. I also think it would add to your difficulty in finding good non-attorney arbitrators, as it would serve as another example of an effectively second class status being assigned to them.

In any case, my impressions are offered for your further consideration, thank you.

Sincerely,

Gregory Gocek

*Request for Comment FINRA is interested in receiving comments on all aspects of the proposed amendments. In particular, FINRA seeks comment on the following questions:*

1. FINRA Rules 12805 and 13805 provide, in relevant part that, in order to grant expungement of customer dispute information under Rule 2080, the panel must comply with the requirements stated in the rule. (Emphasis added.) FINRA notes, however, that if a panel issues an arbitration award containing expungement relief, the award must be confirmed by a court of competent jurisdiction and FINRA could decide to oppose the confirmation. Thus, as the associated person is required to complete additional steps after the arbitrators make their finding in the award before FINRA will expunge the customer dispute information, FINRA believes the word “grant” may not be an appropriate description of the panel’s authority in the expungement process. FINRA is considering changing the word to “recommend.” Please discuss whether the rule should retain “grant” or change to “recommend” or some other description to more accurately reflect the panel’s authority in the expungement process.

*Agree that given mandated court approval, panels are not the ultimate authority on the outcome of the expungement request and therefore are not “granting” such. “Recommend” or “agree with the associated person” seems more appropriate.*

2. Would named associated persons request expungement in every case to preserve the right to have the expungement claim heard and decided, either in the Underlying Customer Case or as a new claim under the Industry Code? If so, what would be the potential costs and benefits of a named person requesting expungement in every case?

*The amendments will introduce a definite incentive to brokers to routinely include expungement requests in customer cases. This will increase the complexity and time of those proceedings, but if the claims were resolved there it would be much less burdensome to FINRA’s administrative capabilities than creating a basically entirely new parallel set of proceedings outside the customer claims.*

3. Should FINRA consider bifurcating the expungement request from the customer’s claim in all cases relating to customer disputes? What would be the costs and benefits of such an approach?

*Anyone with experience in FINRA arbitration would likely recognize this would be ill advised. FINRA staff resources are quite stretched already and adding a separate series of disputes would just make things more problematic for the arbitrators responsible for hearing these claims. This would introduce new scheduling complications and it would of course be impossible to rule on expungement before the underlying customer claim was resolved.*

4. What are the costs and benefits of requiring the unanimous consent of a three-person panel to grant all requests for expungement of customer dispute information?

*It seems most appropriate to have a uniform decision standard for both the customer claim and the subsidiary expungement request. So if unanimous consent is required for one, it is unclear what the rationale would be for a simple majority in the other. If there is a non-public arbitrator in an expungement proceeding, is there a concern that such person will be a hold-out in favor of expungement, making it easier to grant by only requiring one of the public arbitrator’s assent as opposed to requiring approval from both of the public arbitrators? The why not have only public arbitrators hearing expungement requests and then requiring a simple majority for the approval? Unanimity will definitely create a greater burden on brokers seeking expungement,*

5. Is the one-year limitation on being able to request expungement of customer dispute information appropriate? Should the time period be longer or shorter? Please discuss. Regulatory Notice 17 December 6, 2017 17-42

*Agree, if the customers have to satisfy a timeliness standard, it seems fully appropriate to accept the same of brokers for such requests. 1 year seems right, it would seem best to have the requests included as part of the defense to the original proceeding as opposed to having the possibility for a long deferral open to the broker. This would still make it fairly easy for customers to participate if they so wished.*

6. Should the associated person who is requesting expungement be required to appear in person or by videoconference, rather than by phone, at the expungement hearing?

*No, phone calls seem to be fine from the number of expungement requests I've ruled on recently, having separate in person hearings for this would be a real administrative burden and likely delay scheduling, make people incur extra travel expenses, etc.*

7. Should the arbitrators on the Expungement Arbitrator Roster have specific qualifications? If so, are the proposed additional qualifications appropriate or should FINRA consider other qualifications?

*Requiring some extra FINRA training seems OK, but mandating that persons granting expungement all have to be lawyers with extensive trial and regulatory experience seems excessive, sort of like a lawyer protection act to ensure they can get extra work like the entire parallel mediation system to arbitration is currently arranged. If a panel can decide on expungement related to a connected customer case, and not all of them need to be attorneys without such extensive qualifications, will that mean that everyone will then seek expungement at such hearings because they think it will be more likely granted then? Or the fact that a panel did grant an expungement at the customer case level without these extra qualifications, would that make the expungement any less acceptable? Maybe require the arbitrators to have some experience at FINRA, say five years, before qualifying to serve on expungement panels, in addition to the training, seems more than sufficient to me.*

8. Should the arbitrators on the Expungement Arbitrator Roster be lawyers only or could the experience of serving on three arbitrations through award be a sufficient substitute?

*As noted above, having lawyers only seems discriminatory to me and certainly serving on multiple arbitrations panels is more than enough to qualify to be a discerning evaluator of the requests. Further, if three persons will be serving on a panel, that should be enough to cover any potential limitations of one the panelists.*

9. How would the proposed amendments affect the granting or denying of expungement requests? Which aspect of the proposed amendments would have the largest impact on expungement determinations? Why?

*This would likely make expungement requests more challenging to get, as common sense dictates that if great rigor is infused in the process, this will impose greater hurdles- demand curves still are downward sloping, with a higher price indicating less demanded. Adding a lawyer only, three member panel requirement would likely result in longer deliberations and also most probably draw out the proceedings. I've had several occasions recently when lawyer panelists either had more difficulties with their*

*calendars, or wanted to have more extensive consultation with the other panelists, before moving to a decision, and I didn't experience such as positive for the process.*

10. The proposal would establish a one-year limitation period for associated persons to expunge customer dispute information that arose from a customer complaint. The limitation period would start on the date that the member firm initially reported the customer complaint to CRD. Should the one-year limitation period be based on a different milestone? If so, what should it be?

*It seem unfair to require one year from a filing date of a case, this could a negotiating advantage to the customer by putting up delays to the proceeding in order to deny expungement for a more favorable settlement. If also would not make it easier for arbitrators to intervene as referees on scheduling disputes. What if one of the arbitrators is a source of delay in coming to a final ruling? One year seems appropriate, but the clock should start running from when the underlying customer dispute is ruled upon or settled, not from when the claim is first reported or filed.*

11. The proposal would clarify for arbitrators that the standard for granting the permanent removal of customer dispute information from CRD is a finding that at least one of the Rule 2080(b)(1) factors applies and that the customer dispute information has "no investor protection or regulatory value." Are there specific factors that arbitrators should consider when making a finding that the customer dispute information has "no investor protection or regulatory value"?

*Because each case is being judged on its individual merits, and the arbitrators are not qualified as experts on broader systemic concerns or regulatory standards, I don't think there should be great specificity as to this last clause. It can be retained as guidance and an additional check that an expungement would not be considered as some special benefit available to a broker as long as they make some acceptable demonstration that it is appropriate. But why introduce a new potential point of debate as to what constitutes ideal investor protections or regulatory control? These standards are evolving and putting more explicit requirements in would simply guarantee that the written guidelines are more likely to be out of date with FINRA playing catch up, as regulators often do.*

12. In a simplified arbitration case, if a customer requests a hearing, should the single arbitrator be permitted to decide an expungement request, if a request is filed?

*Definitely, adding a three member panel, particularly if they were all required to be lawyers and a whole separate layer of proceedings for expungement, would be totally contrary to the intent of simplified proceedings. Allow one arbitrator to also decide that, and don't impose the excessive qualifications of a licensed attorney with extensive litigation experience, to do so. The whole point of arbitration is to get at the equity of the underlying dispute as efficiently as possible, not to create an adjudicatory system comparable to what parties are exposed to when they have to go to court in the traditional legal system.*

**TO:** FINRA, Office of the Corporate Secretary

**FROM:** Tosh Grebenik, Chief In-House Counsel, FA Expungement, LLC

**DATE:** January 29, 2018

**SUBJECT:** Response to Regulatory Notice 17-42

To Whom It May Concern,

I am writing to express my concerns regarding this proposed rule change. There are multiple issues with this proposed rule change, I will attempt to explain my concern below.

1) 12805(a)(1) states: “If the associated person does not request expungement in the investment-related, customer-initiated arbitration, the associated person shall be prohibited from seeking to expunge the customer dispute information arising from the customer’s statement of claim during any subsequent proceeding.”

a. There are multiple issues with this language. First, one of the reasons that a financial advisor does not request expungement in the initial hearing is because that arbitrator may have bias. The arbitrator has heard comments and issues from the customer for the actual claim. The expungement aspect is separate and should be evaluated from an entirely independent panel.

2) 13800(a)(f): There is a grammatical error under subsection f that should read “at the conclusion of the case” instead of “at the conclusion of the a case.”

3) Under 13805(a)(3)(D) and (E), these are extremely limiting. There are thousands of advisors who have customer disputes and do not know about the expungement process. This time limit should be removed. There are advisors who have never been told that expungement is an option and this will make is to that FINRA’s intent - only show disclosures that have no investor protection or regulatory value – will be nearly impossible to achieve.

There are lots of customer disputes relating to market-driven failures like Auction Rate Securities, Real Estate Investment Trusts (around 2008), and Puerto Rico bonds. These disputes, which were vastly outside of the advisor’s control, do not have any investor protection or regulatory value. As a result, they will be forced to keep and maintain these old, irrelevant disclosures due to this rule.

Customer disputes are the single most common disclosure for advisors. This rule will remove the possibility of getting a more accurate BrokerCheck and CRD system for a large number of disclosures.

4) 13805(c)(2) states that the advisor must appear in person for the expungement hearing. This is going to limit the value of the process and increase costs. As it stands now, arbitrators can be selected from across the country and these arbitrators can be selected solely upon their resumes. If this rule going into effect, either FINRA will have the added expense of flying the arbitrators around the country for hearings or the arbitrators will have to be selected from a pool geographically located together. In addition, the advisor (and his/her counsel) may need to



travel to the location as an added expense for expungement. This acts as a disincentive and indirect tax on the process.

Respectfully,

*Tosh Grebenik*

Tosh Grebenik, JD  
Chief In-House Counsel  
[FA Expungement, LLC](#)  
3000 Lawrence St. #119  
Denver, CO 80205  
O: (720) 619-7117  
C: (303) 523-4022  
F: (888) 923-8585

There needs to be a fair system to remove meritless claims against brokers, especially in the case of 'one off' customer complaints. Maintain the 'majority' decision by an arbitration panel, matching the 'majority' decision in the customer complaint. While there needs to be a 'highest' standard of broker behavior, there are circumstantial events beyond a broker's control, that can lead to disclosures, which follow brokers through customer reviews, job interviews and opportunities throughout a career.

Respectfully submitted,

Jonathan Hagenstein



215 Pennsylvania Avenue, SE • Washington, D.C. 20003 • 202/546-4996 • [www.citizen.org](http://www.citizen.org)

February 5, 2018

Marcia E. Asquith  
Office of the Corporate Secretary  
Financial Industry Regulatory Authority  
1735 K Street, NW  
Washington, DC 20006-1506  
*Via email to: [pubcom@finra.org](mailto:pubcom@finra.org)*

**Re: Regulatory Notice 17-42, Expungement of Customer Dispute Information**

Dear Ms. Asquith:

On behalf of Public Citizen, a non-profit membership organization with more than 400,000 members and supporters nationwide, we write to thank the Financial Industry Regulatory Authority (FINRA) for proposing changes to its rules to better protect investors.<sup>1</sup> We welcome the opportunity to comment on this important notice.

**I. Overview**

Public Citizen strongly opposes the use of forced arbitration clauses, which use fine-print “take-it-or-leave it” agreements to deprive people of their day in court when they are harmed by violations of the law. Instead, these agreements force people into secretive arbitration proceedings with no right to appeal if arbitrators ignore the facts or law. When forced arbitration clauses are combined with class action bans, neither judges nor arbitrators can assess or remedy the full scope of systemic wrongdoing that affects multiple victims. FINRA’s funding source from the very industry that it regulates results in the potential for public perception of bias. Therefore, expungements should be rare, if not altogether prohibited.<sup>2</sup> Thus, our suggested

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<sup>1</sup> *Regulatory Notice 17-42 Expungement of Customer Dispute Information* FINANCIAL INDUSTRY REGULATORY AUTHORITY. (viewed on February 5, 2018).

<sup>2</sup> Susan Antilla, *The Unbelievable Story of One Broker and Her Firm Fighting to Clean Her Tarnished Record*, THE STREET (June 21, 2016), <https://www.thestreet.com/story/13613109/1/the-unbelievable-story-of-one-broker-and-her-firm-fighting-to-clean-her-tarnished-record.html>.

improvements to strengthen the proposal should in no way suggest that we agree with the use of forced arbitration or with the use of expungement of customer dispute information.

## **II. Support for Stronger Standard for Expunging Customer Dispute Information**

Access to accurate information through the Central Registration Depository (CRD) is critical because of the public's limited access to information about FINRA's oversight of its arbitration program.<sup>3</sup> As investor consumer advocate, Public Citizen supports FINRA's BrokerCheck and other public disclosures that help investors make an informed choice about investment advisors. A reliable database is critical for investor confidence, especially in light of a self-policing industry that suffers from a negative public reputation.<sup>4</sup> As such, the issue of expungements must be addressed with care.

FINRA notes that its "long-held position [is] that expungement of customer dispute information is an extraordinary measure."<sup>5</sup> We agree that expunging customer dispute information should be rare, if not disallowed, since access to information about previous disputes is a critical factor that investors weigh when deciding on an investment firm.

Overuse of expungement would not only limit critical transparency, it would decrease the CRD's utility as a reliable tool for investors. The proposed amendments would, among other things, increase the bar for expungement by requiring the associated person who is seeking an expungement to appear at the expungement hearing, place a one-year limitation period on the ability to request an expungement, mandate that a three-person panel of arbitrators unanimously agree that expungement is appropriate, and specify a minimum filing fee for expungement requests.

We agree with these limits to potential overuse of expungement proceedings as they raise the already high bar that is set by FINRA for granting expungements.<sup>6</sup> Moreover, new provisions aimed at providing opportunities for the original customer who filed the complaint at issue to participate in a request for expungement will help make the process less likely to be one-sided. Therefore, we believe that these proposed amendments will better protect investors, insure greater confidence in the process, and foster transparency. Though these amendments would provide an improvement to the status quo, we urge FINRA to strengthen the proposed amendments in several important ways.

<sup>3</sup> See, e.g., *Public Investors Arbitration Bar Ass'n v. SEC*, 930 F. Supp. 2d 55 (D.D.C. 2013).

<sup>4</sup> Emily Ekins, *Wall Street vs. The Regulators*, CATO INSTITUTE (February 5, 2015), <https://www.cato.org/survey-reports/wall-street-vs-regulators-public-attitudes-banks-financial-regulation-consumer/>.

<sup>5</sup> *Regulatory Notice 17-42 Expungement of Customer Dispute Information* FINANCIAL INDUSTRY REGULATORY AUTHORITY, [https://www.finra.org/sites/default/files/notice\\_doc\\_file\\_ref/Regulatory-Notice-17-42.pdf#page=3](https://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-17-42.pdf#page=3) (viewed February 5, 2018).

<sup>6</sup> See generally FINRA rule 2080, [http://finra.complinet.com/en/display/display.html?rbid=2403&element\\_id=8468](http://finra.complinet.com/en/display/display.html?rbid=2403&element_id=8468) (viewed February 5, 2018).

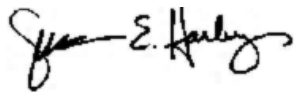
### **III. Suggested Changes to Strengthen Proposed Amendments**

The requirement that arbitrators write a brief explanation of expungement decisions should be strengthened to require those explanations to be made public in order to enhance transparency and public integrity in the system.<sup>7</sup> Moreover, we agree that arbitrators chosen to serve on the Expungement Arbitrator Roster should be randomly selected. To enhance public confidence in the arbitration system, at least one FINRA employee should be a member of every three-person panel that considers an expungement request. Any FINRA staff on a panel, however, should be required to meet the same qualifications as other expungement panel arbitrators.

While we appreciate that these proposed amendments will strengthen current FINRA rules, arbitration is only valuable when both parties willingly agree to arbitrate, after a dispute arises. Therefore, we will continue to advocate for commonsense legislation such as the Investor Choice Act of 2017 that prohibits forced arbitration in the securities market.

We welcome the opportunity to discuss these suggestions in greater detail.

Sincerely,



Susan Harley  
Deputy Director  
Public Citizen  
Congress Watch Division



Remington A. Gregg  
Counsel for Civil Justice and Consumer Rights  
Public Citizen  
Congress Watch Division

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<sup>7</sup> FINRA rule 12805, [http://finra.complinet.com/en/display/display\\_main.html?rbid=2403&element\\_id=7229](http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=7229) (viewed February 5, 2018).

Dear FINRA,

I am recommending that additional mechanisms be put in place to remove customer disputes, that have been investigated by the company and found to have no basis. I believe that all investigated consumer disputes, which have been investigated and found to have no basis, should not become part of the CRD record. As it currently stands they do become part of the CRD record in perpetuity, without any mechanism to remove them. Only customer disputes going to arbitration have any change of being expunged. What about consumer disputes that were found to have no basis and never made it to arbitration. Where is the fairness in the current system? Why should someone's reputation be tainted, when they were absolved from any wrong doing?

My name is Dave Harmon. My CRD number is 1505722. I have been registered with FINRA since July 1986. During that time, I have had only two customer disputes, both which were found to have no basis.

- 1) The first complaint was made on 10/30/10 and was related to service that I was provided to a client, on a variable life insurance policy that I didn't even sell. The client signed off on the proposed changes and made the complaint only after the company refused to reverse the changes made to his policy.
- 2) The second complaint was made on 12/11/14, and was related to incorrect annuity policy information, which was received from my service center and then communicated to the client.

Again, the proposed changes should contain some type of mechanism, which should allow for consumer disputes found to have no basis, to be removed from one's permanent CRD record.

Please feel free to contact me at 1-781-237-8336 with any additional questions that you may have.

Sincerely Yours,

David Harmon ChFC, CLU, MBA  
Financial Advisor  
AXA Advisors, LLC/Boston Branch  
93 Worcester St. Suite 103  
Wellesley, MA 02481  
1-781-237-8336 (Phone)  
1-508-341-1638 (Cell)  
1-781-237-8172 (Fax)

It's absolutely repulsive that you make the expungement process so one sided. Being in the securities industry for over 25 years I have seen many frivolous complaints, and for your regulatory organization to make the process so expensive and complex to have legitimate meritless cases that are sitting on the CRD is a joke. You are treating the very people that support your regulatory firm like criminals. Only in the securities business are you treated guilty until proven innocent. Shame on your organization for treating the financial professionals that way. You imposing these rules only benefit the attorneys. Find a way to penalize the rogue brokers, and not the broker that may have a rogue client post frivolous complaints on a hard working brokers CRD.

Hopefully this gets squashed.



January 6, 2018

**BY EMAIL: [pubcom@finra.org](mailto:pubcom@finra.org)**

Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

**Re: Regulatory Notice 17-42 – Public Comment**

Dear Ms. Asquith:

Thank you for the opportunity to comment on the proposed amendments to FINRA Rules 12805 and 13805.

Herskovits PLLC has an active practice representing broker-dealers and industry professionals in a variety of litigation and regulatory defense matters. As part of that practice, we frequently advocate for financial advisors (FAs) seeking expungement of frivolous customer complaints from CRD.

This comment letter addresses three areas of concern for us: (1) we question the appropriateness of imposing a one-year statute of repose for claims seeking expungement relief; (2) we question the appropriateness of requiring arbitrators to make a factual finding that the customer dispute information “has no investor protection or regulatory value” before awarding expungement; and (3) we question the appropriateness of the burdens placed on FAs under proposed Rule 12805(a)(1).

**Proposed Statute of Repose**

Proposed Rule 13805(a)(3) requires an FA to seek expungement no more than one-year after FINRA closed the underlying customer arbitration or, with respect to a disclosure that did not arise from an arbitration filing, no more than one-year after the customer complaint was reported to CRD. FINRA’s justification for this limitation period is to ensure that customers can be located and records concerning the underlying event still exist. *See* Regulatory Notice 17-42 at 5. There are many reasons to avoid the implementation of a one-year limitation period.

*First*, FINRA has no authority to impose any type of statute of limitation or statute of repose on any cause of action. That power rests with legislative bodies. Of course, FINRA can impose time limits on arbitration claims through eligibility rules and has done so with Rules

Marcia E. Asquith  
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12206 and 13206.<sup>1</sup> Yet, FINRA's existing eligibility rules expressly permit a party to file a claim in court if an arbitrator deems the claim to be outside the six-year eligibility period. In so doing, FINRA acknowledges that it can close its doors to a particular claimant, but not preclude that claimant from seeking relief in court.

*Second*, FINRA's justification for imposing a time limitation is one-sided and unfair. FA's, as well, want access to witnesses and documents when defending a customer-initiated arbitration. Yet, FINRA has never demanded that customers file an arbitration claim within one-year of the event giving rise to the claim.

*Third*, FINRA's concern about document retention seems misplaced. All broker-dealers are required to abide by document retention rules imposed by the SEC and FINRA, which generally mandate the preservation of most records for 3 to 6 years (and many firms preserve documents for longer periods of time). *See generally* 17 CFR § 240.17a-4 and FINRA Rule 4511.

### **Proposed Finding of Fact by the Arbitrator**

Proposed Rule 12805(b)(3) would require an arbitrator to make to make 2 findings of fact when ordering expungement. First, the arbitrator would be required to identify at least one ground for expungement under Rule 2080(b)(1) and, secondly, and more troublingly, the arbitrator would be required to find "that the customer dispute information has no investor protection or regulatory value."

Rule 2080(b)(1) permits expungement awards based on arbitral findings that:

- The claim, allegation or information is factually impossible or clearly erroneous;
- The registered person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation or conversion of funds; or
- The claim, allegation or information is false.

The obvious question is this: if an arbitrator makes the requisite findings under Rule 2080(b)(1), what possible "investor protection" or "regulatory value" needs are served by preserving a debunked claim on CRD? Incredibly, under the proposed rule, an arbitrator could find the customer claim to be "factually impossible," and yet still refrain from awarding expungement.

Additionally, we are concerned by the vagueness and ambiguity of the proposed requirement that an arbitrator find "that the customer dispute information has no investor protection or regulatory value." Where is an arbitrator supposed to draw the line under such a vague standard? How is an arbitrator supposed to determine what type of information may be of

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<sup>1</sup> It is noteworthy that FINRA imposes no time limitation upon itself in connection with regulatory enforcement matters. In theory, FINRA's enforcement division can bring enforcement actions against any registered entity or person without regard to the passage of time.

Marcia E. Asquith  
January 6, 2018  
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“value” to a regulator? Wouldn’t such a vague standard leave open the possibility of wildly inconsistent rulings from one arbitration panel to the next? Furthermore, arbitrators are supposed to be neutrals and they should not be placed in the position of serving as an investor advocate or guardian of regulatory data. Those responsibilities fall squarely on regulators, not arbitrators.

**Proposed Rule 12805(a)(1) Places Unnecessary Burdens on FA’s**

Proposed Rule 12805(a)(1) would require an FA to initiate a new arbitration if the underlying customer arbitration “closes before the hearings on the merits concludes.” Any such rule would place an extraordinary and unnecessary burden on an FA. FINRA arbitrations are time consuming and expensive endeavors. According to data published by FINRA, the average turnaround time for a FINRA arbitration decision is 16.9 months. *See* <http://www.finra.org/arbitration-and-mediation/dispute-resolution-statistics>. Thus, under the proposed rule, an FA may wait more than a year for his “day in court,” only to be forced to wait another year if the broker-dealer resolved the claim with the customer on the eve of a hearing (when most settlements occur). Apart from a being waste of time and money, FAs will respond to the proposed rule by filing a counterclaim or crossclaim for expungement in the customer arbitration, thus preventing the customer arbitration from closing before a hearing is held on expungement or the FAs other claims for relief.

Proposed Rule 12805(a)(1)(A) is also troubling because it bars an FA from filing an expungement arbitration unless the FA requested expungement in the underlying customer arbitration. This requirement is disconcerting because an FA may be unaware of the important rights he is waiving by failing to file a request for arbitration in the underlying arbitration.

We hope FINRA gives consideration to these comments before proposing any rule amendments to the SEC.

Yours truly,

HERSKOVITS PLLC



Robert L. Herskovits

To whom it may concern,

I understand that you are considering changes to the expungement process financial advisors utilize to challenge disclosures on their record. I am writing you to ask that you not make these proposed changes. I have disclosures on my record related to funds offered by my employer, Morgan Keegan, which crashed during the 2007-2008 Financial Crisis. None of the clients named me in their complaints, which were driven by excessive advertising by plaintiff lawyers, and my employer elected to settle the cases for economic reasons rather than fight them, which would have kept them off of my record. If you make it more expensive, change the process from a majority decision to a unanimous decision, or remove any chance of expungement after 12 months, you are making it next to impossible for advisors like myself to be able to try and remove disclosures related to massive settlements like I experienced with Morgan Keegan.

Thank you for your consideration in this very important matter.

Sincerely,  
Jay Higgenbotham

**Jay R. Higgenbotham, CPWA®**  
Wealth Management Advisor  
Senior Vice President - Investments  
Merrill Lynch, Pierce, Fenner & Smith Incorporated  
569 Brookwood Village, Suite 501  
Birmingham, AL 35209  
205-326-9587 Direct  
844-588-3800 Toll Free  
205-383-2408 Fax  
NMLS ID 1277214  
[jay.higgenbotham@ml.com](mailto:jay.higgenbotham@ml.com)



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Yes,

I am in favor of having a fair system to remove meritless claims on our Broker Check. This should not have to be high cost/charge to an Financial Advisor at no fault of their own.

I am NOT in favor of rule 17-42.

Please re-consider.

Sincerely,

-Jim Isola



Cornell University  
Law School

Lawyers in the Best Sense

**WILLIAM A. JACOBSON**  
*Clinical Professor of Law*

154 Myron Taylor Hall  
Ithaca, New York 14853-4901  
T: 607.255.6293  
F: 607.255.3269  
E: waj24@cornell.edu

February 5, 2018

(Via E-mail: [pubcom@finra.org](mailto:pubcom@finra.org))

Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

**RE: Regulatory Notice 17-42 (Expungement of Consumer Dispute Information)**

Dear Ms. Asquith,

The Cornell Securities Law Clinic (the "Clinic") welcomes the opportunity to provide feedback on the request for comment (the "Request") of the Financial Industry Regulatory Authority ("FINRA") on Proposed Amendments to the Codes of Arbitration Procedure Relating to Requests to Expunge Customer Dispute Information ("CDI"). The Clinic is a Cornell Law School curricular offering, in which law students provide representation to public investors and public education as to investment fraud in the largely rural "Southern Tier" region of upstate New York. For more information, please see: <http://www.securities.lawschool.cornell.edu/>

FINRA operates the Central Registration Depository (CRD) in order to maintain consolidated records of the employment histories, qualifications, and disclosures of broker-dealers and registered individuals. Some of this information is publicly accessible through the BrokerCheck system. Through the BrokerCheck system, public investors can view a variety of employment and dispute information that enables them to make informed choices regarding financial advisers.

For the reasons set forth below, the Clinic supports several of the Proposed Amendments, including (1) the Expungement Arbitrator Roster; (2) the one-year limitation on requesting expungement of CDI under Proposed Rule 13805(a)(3)(D); (3) the unanimity requirement for granting expungement under Proposed Rule 13805(b)(3); (4) the heightened standard for granting expungement under Proposed Rule 13805(b)(3)(B); (5) the personal appearance requirement for an associated person requesting expungement under Proposed Rule 13805(c)(2); and (6) changing the word "grant" to "recommend" within the text of Rules 12805 and 13805.

However, the Clinic also strongly opposes the Rule Proposal's requirement that an associated person request expungement during the underlying customer case.



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Historically, there are numerous instances of associated persons abusing the expungement process, and that abuse has damaged a system designed to protect public investors. Five years before investors lost \$125 million in a Ponzi scheme allegedly run by Carl Matellaro, two investors claimed that they lost \$1.75 million with Matellaro's firm.<sup>1</sup> However, investors in the Ponzi Scheme could not have found out about the prior claims because they had been expunged from Matellaro's NASD record.<sup>2</sup> In 2013, an individual had a dispute expunged from her record, despite Wells Fargo's payment of a \$125,000 settlement in the case and the presence of nine other disputes on the individual's record.<sup>3</sup>

As discussed in the regulatory notice, between 2014 and 2016, arbitrators granted expungement for at least one associated individual in 75% of the 808 cases.<sup>4</sup> When cases closed by settlement, arbitrators granted expungement for at least one associated person in 88% of the cases.<sup>5</sup> The Clinic recognizes that there are a small number of cases where expungement may be an appropriate remedy. Nevertheless, the history of abuse of the expungement process warrants stringent requirements for this extraordinary remedy.

#### **1. The Clinic Supports The Expungement Arbitrator Roster**

Currently, in order to determine expungement requests, an arbitrator need only be qualified pursuant to FINRA Rule 13400. We support creating an Expungement Arbitrator Roster so that the arbitrators considering expungement have been trained on the unique issues and rules related to expungement. That will likely lead to more consistent results.

Under the Proposed Amendments, individuals on the Expungement Arbitrator Roster would need to meet additional requirements. Specifically, the individual would need to have (1) completed enhanced expungement training; (2) be admitted to practice law in at least one jurisdiction; and (3) have five years' experience in one of the listed disciplines.

The Clinic supports the additional requirements for an individual to be listed on the Expungement Arbitrator Roster. Additional training will ensure that the arbitrators considering expungement have training on the unique issues and rules related to expungement. It is likely that the additional training and qualifications will lead to more consistent applications of this extraordinary remedy.

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<sup>1</sup> <https://www.forbes.com/global/2000/1225/0326129a.html#7e931af36422>

<sup>2</sup> *Id.*

<sup>3</sup> <https://dealbook.nytimes.com/2013/06/10/a-rise-in-requests-from-brokers-to-wipe-the-slate-clean/>

<sup>4</sup> Regulatory Notice, p. 14

<sup>5</sup> *Id.*

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**2. The Clinic Supports The One-Year Limitation On Requesting Expungement Of CDI Under Proposed Rule 13805(a)(3)(D)**

Currently, there are no time-based restrictions under Rule 2080 that limit when an associated person may pursue expungement. As a result, an associated person may seek expungement long after the resolution of the underlying dispute with the customer. The Clinic believes that this system does not serve the interests of public investors.

Under the Proposed Amendments, an associated person is barred from bringing a claim for expungement, unless that claim is brought within one year of the closure of the underlying dispute with the customer. This Proposed Amendment will make it more difficult for an associated person to bring a stale claim for expungement. The Clinic supports this proposal because it will help resolve the issue, one way or another, in a timely fashion when the witnesses and evidence are still available that might cause arbitrators to decline expungement.

One comment letter notes that “brokers can go years before they learn of a standalone customer complaint that had been denied by their firm (often their former firm with which they have no contact) and not followed-up on by the customer.”<sup>6</sup> The Clinic is sympathetic to associated persons who did not receive notice that their firm (or former firm) denied a customer complaint. However, public investors should not be penalized for the failure of firms to implement streamlined notification and recordkeeping procedures. Certainly if an associated person is aware of an initial claim, it is not too much to ask that the associated person follow up as to disposition by the firm. The Clinic strongly believes that the one-year limitation on expungement requests is neither inequitable, nor harsh, and will improve the process.

**3. The Clinic Supports The Unanimity Requirement For Granting Expungement Under Proposed Rule 13805(b)(3)**

Currently, an arbitration panel need not unanimously determine that expungement is an appropriate remedy in order to grant expungement.

Under the Proposed Amendments, in order to grant expungement, a panel of three arbitrators would need to unanimously determine that expungement is an appropriate remedy. Expungement prevents public investors from knowing that the person whom they might trust to manage their investments was involved in a dispute. Since it may impede the ability of public investors to make informed investment decisions, expungement ought to be an extraordinary remedy. Requiring three qualified arbitrators to unanimously determine that expungement is an appropriate remedy protects public investors.

One comment letter argues that the unanimity requirement is unfair because, inter alia, even in FINRA disciplinary decisions, only a simple majority of arbitrators is required to determine that a registered representative or firm violated the rules and that sanctions are

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<sup>6</sup> See 17-42\_Robbins\_Comment.pdf at 5.

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warranted.<sup>7</sup> Nevertheless, the history of abuse of the expungement process has caused particular damage to the legitimacy of the expungement process. As a result, special measures to ensure the accuracy of that process and restore its legitimacy are justifiable.

The unanimity requirement protects public investors by ensuring that the threshold for expungement is high. At the same time, given the history of abuse of the expungement process, the unanimity requirement helps to ensure that when expungement is granted, the expungement is legitimate.

For the reasons delineated above, the Clinic supports the unanimity requirement for granting expungement under Proposed Rule 13805(b)(3).

**4. The Clinic Supports The Heightened Standard For Granting Expungement Under Proposed Rule 13805(b)(3)(B)**

Currently, under Rule 2080(b)(1), in order to grant expungement, the arbitration panel must determine that (1) the claim, allegation, or information is factually impossible or clearly erroneous; (2) the registered person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation or conversion of funds; or (3) the claim, allegation or information is false.

Under Proposed Rule 13805(b)(3)(B), in addition to identifying one of the Rule 2080(b)(1) criteria listed above as a grounds for expungement, the arbitration panel must “make a finding that the customer dispute information has no investor protection or regulatory value.”

Requiring the panel to determine that CDI has no investor protection or regulatory value allows the panel to look beyond the claim at hand and at the associated person’s record as a whole. When CDI has investor protection or regulatory value, customers should have access to it so that they can make informed investment decisions. If, for example, an associated person has a history of expungements, it would not serve investor protection or regulatory oversight to allow such a person to present a cleansed regulatory record. This is something arbitrators should consider, since expungement is supposed to be extraordinary, not merely a resume-cleansing process.

In the example cited in the introduction, a registered person was granted expungement despite the presence of nine disputes on her record. When one claim with limited investor protection value is considered in light of the entire record, it may reveal a pattern that has greater investor protection or regulatory value than that claim may have when considered in isolation. The Clinic strongly supports codifying this heightened standard for granting expungement under Proposed Rule 13805(b)(3)(B) because we believe it will protect public investors.

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<sup>7</sup> See 17-42\_Robbins\_Comment.pdf at 4.

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**5. A Personal Appearance Should Be Required For An Associated Person Requesting Expungement Under Proposed Rule 13805(c)(2)**

Currently, Rule 13805 allows an expungement hearing to be conducted via telephone, or in person.

Under Proposed Rule 13805(c)(2), a party requesting expungement would be required to appear before the arbitration panel in person or via videoconference. Expungement is designed to be an extraordinary remedy. Requiring a party requesting expungement to appear in person or via videoconference impresses the seriousness of the request upon the party. Physical or videoconference appearance will allow the arbitration panel to question the party requesting this extraordinary measure face-to-face, enabling the panel to better judge the responses of the party. The Clinic supports this measure because it will help the arbitration panel to more accurately judge the responses of the party requesting expungement.

**6. Changing The Word “Grant” to “Recommend” Within The Text of Rules 12805 and 13805 Will More Accurately Reflect The Powers of The Arbitration Panel**

Currently, Rules 12805 and 13805 state that in order to “grant” expungement, the arbitration panel must follow certain procedures. However, under Rule 2080, a party requesting expungement must obtain a court order confirming the arbitration panel’s expungement decision in order to have CDI expunged from that party’s record.

The Clinic believes that within Rules 12805 and 13805, the word “grant” should be changed to “recommend.” Since the expungement does not take effect until the associated person obtains a court order, the word “recommend” more accurately describes the power of the arbitration panel.

**7. The Clinic Strongly Opposes The Proposed Requirement That An Associated Person Request Expungement During The Underlying Customer Case**

The Clinic sees the value in deciding expungement requests in proximity to the underlying dispute with the customer. Nevertheless, we are concerned that requiring associated persons to request expungement in the underlying customer case may lead associated persons to request expungement in every dispute in order to preserve their right to request expungement.

Additionally, the Clinic is concerned that requiring associated persons to request expungement during the underlying dispute with the customer will transform hearings designed to determine the merits of a customer dispute into lengthy expungement hearings. Specifically, the Rule Proposal states that “[i]f the underlying customer case closes by award, the panel would be required to decide the expungement request during the Underlying Customer Case.” It is unfair to require a customer to participate in a potentially lengthy expungement hearing that they did not ask for.

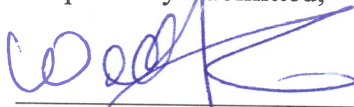
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It is the Clinic's view that any hearing on expungement should be separate from the Underlying Customer Case. The Clinic believes that it is desirable for the same panel of arbitrators who determined the underlying case to make a determination regarding expungement. However, in order to prevent substantial inconvenience to the customer, the expungement issue ought to be decided in a separate proceeding. The one-year limitation under Proposed Rule 13805(a)(3)(D) should serve as an adequate safeguard against stale claims and loss of relevant documentation.

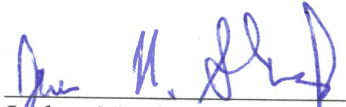
**Conclusion**

While the Clinic supports most of the Proposed Amendments, the Clinic strongly opposes the proposal to require that the expungement hearing be incorporated into the Underlying Customer Case.

Respectfully Submitted,



William A. Jacobson, Esq.  
Clinical Professor of Law  
Director, Cornell Securities Law Clinic



Joshua N. Shinbrot  
Cornell Law School, Class of 2019

This letter is to express my frustration with the effort to eliminate (or make ridiculously expensive) the ability of people in our industry to remove events from our record that may be totally wrong. I have learned that when changing firms in this industry the Broker Dealer holds all of the cards. They can literally say anything they want and we are helpless, at a difficult time in our career to immediately battle with firms that have huge budgets. On the surface, this appears to favor the big entrenched firms and make it close to impossible for those who are actually meeting with and servicing average Americans every single day. I would appreciate a response to my concerns. Thanks, Dave.

*David Wm. James*   
**Legacy Planning Group, Inc.**

Bach Building  
11650 South State Street, Suite 200  
Draper, UT 84020  
Office: (801)207-1400  
Toll Free: (866)282-1400  
Fax: (801)207-1405

[www.investlpg.com](http://www.investlpg.com)[\[investlpg.com\]](http://investlpg.com)

Please continue to allow the expungement of meritless claims. The new process is onerous.  
There are serious financial advisors who work hard, and one crazy person can impact a career.  
That seems unfair.

Catherine Joyce

Catherine Joyce, CIMA®  
Senior Vice President | Financial Advisor | Senior Portfolio Manager  
NMLS# 1262322

**Morgan Stanley Wealth Management**  
1775 Eye Street NW, Suite 200 | Washington, DC 20006  
Phone: 800-745-2451  
Direct: 202-862-9171  
Fax: 202-654-5643  
[catherine.joyce@ms.com](mailto:catherine.joyce@ms.com)



February 5, 2018

**By email to [pubcom@finra.org](mailto:pubcom@finra.org)**

Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K. Street, NW  
Washington, DC 20006-1506

Re: FINRA Regulatory Notice 17-42  
**Expungement of Customer Dispute Information**

Dear Ms. Asquith:

On behalf of the Investor Protection Clinic at the William S. Boyd School of Law at the University of Nevada, Las Vegas, we write to comment on FINRA Regulatory Notice 17-42. We represent investors who have suffered losses resulting from unsuitable financial advice. We provide pro bono assistance to investors who cannot secure private legal representation because of the size of their claims. Our clients have a direct interest in the rules promulgated by the Financial Industry Regulatory Authority ("FINRA").

We thank you for the chance to comment on proposed changes to FINRA's rules governing the expungement of customer dispute information from an associated person's Central Registration Depository ("CRD") record. Below are our Clinic's comments on several of the questions.

**Request for Comment No. 3.** *Should FINRA consider bifurcating the expungement request from the customer's claim in all cases relating to customer disputes? What would be the costs and benefits of such an approach?*

FINRA should bifurcate expungement requests from the customer's claim in all cases. As explained below, bifurcation would promote FINRA's goal of preventing expungement requests from inappropriately interfering with the arbitration process or an arbitrators' authority to award appropriate remedies.<sup>1</sup>

First, a natural distinction exists between FINRA's standards and policies governing expungement compared to all other arbitration awards. For example, the central focus for deciding whether to grant an expungement request is the protection of future customers of an

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<sup>1</sup> Notice of Filing of Proposed Rule Change and Amendment Concerning the Expungement of Customer Dispute Information from the Central Registration Depository System, 73 Fed. Reg. 18308 (April 3, 2008), <https://www.sec.gov/rules/sro/34-47435.htm> (last visited Jan. 26, 2018).

associated person;<sup>2</sup> but nearly all other remedies under FINRA's arbitration process focus on a narrower dispute between a customer and a firm or associated person. Bifurcation would clarify this distinction because it ensures that the public's interests would remain the central focus in expungement requests.

Similarly, the standard of review for granting expungement requests differs significantly from other FINRA remedies. Under FINRA Rule 2080, arbitrators may recommend expungement only when "the information is found to have no meaningful investor protection or regulatory value."<sup>3</sup> This is a relatively high standard—demanding certainty for any expungement request approval. In contrast, most other remedies in FINRA's arbitration program use a "preponderance of the evidence standard."<sup>4</sup> These different standards have likely confused arbitrators in the past.<sup>5</sup> Bifurcation, however, would prevent this confusion by ensuring that these legal standards remain distinct.

FINRA should also recognize that requiring bifurcation in all cases will not diminish arbitrators' ability to collect the information that they need to evaluate expungement requests. FINRA's Arbitrator's Guide states that "arbitrators should request any documentary or other evidence they believe is relevant to the expungement request," and "arbitrators should ensure they have all the information necessary to make an informed and appropriate recommendation on expungement."<sup>6</sup> These guidelines show that during any bifurcated expungement request, arbitrators would have the means necessary to gather relevant information.

Finally, a bifurcation requirement aligns directly with FINRA's proposal to establish specially trained Expungement Arbitrators. These Expungement Arbitrators would have enhanced qualifications and expungement training.<sup>7</sup> Bifurcation would thus ensure that all expungement requests are decided under equal standards—through the specialized analysis and skill of these Expungement Arbitrators.

**Request for Comment No. 4.** *What are the costs and benefits of requiring the unanimous consent of a three-person panel to grant all requests for expungement of customer dispute information?*

FINRA should require unanimous consent of a three-person panel to grant all requests for the expungement of customer dispute information. Requiring unanimous consent is critical, because

<sup>2</sup> Hammad Qureshi & Jonathan Sokobin, *Do Investors Have Valuable Information About Brokers?*, 2–3 (FINRA Office of the Chief Economist, Working Paper, Aug. 2015), <http://www.finra.org/sites/default/files/OCE-Working-Paper.pdf> (last visited Jan. 26, 2018) ("To help investors make informed choices about the brokers with whom they conduct business, [FINRA] provides . . . BrokerCheck . . . to investors.").

<sup>3</sup> See FINRA, Regulatory Notice 09-33, 2009 WL 1701937 [hereinafter FINRA Rule 2080].

<sup>4</sup> FIN. INDUSTRY REG. AUTHORITY, DISPUTE RESOLUTION ARBITRATOR'S GUIDE 62 (2014) [hereinafter ARBITRATOR'S GUIDE].

<sup>5</sup> See Christine Lazaro, *Has Expungement Broker Brokercheck?*, 14 J. BUS. & SECURITIES L. 123, 146 (2013) ("Expungements continue to be too readily granted by arbitrators. This does not appear to be solely a result of customers not opposing the expungement requests because they have settled their claims. This is more likely a result of arbitrators not fully understanding the standards pursuant to which expungements should be granted.").

<sup>6</sup> ARBITRATOR'S GUIDE, *supra* note 4, at 70.

<sup>7</sup> See FINRA Regulatory Notice 17-42, *Expungement of Customer Dispute Information* 10, [www.finra.org/sites/default/files/notice\\_doc\\_file\\_ref/Regulatory-Notice-17-42.pdf](http://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-17-42.pdf) (last visited Jan. 26, 2018).

if FINRA holds expungement out to be an *extraordinary* remedy, then it must be guided by a higher standard of review and certainty than all other matters.<sup>8</sup> FINRA has even recognized a need for a higher standard of review with expungement requests in its current Rules and its Dispute Resolution Arbitrator's Guide. FINRA Rule 2080 and the Arbitrator's Guide state that expungement may only be granted "when the arbitrators find and document one of [the following] narrow grounds:"

1. the claim, allegation or information is factually impossible or clearly erroneous;
2. the registered person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation or conversion of funds; or
3. the claim, allegation or information is false.<sup>9</sup>

Rule 2080 also requires that "arbitrators recommend expungement only when the information is found to have no meaningful investor protection or regulatory value."<sup>10</sup> These requirements demand far more certainty than any other remedy in FINRA's arbitration process—certainly higher than the "preponderance of the evidence standard" for damage awards on the merits.<sup>11</sup> FINRA's future rules to recommend expungement should maintain these already established, high standards.

Looking to the potential costs of a unanimous agreement standard, opponents generally argue that unanimity is unfair given that other arbitral awards only require a panel's majority vote.<sup>12</sup> This contention misses the point, however, because FINRA designed expungement to be unique from all other arbitral decisions. Compare, for example, the process to grant expungement requests with the process to grant an award of damages on the merits of a claim. On one hand, FINRA's rules currently allow a majority of arbitrators to *refuse* an expungement request although a majority denies damages;<sup>13</sup> but, on the other hand, arbitrators can *grant* an expungement request even when the arbitrators award damages.<sup>14</sup> This comparison shows that FINRA designed expungement to be isolated from all other parts of a claim. So, in keeping with this design, FINRA should not be guided by any other arbitral standards in promulgating this proposed rule—expungement procedures must remain unique to the remedy.

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<sup>8</sup> *Id.*; *Expungement: an "Extraordinary Remedy,"* NEW ENGLAND SEC. LITIG. & ARB. BLOG, <http://pretisecuritieslitigationarbitration.blogspot.com/2017/07/expungement-extraordinary-remedy.html> (last visited Feb. 1, 2018) (explaining that "the net result [of FINRA Rules 2080, 12805, and 13805] is a strong default rule against expungement").

<sup>9</sup> ARBITRATOR'S GUIDE, *supra* note 4, at 73.

<sup>10</sup> FINRA Rule 2080, *supra* note 1.

<sup>11</sup> ARBITRATOR'S GUIDE, *supra* note 4, at 62.

<sup>12</sup> See Kaufman, Gildin & Robbins LLP, Comment on FINRA's Proposed Amendments to Its Expungement Arbitration 4, [www.finra.org/sites/default/files/notice\\_comment\\_file\\_ref/17-42\\_Robbins\\_Comment.pdf](http://www.finra.org/sites/default/files/notice_comment_file_ref/17-42_Robbins_Comment.pdf) (last visited Feb. 1, 2018).

<sup>13</sup> FIN. INDUSTRY REG. AUTHORITY, DISPUTE RESOLUTION: EXPUNGEMENT TRAINING 19 (2015), [www.finra.org/sites/default/files/FINRA-Expungement-Training-May-2015.pdf](http://www.finra.org/sites/default/files/FINRA-Expungement-Training-May-2015.pdf) (last visited Jan. 26, 2018) ("when a broker prevails in an arbitration case, that is not, in and of itself, an appropriate ground for expunging information . . .").

<sup>14</sup> See FINRA Rule 2080, *supra* note 1 (explaining that when multiple associated persons are named in a claim, an arbitrator can grant expungement for one of those persons if the arbitrator determines that "the registered person was not involved in the alleged investment-related sales practice violation").

In sum, a unanimous panel requirement would align directly with the high level of certainty that FINRA currently requires for granting a request for expungement. A unanimous panel requirement would also ensure that expungement truly is an extraordinary remedy—granted only when arbitrators find that a claim has no meaningful investor protection or regulatory value.

**Request for Comment No. 6.** *Should the associated person who is requesting expungement be required to appear in person or by videoconference, rather than by phone, at the expungement hearing?*

FINRA should require that an associated person who requests expungement appear either in person or by videoconference rather than by phone. Unlike appearing in person or by videoconference, telephonic appearance limits arbitrators' ability to assess the credibility and sincerity of the associated person's testimony during the expungement process.<sup>15</sup>

Psychological research indicates that witness sincerity is observable through non-verbal cues.<sup>16</sup> For example, rigid posture or relaxed facial expressions may indicate that a witness is lying in their testimony.<sup>17</sup> Similarly, lying witnesses are more likely to "move their hands less, speak with higher pitched voices, and . . . through foot and leg movements."<sup>18</sup> Appearances in person and by videoconference allow arbitrators to directly observe these cues. Appearance by telephone, however, does not.

FINRA's decision to allow only in-person or videoconference appearances would also reflect the principle that expungement is an extraordinary remedy.<sup>19</sup> FINRA demands that arbitrators only recommend expungement under limited circumstances and when arbitrators are certain that the underlying complaint has "no meaningful investor protection or regulatory value."<sup>20</sup> The physical appearance of an associated person—in person or by videoconference—allows the arbitration panel to reach this high level of certainty. That is, the panel can garner relevant information from an individual by questioning that person while also observing both the verbal and non-verbal cues that signal the credibility of their responses.

Alongside the benefits to arbitrators of more easily observing a person's credibility, any limitation of appearances to only in person or videoconference carries minimal, if any, costs. FINRA currently offers 71 hearing venues.<sup>21</sup> Likewise, all four of FINRA's main regional

<sup>15</sup> James P. Timony, *Demeanor Credibility*, 49 CATH. U. L. REV. 903, 915 (stating that "[v]ideo technology allows a witness to testify without being physically present in court, while still giving the fact-finder the advantage of observing the witness's demeanor," while telephonic appearances do not.).

<sup>16</sup> Steven I. Friedland, *On Common Sense and the Evaluation of Witness Credibility*, 40 CASE W. RES. L. REV. 165, 185–86 (1989).

<sup>17</sup> *Id.*

<sup>18</sup> *Id.*

<sup>19</sup> See FINRA Rule 2080(b)(2), *supra* note 1; see also *Notice to Arbitrators and Parties on Expanded Expungement Guidance*, FINRA, <http://www.finra.org/arbitration-and-mediation/notice-arbitrators-and-parties-expanded-expungement-guidance> (last visited Jan. 28, 2018).

<sup>20</sup> See *Notice to Arbitrators and Parties on Expanded Expungement Guidance*, *supra* note 19.

<sup>21</sup> *Dispute Resolution Regional Offices and Hearing Locations*, FINRA, <https://www.finra.org/arbitration-and-mediation/dispute-resolution-regional-offices-and-hearing-locations> (last visited Jan 31, 2018) ("including at least one in each state of the United States, one in San Juan, Puerto Rico, and one in London, UK.").

offices offer videoconferencing capabilities.<sup>22</sup> And in circumstances where an expungement hearing is not held at one of FINRA's physical offices, several companies offer videoconferencing solutions compatible with FINRA's videoconferencing system.<sup>23</sup> This accessibility makes any travel costs unnecessary, while also giving the arbitration panel a clear chance to observe the demeanor of any person seeking expungement.

**Request for Comment No. 11.** *The proposal would clarify for arbitrators that the standard for granting the permanent removal of customer dispute information from CRD is a finding that at least one of the Rule 2080(b)(1) factors applies and that customer dispute information has "no investor protection or regulatory value." Are there specific factors that arbitrators should consider when making a finding that the customer dispute information has "no investor protection or regulatory value"?*

FINRA should provide arbitrators with clear guidance documents that practically explain the factors in Rule 2080(b)(1) as well as the level of certainty required by arbitrators to find that customer dispute information has "no investor protection or regulatory value." The discussion below outlines how these guidance documents should explain the meaning of terms such as "clearly erroneous," "not involved," "factually impossible," or "false." In crafting this guidance, FINRA should explain the level of certainty required for expungement by reference to the standards that our judicial system already recognizes.

An arbitration decision in 2013 shows the importance of guidance documents that explain the expungement standard by reference to those already in public courts.<sup>24</sup> In that decision, an arbitrator explained the burdens he *believed* were required by the Rule 2080(b)(1) factors of "clearly erroneous" and "false."<sup>25</sup> The arbitrator described "clearly erroneous" as being closest to a "clear and convincing evidence" standard used commonly within civil courts.<sup>26</sup> Similarly, the arbitrator clarified "false" to mean that "[w]hen an allegation is supported by some reasonable proof, even short of 'preponderance,' it cannot be said to be 'false.'"<sup>27</sup> The arbitrator did not rely on any FINRA guidance, however, to create these standards of review. Instead, the arbitrator merely explained the vagueness of the current expungement standards and stated "until FINRA substantially clarifies Rule 2080, requests for expungement will multiply, resulting in many expungements FINRA never intended."<sup>28</sup>

This decision explains how arbitrators need to rely on an established legal standard to evaluate expungement requests. Vague terms such as "false" or "factually impossible" are simply impractical without context.

<sup>22</sup> *Videoconferencing Available in FINRA Regional Offices*, FINRA, <https://www.finra.org/arbitration-and-mediation/videoconferencing-available-finra-regional-offices> (last visited Jan. 28, 2018).

<sup>23</sup> *Id.* ("Other companies may also provide off-site videoconferencing compatible with FINRA's.s.").

<sup>24</sup> *Gilliam v. SagePoint Fin., Inc.*, FINRA No. 12-03717, 2013 WL 3963949 (2013) (Meyer, Arb.).

<sup>25</sup> *Id.* at \*2 (2013).

<sup>26</sup> *Id.*

<sup>27</sup> *Id.* (emphasis added).

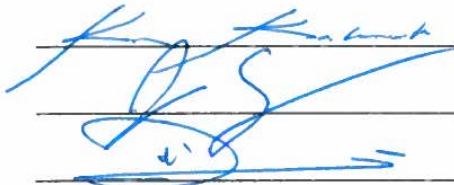
<sup>28</sup> *Id.* at \*4.

**Request for Comment No. 12.** *In a simplified arbitration case, if a customer requests a hearing, should the single arbitrator be permitted to decide an expungement request, if a request is filed?*

FINRA should not allow the single arbitrator in a simplified arbitration case to decide an expungement request. As stated throughout this comment, expungement must be treated as an extraordinary remedy. A unanimous decision by three arbitrators provides a better assurance that the public's interest in knowing about complaints will be protected.

Respectfully Submitted,

INVESTOR PROTECTION CLINIC  
Thomas & Mack Legal Clinic  
William S. Boyd School of Law  
University of Nevada, Las Vegas

A handwritten signature in blue ink, appearing to read 'Kristopher J. Kalkowski', is written over three horizontal lines.

Kristopher J. Kalkowski  
Jacob Crawley  
Omar Nagy  
*Student Attorneys*  
*Investor Protection Clinic*  
*William S. Boyd School of Law*

I am writing to you to express my views on the new proposed rules. I have been registered with your organization since 1992 and have experienced firsthand how customer complaints can be driven by a firm-wide decision (keeping complaints on auction rate preferred claims, which were reimbursed in full by firms) or untrue allegations. I strongly urge you to reconsider your stance on taking away the option to expunge an allegation over 12 months old as well as a majority decision by an arbitration panel. I do understand the need to protect clients but there should also be a balance maintained in the arbitration proceedings.

Respectfully,

William Leven

**William Leven, CFA**

Managing Director

Senior Portfolio Manager

Private Banking and Investment Group

NMLS ID 1394286

Please accept these comments regarding the proposed rule change.

My name is David Liebrader. For the past 25 years I have been representing public customers in claims against brokerage firms and registered representatives in the FINRA (formerly NASD) forum. I have handled well over 1000 cases in the forum.

I write in support of the amendment requiring "unanimous agreement among the panel" that the customer complaint sought to be expunged would have "no investor protection or regulatory value." Too many legitimate claims disappear from public view in the largely uncontested expungement process.

Over the course of many years I have settled hundreds of cases where the registered representative's counsel indicated that the rep wanted to seek expungement of the customer complaint if the case settled. As a practical matter, and as an advocate for my client, my primary consideration in prosecuting the case was to make my client "whole".

During settlement discussions Respondent's counsel would typically ask that my client "not oppose a request for expungement" as a condition to settling the case. Most of my clients, out of either the kindness of their hearts, the eagerness to have closure, or simply because the settlement was too good to pass up would agree not to oppose the request..

After settlement documents are negotiated and the settlement proceeds deposited the clients consider the matter closed. None of my clients ever appeared before a panel to testify as to the events, nor have any panels ever asked to speak with my clients formally or informally as to the allegations made in those claims. ZERO TIMES out of several hundred expungements.

In my experience the expungement hearings are one sided affairs that lack any substance or nuance, and allow the rep to paint the rosiest picture possible, and panels seem to grant the requests at an 80% rate.

I think the public would be better served if there were higher bars to expungement, and requiring unanimous consent after considering the interests of the broader investing public seems a good thing.

I also write to comment on the filing fee for expungement proceedings. I think they are too high. Court filing fees are in the \$200 - \$300 range. FINRA, as a self regulatory agency is clearly in a position to require its members to shoulder more of the cost in this mandatory arbitration forum.

Having represented a handful of reps over the years, I can tell you that when a frivolous claim is filed, it adds insult to injury to require these innocent reps to pay close to \$1500 just to file their claim. The same holds true for aggrieved investors. I would like to see FINRA lower filing fees, not raise them, and to provide more relief for Claimants who for financial reasons have trouble coming up with the filing fees.

Thank you for considering these comments.

Dave Liebrader.

The public is aware of the tremendous penalty a broker can pay with the filing of a complaint. Not all clients listen to their advisors. Nonetheless, many blame the advisor for their own decisions when it changes comes to investing and potential for loss.

**John C. Lindsey, CFP®,CKA®**

President / CEO

[john@lindseyandlindsey.com](mailto:john@lindseyandlindsey.com)



The Law Offices of  
**PATRICK R. MAHONEY, P.C.**  
1055 WILSHIRE BLVD.,  
SUITE 850  
LOS ANGELES, CA 90017  
[www.pmahoneylaw.com](http://www.pmahoneylaw.com)

February 5, 2018

**Patrick R. Mahoney**  
P: (213) 805-5677  
F: (213) 805-6477  
[patrick@pmahoneylaw.com](mailto:patrick@pmahoneylaw.com)

**Via Email Only ([pubcom@finra.org](mailto:pubcom@finra.org))**

To Whom it May Concern  
FINRA Dispute Resolution  
Office of the Corporate Secretary  
1735 K Street, N.W.  
Washington, DC 20006-1506

Re: **The Law Offices of Patrick R. Mahoney, P.C.**  
**Official Comment on FINRA Regulatory Notice 17-42**

To Whom It May Concern:

Please allow this letter to represent The Law Offices of Patrick R. Mahoney, P.C.'s ("PRM") comment on FINRA Regulatory Notice 17-42, which discusses proposed amendments to Codes of Arbitration Procedure relating to expungement requests of customer dispute information (the "proposed rules").

**I) Introduction**

PRM has handled numerous expungement matters on behalf of associated persons, and submits this comment with the best interests of those associated persons in mind.

In short, PRM strongly disagrees with the proposed rules—particularly as they relate to matters where the associated person is not a named party to an underlying customer case. These proposed changes would create a suffocating burden on associated persons to *disprove* the merits of an underlying customer complaint in instances in which (often) they are not even a named party to a customer case, and, in many cases, are not even *mentioned* in the customer case. If these proposed rules involved government actors, they would be dismissed out of hand as a violation of basic civil procedural and substantive due process rights.

There is no other industry (that this humble author can think of) in the United States that maintains a system that creates a rebuttable presumption of liability in the face of (often ambiguous) *allegations* of wrongdoing. The proposed rules do just that through their continued requirement that such allegations, irrespective of merit, remain publicly available *unless* the associated person has the resources to spend tens of thousands of dollars just to to *try* prove otherwise.

What's more, as a result of the proposed rules' requirement for unanimity amongst the three arbitrator panel tasked with rendering a decision for, or against expungement, the burden of proof required to overcome this rebuttable presumption of liability is akin to "beyond a reasonable doubt"—the highest burden contemplated.

PRM agrees that the rules concerning expungement must be changed, but these proposed rules are not the answer.

**II) PRM's Concerns Relating to Expungement Requests Involving Associated Persons who are named as a Party to a Customer Case.**

**1) Registered Representatives Benefit from the Rights Available to all Respondents When they are named in a Customer Case.**

PRM agrees that a CRD record disclosure of an underlying customer complaint is warranted when a customer actually names the registered representative as a respondent to their case. By actually naming the registered representative, the customer undeniably makes an allegation, *specifically directed at the registered representative*, that he or she made some type of sales practice violation.

Meanwhile, the registered representative has all of the rights available to any respondent in a FINRA case. They can: (1) answer the statement of claim and assert all available defenses; (2) engage in discovery; (3) attend all underlying arbitration hearings; (4) choose their own counsel; and, (5) (most importantly) may benefit from the fundamental requirement that places the burden on the Claimant to establish his or her claims *directed towards the registered representative* by a preponderance of the evidence.

**2) If the Underlying Customer Case Closes by Award, and the Customer's Claims are Denied in their Entirety, FINRA should Automatically Grant Expungement.**

Where the underlying customer case closes by award, and the award denies all claims directed at the associated person, the associated person should automatically have their CRD record expunged of all reference to the complaint. After all, *the associated person won the case on the merits*. FINRA rules should not then subject associated persons to a second determination that shifts the burden on the associated person to further disprove a claim that they already successfully defended.

The proposed rules do not subject the member firm (and co-respondent to the hypothetical action) to such burden-shifting. If the proposed rules did, member firms would undoubtedly oppose them en masse.

Therefore, if a customer names an associated person as a respondent in a customer case, and the arbitration panel renders an award denying the customer's claims directed at the registered representative, there should be no need to make a second determination on expungement. To require otherwise unfairly creates a separate set of standards depending on whether the respondent is a registered representative or member firm.

**III) Unnamed Associated Persons in Customer Cases Should Not Be Subjected to the Same Expungement Standards as Named Associated Persons to Customer Cases.**

**1) FINRA's Overbroad CRD Reporting Rules are the Exclusive Source of the Influx of Expungement Proceedings.**

Though not stated explicitly in Regulatory Notice 17-42, the proposed rules seek to develop a new expungement system that aims to decrease the amount of instances that arbitrators grant expungement relief so that the statistics will properly reflect the remedy's "extraordinary" nature.

Ironically, FINRA created this problem when it broadened the rules as to what type of customer complaint a member firm must report on the CRD records of its associated persons. These overly broad reporting rules created countless situations where associated persons, with peripheral (at best) involvement in a customer complaint, had their CRD records tarnished due to flawed reporting criteria, and not actual wrongdoing. This, in turn, has led to an influx of successful expungement requests. If FINRA does not change its reporting standards, however, and implements the proposed rules, FINRA will exacerbate this existing problem to the extreme detriment to the associated persons who fall victim to it.

Pursuant to Regulatory Notice 09-23 ("RN 09-23") and the amendments FINRA made to Forms U4 and U5 that coincided with that regulatory notice, member firms are the exclusive arbiter in deciding which customer complaints require CRD record disclosure, and which do not.

RN 09-23 and its progeny require member firms to disclose customer complaints under the following situations:

- Where the associated person is a named party to the Statement of Claim;
- The Statement of Claim or complaint specifically mentions the individual by name and alleges the individual was involved in one or more sales practice violations; or
- Where the Statement of Claim or Complaint does not mention the individual by name but the firm has made a good faith determination that the sales practice violation(s) alleged involves one or more particular individuals.

The CRD record reporting criteria concerning customer complaints contemplate a massive scope of scenarios that might (depending on the member firms' subjective interpretation of the reporting rules) trigger a CRD record disclosure. These overbroad reporting criteria, coupled with the unfettered discretion given to member firms to determine reportability, have unfairly subjected someone who is neither named nor mentioned in a customer complaint, to the exact same expungement standard as someone named as a Respondent in a customer complaint and subjected to clear allegations of sales practice violations.

For example, suppose a customer names an associated person in their customer case, and directs specific causes of action against that associated person for fraud, breach of fiduciary duty, and unsuitability. Under RN 09-23, the firm where the associated person worked at the time of the complaint would amend the associated person's CRD record to reflect the complaint because the customer named the associated person as a respondent, and made unambiguous allegations that the associated person committed sales practice violations.

Alternatively, suppose a customer does not name or even mention any associated person in their case and makes allegations against only a member firm for fraud, breach of fiduciary duty, and unsuitability. RN 09-23 requires the reporting member firm to make the completely subjective determination to report this customer case on the CRD records of all associated persons "involved" in the allegations. This might include (among many other examples): the customer's broker of record; the broker of record's manager; or a licensed assistant who did nothing other than process paperwork at the direction of the broker of record.

And yet consider that: (1) the licensed assistant in the above example would have his CRD record blemished the same as the associated person actually named in the customer complaint in the first example; (2) the licensed assistant is presumed liable for reporting purposes in the same way as the associated person actually named in the complaint; and (3) the licensed assistant must convince a panel of three arbitrators, who FINRA will educate on the extraordinary nature of the expungement remedy, to unanimously agree that his record should be expunged pursuant to the same, one-sided expungement standards available to the associated person named in the complaint. And that is to say nothing of the cost associated with the licensed assistant's attempt to earn expungement.<sup>1</sup>

FINRA cannot continue to treat these immensely different situations equally for purposes of creating CRD reporting and expungement standards.<sup>2</sup>

**2) The Customer's Complaint should have to Unmistakably Direct Allegations of Sales Practice Violations towards an Associated Person to trigger any CRD Record Reporting.**

FINRA Rule 12313(a) specifically permits customers, at their own discretion, to name multiple respondents. That rule states in relevant part, "One or more parties may name one or more respondents in the same arbitration if the claims contain any questions of law and fact common to all respondents..."

FINRA Rule 12302(a) similarly gives customers carte blanche authority to state their allegations in their statement of claim. Indeed, the statement of claim must "specify the relevant facts and remedies requested."

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<sup>1</sup> PRM estimates that the Proposed Rules would regularly cost an associated person upwards of \$20,000 to seek expungement. These costs are attributable to FINRA's proposed set filing fee for expungement proceeding, hearing costs, and proposed requirement that an in-person hearing and/or video conference be held in all expungement matters.

<sup>2</sup> PRM further notes the inherent ambiguity in trying to apply the standards set out in FINRA Rule 2080 (i.e. (1) that the claim is impossible or clearly erroneous ; (2) that the claim is false, or (3) that the associated person lacked involvement) when the associated person is not even mentioned in the underlying complaint.

Accordingly, the customer's complaint itself, above all else, should dictate whether it warrants disclosure on an associated person's CRD record in the first place. If a customer, in evaluating the parties he or she wants to name as respondents in their Statement of Claim, decides *not* to name an associated person as a respondent to their claim, FINRA must consider that to the associated persons' benefit when developing its reporting and expungement rules.

Similarly, if the customer does not include as part of their statement of "relevant facts and remedies" any specific allegations of wrongful conduct directed towards an associated person in their statement of claim; or, where the customer doesn't even *mention* any associated person in the statement of claim, FINRA must also consider those issues to the associated persons' benefit when developing CRD reporting and expungement rules.

Nevertheless, the proposed rules require the same rebuttable presumption of liability, and the same expungement standard regardless of whether the associated person is named in the customer case, unnamed but mentioned in the customer case, and unnamed and not mentioned in the customer case.

#### **IV) Conclusion**

FINRA's proposed rules are patently unfair to associated persons. They devalue the impact that publicly available customer complaints have on the reputation and continued employment of associated persons in the financial services industry. They do nothing to change the overbroad CRD record reporting rules that promote CRD record reporting under frivolous circumstances. And they create an unprecedented rebuttable presumption of liability, subject to "beyond a reasonable doubt" burden of proof, the likes of which are unseen in any other industry.

For those reasons, PRM opposes the proposed rules.

Sincerely,

/s/ Patrick R. Mahoney

Patrick R. Mahoney  
The Law Offices of Patrick R. Mahoney, P.C.

I have a question. Why are Chairs for Expungement proceedings required to be attorneys when that is not a requirement for Chairs of other proceedings?

Thank you for your response.

*Mimi B. Osiason*

Arbitrator # A15927

LBO Consulting  
3301 Bayshore Blvd., Unit 608  
Tampa, FL 33629  
813/287-3602

To whom it may concern:

I believe that if a complaint winds up as a FINRA violation then the complaint and resulting damages asserted by FINRA should be posted to the U-4. Moreover, if the party has more than one complaint even if it does not result in a penalty should be posted to the U-4. If the FINRA rep is clean for 5 years after the last complaint with FINRA asserted damages or complaints with FINRA asserted damages should be lifted from the U-4.

Hi my name is leonardo ramirez and i would love to see my record clean ive been in the business for over 10 years and had a very clean record until a client with not merit wanted to ruin and damage my track record. Although i won the case and client had no merit and substance in accusations i was still left with the one mark on my license.

Please i would love to get this removed.

Please let me know what i need to do

thank you

leo ram

Please keep in place a reasonable and cost effective mechanism for advisors to have their records reviewed and expunged.

There are plenty of examples of either false or frivolous claims against advisors that shouldn't be on their records.

This isn't to say that there also are bad apples who deserve to have marks on their records or to not be in the business of advising.

But to not have a reasonable forum with reasonable costs and mechanism in place to have things heard is simply not fair.

Regards,

**Andy Rieger**  
**Senior Vice President**  
**Financial Planning Specialist**  
Morgan Stanley

|                               |                     |
|-------------------------------|---------------------|
| Wealth Management             | 703 739-3694 Direct |
| 333 John Carlyle St. Ste. 650 | 703-879-1000 eFax   |
| Alexandria, VA 22314          | 800-336-5405 x3694  |

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[www.morganstanleyfa.com/rieger\[morganstanleyfa.com\]](http://www.morganstanleyfa.com/rieger[morganstanleyfa.com])

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KAUFMANN  
GILDIN &  
ROBBINS LLP  
ATTORNEYS AT LAW

767 THIRD AVENUE  
NEW YORK, NEW YORK 10017  
TEL (212) 755-3100  
FAX (212) 755-3174  
WWW.KAUFMANNGILDIN.COM

Direct Dial: 212-705-0815  
[drobbins@kaufmanngildin.com](mailto:drobbins@kaufmanngildin.com)

December 27, 2017

**Via FedEx**

Ms. Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

Re: Comment on FINRA's Proposed Amendments to its Expungement Arbitration  
Rules [Regulatory Notice 17-42]

Dear Ms. Asquith:

While the evolving guidance and rules on FINRA arbitration expungement procedures are based on the well-meaning precepts of investor protection and regulatory value,<sup>1</sup> it is my respectfully submitted opinion that three provisions of the proposed rules are *inequitable and unfairly harsh* to financial advisors and should be reconsidered before FINRA submits the rules to the SEC. In Regulatory Notice 17-42,<sup>2</sup> FINRA states that it "is interested in receiving comments on all aspects of the proposed amendments." Three of the questions posed by FINRA at the end of the Notice deal with procedural provisions I would like to address.

**1. Context for Opinions**

By way of brief context to my comments, they are based on representing investors, brokers and firms for decades; having the honor of being on FINRA's Arbitration and Mediation Committee for four years; and, being the author of a two volume treatise for attorneys on securities arbitration (published for almost 30 years) and of an annual *Practice Commentary* to the Laws of the State of New York on the subject.

On behalf of my investor clients, I have argued *against* the expungement of their arbitrations from a broker's BrokerCheck Report and as an attorneys for brokers, I have - only where appropriate<sup>3</sup> - argued for the expungement of arbitration Statements of Claim and customer complaints that were denied by brokerage firms and not followed-up with an arbitration.

<sup>1</sup> See proposed Rule 12805(b)(3)(B).

<sup>2</sup> <http://www.finra.org/industry/notices/17-42>

<sup>3</sup> See Rule 2080(b)(1) - (A) the claim, allegation or information is factually impossible or clearly erroneous; (B) the registered person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation or conversion of funds; or (C) the claim, allegation or information is false.

**KAUFMANN GILDIN & ROBBINS LLP**

As a founding member of the Public Investors Arbitration Bar Association (PIABA), I have been critical of my colleagues who, after settling customer cases, offer no opposition to a broker's pursuit of expungement.<sup>4</sup> As a member of the Compliance and Legal Division of the Securities Industry Association (SIFMA), I am sensitive to meritless claims harming a financial advisor's right to earn a living in the pursuit of his or her profession. In any context, it is offensive to be unjustly accused of a wrongdoing and not be able to defend oneself or to be saddled with inequitable and harsh burdens in trying to do so.

In expungement cases, I fully appreciate the shifting of burdens of proof from:

- The customer's obligation to prove that a broker engaged in wrongdoing and that that wrongdoing directly resulted in specific damages to
- The broker's burden that either the claim was impossible or erroneous, that the broker was not involved in the sales practice violation or that the claim was false.

## **2. Problematic Procedural Provisions**

With that context in mind, let me first say that I fully appreciate the overview language of Regulatory Notice 17-42:

It has been FINRA's long-held position that expungement of customer dispute information is an extraordinary measure, but it may be appropriate in certain circumstances.

Expungement of a customer's arbitration Statement of Claim or a customer's stand-alone complaint that was denied and not followed-up on *should* be an extraordinary remedy, but, in my opinion, three provisions in the proposed rules could very well have the effect of adding the word "very" to the already onerous, though necessary word "extraordinary." They are proposed:

- Rule 12805(b)(1) - hearing session attendance;
- Rule 12805(b)(3) - necessity of unanimous decision; and,
- Rule 13805(3)(E) - one year time limitation for stand-alone complaints that were denied and not followed-up on.<sup>5</sup>

More specifically:

### **12805. Expungement of Customer Dispute Information under Rule 2080**

#### **(b) Deciding a Request for Expungement of Customer Dispute Information**

<sup>4</sup> See *PIABA Law Journal*, "Challenging Expungements After Settlements," Vol. 3, No. 3, 2016).

<sup>5</sup> I have no issue with a one year time limitation following the closure of an arbitration case through other than an Award [proposed Rule 13895(a)(3)(D)] since there is little question that the broker would have been on notice of the customer's complaint.

KAUFMANN GILDIN & ROBBINS LLP

In order to grant expungement of customer dispute information under Rule 2080, the panel must:

- (1) Hold a recorded hearing session **in person or by videoconference** regarding the appropriateness of expungement.
- ...
- (3) **Agree unanimously** to grant expungement ...

**13805. Expungement of Customer Dispute Information under Rule 2080 (a)  
Requesting Expungement of Customer Dispute Information**

(3) An associated person may not file a request for expungement of customer dispute information:

- ....
- (E) if there was no investment-related, customer-initiated arbitration involving the customer dispute information, and **more than one year has elapsed** since the date that the customer complaint was initially reported to the Central Registration Depository system.

**3. Regulatory Notice 17-42 “Request for Comments”**

Among the 12 questions posed by FINRA at the end of Regulatory Notice 17-42 are the following three. Under each of these three questions, I’ve added FINRA’s rationale for the provision.

**Question #4 – Unanimous Award Required**

**Question #4** - What are the costs and benefits of requiring the unanimous consent of a three-person panel to grant all requests for expungement of customer dispute information?

**FINRA’s Rationale** – “The unanimity requirement would apply to all requests for expungement of customer dispute information. Thus, when a panel decides an associated person’s expungement request during the Underlying Customer Case, the panel would be required to agree unanimously to grant expungement. In deciding the customer’s claims, however, a majority agreement of the panel would continue to be sufficient. The requirement that the decision be unanimous, rather than a majority decision, could also increase the difficulty for an associated person to obtain expungement. To the extent that customers and firms use customer dispute information to make business and employment decisions, if customer dispute information is not expunged as frequently, associated persons could experience a loss of business and professional opportunities, loss of employment at their current firm, and thus, decreased income.”

KAUFMANN GILDIN & ROBBINS LLP

**Comment**

- While securities arbitration at FINRA (and arbitration in general) is an equitable forum, it is inequitable and harsh to require a broker to prove one of the three grounds for expungement to a *unanimous* panel of arbitrators and only require a *majority vote* for the customer who had alleged misconduct against that broker.
- For as long as I have been involved in securities arbitration,<sup>6</sup> Awards have been based on a majority of the panel for customers and brokers alike, be they claimants or respondents.
- A FINRA expungement arbitration is not a FINRA disciplinary decision, where even there a *majority* of panelists can decide that a broker or firm violated FINRA rules and can be sanctioned.<sup>7</sup> That is, since a unanimous decision is not required in a FINRA regulatory action, it is inequitable and harsh to require such a standard in a FINRA arbitration.
- Even in civil litigation, it is the law of most states that a jury need not come to a unanimous decision in favor of a plaintiff for that party to prevail.<sup>8</sup>
- FINRA is enhancing the quality of expungement panels. In the process, it should show due respect to such arbitrators. If two of the three panelists believe expungement is in order, such a determination should be honored.

**Question #5 - One Year Time Limitation**

**Question #5** - Is the one-year limitation on being able to request expungement of customer dispute information appropriate? Should the time period be longer or shorter?

**FINRA's Rationale** - is presented in its discussion of customer arbitration cases and then with respect to stand-alone customer complaints. FINRA offers a rationale for the former but is silent for a one year time limit on the latter.

- *Arbitrations* – “With respect to the fourth limitation, if the expungement request is not filed within a year after the Underlying Customer Case closes, the associated person would forfeit his or her right to request expungement. The one-

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<sup>6</sup> In the early 1980s, I was Director of Arbitration of the American Stock Exchange, when arbitration of customer disputes was a voluntary process.

<sup>7</sup> See FINRA Rule 9268(a) – “Decision of Hearing Panel or Extended Hearing Panel,” which states that: (a) Majority Decision - Within 60 days after the final date allowed for filing proposed findings of fact, conclusions of law, and post-hearing briefs, or by a date established at the discretion of the Chief Hearing Officer, the Hearing Officer shall prepare a written decision that reflects the views of the Hearing Panel or, if applicable, the Extended Hearing Panel, as determined by majority vote.

<sup>8</sup> See, McKinney's New York CPLR § 4113, Disagreement by Jury

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year limitation period would ensure that the expungement hearing is held close in time to the Underlying Customer Case, when information regarding the Underlying Customer Case is available and in a timeframe that would increase the likelihood for the customer to participate if he or she chooses to do so.”

- *Complaints* – “The fifth limitation would establish a one-year period for associated persons to expunge customer dispute information that arose from a customer complaint and did not result in an arbitration claim. Under the proposal, the associated person would have a year from the date that a member firm initially reported a customer complaint to CRD to file an expungement request.”

Note: FINRA does not offer any rationale for imposing a one year time limit for expungement arbitrations following stand-alone customer complaints.

**Comment**

- I find no fault in imposing a one year time limitation for seeking expungement relief after a customer arbitration closes without an Award (i.e., it settles) since the broker was either a party to the arbitration or had to be aware of it because his/her firm required assistance in defending the claims.
- However, from my experience, brokers can go years before they learn of a stand-alone customer complaint that had been denied by their firm (often their former firm, with which they have no contact) and not followed-up on by the customer.
- Such claims are denied by brokerage firms because it was determined that the claims had no merit. It is unfair to keep meritless claims permanently on a broker’s record and overly harsh to prevent brokers from seeking expungement relief of such claims when they learn of them.
- While some argument can be made that the six year eligibility rule<sup>9</sup> could apply to expungement claims as they do for all other claims, reducing them to one year from their denial by the brokerage firm – thus rendering nonarbitrable thousands of stand-alone customer complaints presently on broker records – is punitive in nature and anathema to the cornerstone of securities arbitration as an equitable forum for all parties.

**Question #6 - In Person or Videoconference Hearing**

**Question #6** - Should the associated person who is requesting expungement be required to appear in person or by videoconference, rather than by phone, at the expungement hearing?

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<sup>9</sup> See Rule 12206 and Rule 13206.

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**FINRA's Rationale** – “As the associated person is requesting the permanent removal of information from CRD, FINRA believes that the associated person should be available in person or by videoconference to present his or her case and respond to questions from the panel. Associated persons would also be required to attend expungement hearings in person, either by traveling to the hearing location or by videoconference, depending on the method permitted by the arbitration panel. Traveling to the hearing location could significantly increase the cost of having their request heard, by increasing both transportation and room and board costs as well as lost time in transit. Attendance by videoconference would eliminate many of these costs.”

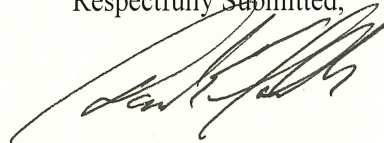
**Comment**

- In person hearings or videoconferencing are much preferred over a teleconferenced hearing, but it may simply not be possible to provide videoconferencing nationwide (or worldwide).
- In addition, since a broker is not seeking financial relief of any kind in an expungement arbitration, the burden of traveling to a remote location to be present at a hearing could very well discourage the broker from bringing a meritorious expungement case.
- I would suggest that the issue of in-person v. video conferenced v. teleconferenced hearings be determined by the arbitrators and not by the administrators (however well-mean they are). Let the enhanced panel of FINRA arbitrators decide what they need to come to a decision in the case.
- I have taken part in many teleconferenced expungement hearings that worked absolutely fine, with arbitrators able to ask all the questions they wanted and have those questioned answered as effectively as if the broker were in the room.

**Conclusion**

FINRA arbitration has long provided customers, brokers and firms with a full and fair opportunity to be heard, with equity as its cornerstone. My comments seek to preserve FINRA's respected and evolving alternative dispute resolution program.

Respectfully Submitted,



Good Morning Ms. Asquit:

As requested, the following are my thoughts on the proposed Expungement Rules Changes:

Please refer to the language below. I have been a FINRA arbitrator in good standing since early 1995 and have participated in countless hearings both as a Panel Member as the Chairperson. I have also participated in many Expungement Hearings as both a Panel Member and as Chair. I have provided the language for the Expungement Award not only when I have been the Chair, but also when the person acting as Chair had no idea of what to say. I am not a lawyer. Some of the individuals that I have provided language for have been. I think it is very unfair to place these requirements without grandfathering members that been providing this service for years. Perhaps, FINRA may want to provide a special training for Expungement Panel Members, as they do for Chairpersons. But to unilaterally exclude knowledgeable experience arbitrators that have been providing this service serves no purpose to anybody, to the contrary treats these arbitrators unfairly.

"III. Requests for Expungement of Customer Dispute Information Under the Industry Code and the Expungement Arbitrator Roster As explained above, if an expungement request is not decided during the Underlying Customer Case, the proposal would permit an associated person to file the expungement request as a new claim against the firm<sup>33</sup> at which he or she was associated at the time of the events giving rise to the customer dispute, provided the claim is not barred.<sup>34</sup> A three-person panel selected from the Expungement Arbitrator Roster would decide this new claim. A. Selection of Panel Under the proposal, the Neutral List Selection System<sup>35</sup> (NLSS) would randomly select three public chairpersons<sup>36</sup> from the Expungement Arbitrator Roster to decide an expungement request.<sup>37</sup> To be on the Expungement Arbitrator Roster, the public chairpersons would be required to have the following additional qualifications: (1) completed enhanced expungement training;<sup>38</sup> (2) admitted to practice law in at least one jurisdiction; and (3) five years' experience in any one of the following disciplines: (a) litigation; (b) federal or state securities regulation; (b) administrative law; (c) service as a securities regulator; or (d) service as a judge. The proposed changes to the expungement framework would help arbitrators on the Expungement Arbitrator Roster better understand the unique nature of this extraordinary remedy and the importance of maintaining the integrity of the public record. The proposed roster composition and the proposed additional requirements to grant expungement, taken together, should help FINRA maintain the integrity of its CRD records and ensure that expungement is only granted in appropriate circumstances."

Please consider my comments. I can be contacted at  
[drmegr@bellsouth.net](mailto:drmegr@bellsouth.net)  
(305) 238-7861

Thank you for your time,

Elena Rodriguez

Why are you contemplating unilaterally taking away my right to due process?  
If I had a meritless customer claim filed conveniently after I left a firm (which can happen), I will no longer have the opportunity to remove that information.  
If I had a customer have their claim denied or they withdrew it themselves because of a misunderstanding,  
I will no longer have the opportunity to remove that information.

What are you trying to accomplish?

***Virgil O. Rosser IV***  
***First Vice President - Investment Officer***  
***Certified Retirement Counselor***

***Wells Fargo Advisors***  
***9311 San Pedro***  
***Suite 1200***  
***San Antonio, TX 78216***



February 2, 2018

**By Electronic Mail** ([pubcom@finra.org](mailto:pubcom@finra.org))

Marcia E. Asquith  
Office of the Corporate Secretary  
Financial Industry Regulatory Authority (FINRA)  
1735 K Street, NW  
Washington, DC 20006-1506

**Re: Regulatory Notice 17-42: FINRA Requests Comments on Proposed Amendments to the Codes of Arbitration Procedure Relating to Requests to Expunge Customer Dispute Information**

Dear Ms. Asquith,

Thank you for the opportunity to submit these comments on the proposed amendments to the Financial Industry Regulatory Authority ("FINRA") Code of Arbitration Procedure for Customer Disputes, Rule 12000 Series (FINRA Rules 12100 and 12805) and Code of Arbitration Procedure for Industry Disputes, Rule 13000 Series (FINRA Rules 13805 and 13806) (the "Proposed Rules") on behalf of AdvisorLaw, LLC ("AdvisorLaw").

AdvisorLaw assists industry professionals in a variety of regulatory matters, and appreciates FINRA's continuous efforts to improve the financial services industry and protect the public by maintaining administrative, disciplinary and other useful information about registered persons in the Central Registration Depository ("CRD") system and making much of the same information publicly available through the FINRA BrokerCheck ("BrokerCheck") system.

As FINRA is aware, the efficacy of the CRD and BrokerCheck is greatly dependent on the timeliness and accuracy of the information provided therein. Further, to ensure the ongoing integrity of the CRD and BrokerCheck, both systems must continue to provide meaningful information to investors, employers and regulators. We applaud FINRA for the measures it has undertaken over the years to improve these systems, and for providing an avenue whereby inaccurate information may be either corrected through the filing of a BrokerCheck Dispute Form, or in the case of allegations made by customers, by way of expungement pursuant to FINRA Rule 2080.

FINRA has long-held the position that expungement of customer dispute information is an extraordinary measure, but it may be appropriate in certain circumstances. FINRA's historical position regarding expungements demonstrates FINRA's dedication to providing a system that not only protects the public, but one that is also equitable – recognizing the irreparable reputational and economic harm to registered persons who are falsely accused of sales practice violations. We are grateful to FINRA for advancing a well-thought-out proposal in efforts to

continue the pursuit of integrity and fairness in the CRD and BrokerCheck. In the spirit of partnering with FINRA for the overall improvement of the CRD and BrokerCheck, we offer the following comments for FINRA's consideration regarding the Proposed Rules.

### **1. Expungement Arbitrator Roster and the Neutral List Selection System ("NLSS")**

FINRA's proposal for the establishment of a roster of arbitrators with additional training and specific backgrounds and experiences to hear an associated person's request for expungement of customer dispute information is well aligned with the spirit of the Rules. Such a panel of arbitrators with enhanced expungement training would help improve the overall accuracy and preserve the integrity of the CRD and BrokerCheck by ensuring that only those customer allegations that meet the strict standards of FINRA Rule 2080 receive an arbitration award granting expungement of the allegations.

We also agree with FINRA's proposed requirements regarding additional qualifications of public arbitrators selected for expungement hearings, and ask FINRA to consider strengthening the qualifications to require selected arbitrators meet a minimum of five years' experience with the financial services industry. Requiring all expungement arbitrators to have a minimum of five years' experience with the financial services industry is appropriate considering the complexity of expungement requests in cases involving customer dispute information. Although we support additional training and relevant experience, we caution FINRA to not limit the roster of arbitrators to those who are admitted to practice law. FINRA's existing pool of public arbitrators is made up of very competent and capable arbitrators, many of whom have performed their arbitral duties with great care for several decades.

Finally, FINRA's proposal for the NLSS is reasonable considering the nature of expungement requests in cases involving customer dispute information. We also support Proposed Rules 13806(b)(4), (5) and (6) – allowing for removal of arbitrators for cause, requiring a randomly selected panel of three arbitrators and placing restrictions on the associated person's ability to withdraw the case once the panel has been selected. Proposed Rule 13806(b)(6) will create safeguards, and prevent an associated person from simply withdrawing their case and refiling in hopes of drawing a more favorable pool of randomly selected arbitrators.

### **2. Three-Person Panel and Unanimous Decision**

We are in agreement with FINRA's proposal for a three-person panel; however, we believe the requirement for a unanimous decision of the panel to grant expungement in cases involving customer dispute information places an undue burden on associated persons and chills the traditional notions of fairness and due process. We understand FINRA's position that expungement under Rule 2080 is an extraordinary remedy, but FINRA's own Rules concerning customer disputes allow rulings to be made by a majority of arbitrators. We are unaware of any other system of review that requires such a high bar. This is especially troubling considering the irreparable harm that a meritless complaint causes to an associated person's reputation and career.

### **3. Changing the Language in Rules 12805 and 13805 from “Grant” to “Recommend”**

We appreciate FINRA’s inquiry regarding the use of the word “grant” versus “recommend,” when referring to expungement awards involving customer dispute information. Using the correct language is especially important when considering that an arbitration panel’s decision must be confirmed by a court of competent jurisdiction. To that end, we believe retaining the original language as “grant” is appropriate.

It has long been established that the decisions made in arbitration are final and binding upon the parties, and may not be challenged except for extreme circumstances. The integrity of the arbitration system depends on this very notion, and must be preserved if arbitration is to serve as a viable alternative to the courts. Changing the language of the Rule from the word “grant” to “recommend” may lessen the perceived binding effect of the decision. The arbitration panel needs to be given full authority to hear a case requesting expungement, and make a binding decision. The requirement for post-hearing confirmation by a court of competent jurisdiction should serve as safeguard in those rare instances where a state court finds the harm to the public interest exceeds the binding decision of the panel. If the decision of the arbitration panel is limited to a mere “recommendation,” the legitimacy of the arbitration process may be compromised.

FINRA’s concerns regarding the post-hearing confirmation process may be easier addressed by way of expanded instruction to the courts, without the need to replace critical language in the rules or the risk of compromising to the authority of the arbitrators.

### **4. In-Person Appearance for Associated Persons**

We find FINRA’s Proposed Rules regarding in-person appearance by the associate person seeking expungement of customer dispute information to be unnecessarily burdensome, especially when considering the already high cost to associated persons when requesting expungement of meritless claims against them. The decision whether to hold a hearing telephonically, by video or in-person should be left with the arbitration panel.

### **5. Bifurcation of Expungement Hearing from the Customer’s Claim in Cases Involving Customer Disputes**

Current FINRA Rules 12805 and 13805 do not provide any guidance as to how and when an associated person may request expungement of customer dispute information. Therefore, an associated person currently has the option to request expungement during the Underlying Customer Case whether or not the associated person is named, or the request for expungement can come in the form of a separate Rule 2080 hearing. The Proposed Rules provide additional guidelines and clearly define how and when an associated person may seek expungement; however, in doing so the Proposed Rules also create an inherent disparity between expungement requests brought under the Proposed Rule 12805 and 13805.

The disclosure of an alleged sales practice violation can have a crippling effect on an associated person's career – limiting their ability to earn business or seek employment. Such effects, although severe, are appropriate where the customer allegations are accurate. There are, however, many instances where the customer allegations are without merit, and FINRA's Rules pertaining to expungement of such disclosures must provide associated persons with an honest and impartial review process.

*a. Access to Special Expungement Arbitrator Roster Under Proposed Rule 13806*

FINRA's proposal for the establishment of a Special Expungement Arbitrator Roster is a welcomed step to help preserve the integrity of the CRD and BrokerCheck. As FINRA is well aware, expungement of customer dispute information is an extreme remedy, which is only appropriate pursuant to FINRA Rule 2080 if the claim or allegation is factually impossible, clearly erroneous or false, or if the associated person was not involved in the alleged investment related sales practice violation.

FINRA's Proposed Rules, if implemented, would obligate an associated person who is named in the Underlying Customer Case to request expungement within the underlying case or be prohibited from seeking to expunge the customer dispute information arising from the customer's statement of claim during any subsequent proceeding. Yet doing so means a request for expungement brought within the Underlying Customer Case would not be placed before an arbitration panel comprised of the Special Expungement Arbitrator Roster. This creates an inherent disparity in the effect of the Proposed Rules, and would unfairly prejudice both the Customer and the associated person. In cases where the Customer was genuinely harmed by a sales practice violation, an expungement of the customer dispute information is not appropriate, and a request to have such information expunged should receive the same level of review and consideration by a specially trained arbitration panel as would be the case in other expungement requests pursuant to Proposed Rule 13805. Conversely, where the customer dispute information is without merit and expungement is appropriate pursuant to FINRA Rule 2080, the associated person should also be afforded the same opportunity to be heard before a specially trained arbitration panel. It should also be noted that the same concerns apply where the associated person is not named in the Underlying Customer Case, but a named party requests expungement on behalf of the unnamed person.

To remedy this inherent disparity, FINRA must either prohibit an associated person's request for expungement from being heard in the Underlying Customer Case, or create a mechanism by which such a request is heard by a panel of specially trained arbitrators from Special Expungement Arbitrator Roster. The former is easily achieved through bifurcation of the Underlying Customer Case and expungement cases brought pursuant to FINRA Rule 2080. The latter, however, is somewhat problematic. To allow both the Underlying Customer Case and the request for expungement to proceed within the same case, and avoid the inherent disparities discussed above, FINRA would need to adopt rules requiring that all Underlying Customer Cases where a request for expungement is made be heard by a panel of specially trained arbitrators. The same rules regarding the random selection of the arbitrators via the NLSS would also have

to apply, but doing so would deny all parties in the Underlying Customer Case from the ability to strategically rank or strike specific arbitrators from the panel. Under the latter approach, one disparity is resolved at the expense of creating another. We therefore urge FINRA to consider revising the Proposed Rules and force all FINRA Rule 2080 expungement hearings to be heard pursuant to Proposed Rule 13805.

*b. Potential for Bias Imputed onto Associated Person Due to Actions of Member Firm*

The Proposed Rules obligating associated persons to join their request for expungement when named in the Underlying Customer Case may also create an environment where wrongdoing on behalf of the member firm is imputed onto the associated person. This is especially concerning since associated persons are often not represented by independent counsel in such hearings, and when considering the severity of harm to the associated person if a request for expungement is denied unfairly. A bifurcation of the Underlying Customer Case from the expungement request will provide the associated person an opportunity to have their request heard by an impartial panel of specially trained arbitrators.

*c. Conflict of Interest Where a Member Firm Requests Expungement on Behalf of an Associated Person Not Named as a Respondent in the Underlying Customer Case*

The Proposed Rules, if implemented, will allow a member firm the ability to request expungement on behalf of an associated person who is otherwise not named in the Underlying Customer Case. We respectfully ask FINRA to reconsider this approach and instead prohibit the practice entirely, as there is too great of a potential for conflict of interest in co-representation.

In cases involving customer disputes with the member firm, counsel for the member firm is obligated to represent the best interest of their client. Yet those interests are rarely aligned with the interests of the associated person, and therefore there is inherent conflict. This conflict is heightened further by the fact that counsel for the member firm may have a considerable monetary incentive for maintaining a healthy relationship with the member firm – since counsel most likely represents the member firm regularly. The concern for such conflict of interest is so great in the legal community that Rule 1.7(a)(2) of the Model Rules of Professional Conduct (as well as most, if not all, state rules pertaining to professional conduct) prohibit co-representation of parties where “there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.”

Rule 1.8(b) of the Model Rules of Professional Conduct also state that “a lawyer shall not use information relating to representation of a client to the disadvantage of the client unless the client gives informed consent.” The starting point in this rule is the consideration that counsel should not use any information relating to the representation of a client to the client’s disadvantage. The rule creates a caveat where the client has given informed consent; however, we question the authenticity of such informed consent in cases where the associated person is currently employed by the member firm and likely has incentive to remain employed and in good standing. Further, such “consent” may be compromised in the likely scenario where the member

firm is providing financial assistance for the legal representation, as the associated person may agree under financial duress. The potential for financial duress, and the compromise of representation due to conflict is enough of a concern that the Model Rules of Professional Conduct specifically address the issue in Rule 1.8(f) stating: “A lawyer shall not accept compensation for representing a client from one other than the client.” Rule 1.8(f) does provide some exceptions; however, when considering the disproportionate allegiance that counsel may have to the member firm as well as other ethical considerations, we believe a conflict of interest is simply unavoidable.

## **6. Time Limitation Period for Associated Persons to Expunge Customer Dispute Information**

The Proposed Rules require that an associated person seek expungement of the customer dispute information relating to a costumer complaint within one year of the member firm initially reporting the customer complaint if the complaint does not result in an arbitration claim, or within one year after the Underlying Customer Case closes either through a binding decision of the arbitrators or settlement between the parties. In support of the Proposed Rules, FINRA represents that given the length of time currently between the initial complaint or the case closure, and filing of the request for expungement, the customers and relevant documentation cannot be located.

We respectfully challenge the Proposed Rules, and draw FINRA’s attention to its own Rule 4511, which requires members to preserve books and records for a minimum of six years. We also note that while this is the absolute minimum retention period, many member firms retain books and records for far longer periods, and some simply do not destroy any books and records regardless of time passed. Barring an exceedingly rare circumstance (*e.g.*, the collapse of Tower 7 World Trade Center in the September 11 attacks), it is highly unlikely that relevant documents will not be available for at least the minimum required retention period.

When considering the fact that all of the relevant documentation is readily available during the requisite six-year retention period, and the availability of numerous online public records, an associated person’s counsel or FINRA should have no difficulty locating the customers. In the seven hundred plus customer dispute disclosures that we have brought before FINRA for expungement, finding the customer has very rarely been an issue. The more common scenario, in fact, is that once the customer is reached they show little to no interest in opposing the associated person’s request for expungement – often citing one of three reasons for their lack of interest: (a) they never intended their complaint against the associated person; (b) they have since been made whole or the perceived loss of value in their investment at the time of the complaint resulted from volatility in the market and their investments have since recouped; or (c) they are not interested in participating unless there is a monetary incentive.

Based on the above, we urge FINRA to reconsider the one-year period in the Proposed Rules, and instead allow associated persons six years in which to bring a case for expungement pursuant to FINRA Rule 2080. Further, in the Proposed Rules, FINRA suggests reducing the time period from one year to six months in all cases where the customer case closes on or prior

to the effective date of the Proposed Rules. Yet FINRA offers no support for this proposed six-month time frame, which not only appears to be completely arbitrary but also plainly creates an unjustifiable distinction between cases that close prior to the rules and those that close after. We therefore ask FINRA to consider either grandfathering all cases that close prior to the effective date of the Proposed Rules without any time limit, or in the alternative, apply the same time limitation to those cases as the ones that close after the effective date of the Proposed Rules.

## **7. Incorporation of Public Petition**

To ensure a fair representation of industry person's regarding these Proposed Rules, we circulated an online petition and wish to incorporate all signatories and comments here. The online petition may be found here: <https://www.ipetitions.com/petition/fighting-for-a-balanced-finra-expungement-process#comments>

Once again, AdvisorLaw thanks you for the opportunity to submit these comments. If there is any further information or other assistance that we may be able to provide, or if there are any questions we may be able to answer, please contact me at [armin@advisorlawyer.com](mailto:armin@advisorlawyer.com) or 720-549-2880.

Respectfully,

A handwritten signature in black ink, appearing to read 'A. Sarabi'.

Armin Sarabi  
Senior Attorney  
AdvisorLaw, LLC



February 5, 2018

**Jonathan M. Sterling**  
jsterling@saretsky.com

VIA EMAIL AND FEDERAL EXPRESS

Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

Re: Comments on FINRA's Proposed Amendments to its Expungement  
Arbitration Rules (Regulatory Notice 17-42)

Dear Ms. Asquith:

Below please find our comments on FINRA's proposed rule changes to the expungement process. We respectfully request that these comments be given careful consideration by FINRA.

Our comments are based on representing parties to FINRA arbitrations for many years. We have substantial experience in handling expungement proceedings. Although FINRA believes the amendments will further promote investor protection and regulatory value considerations, we cannot agree. Instead, we believe the proposed rules are inequitable, and instead have the effect of placing unnecessary and unfairly harsh, costly and unwarranted burdens on associated persons trying to recapture their business reputation. Our specific comments follow.

**Expungement Requests Regarding an Underlying Customer Case  
Where the Associated Person is Named**

**Rule Change:** An associated person is required to request expungement during an underlying customer case where he/she is named as a party.

**FINRA's Rationale:** Years after FINRA has closed an underlying customer case, a broker files a separate expungement request. "[I]n many of these instances, the customers cannot be located and any documentation that could explain what happened in the case is not available or cannot be located." Notice 17-42, p. 5.



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**Comment:** In all of our many expungement actions, we have yet to encounter a situation in which a customer could not be located. The overwhelming majority of customers are represented by counsel, who are able to offer the customer's most recent contact information. Modern techniques to locate people (such as the internet's many people finder sites) make searches easy, efficient and economical.

The concern that important documentary evidence will not be available is not legitimate. Even ignoring the likelihood that a customer and/or his/her attorney retained relevant records beyond the arbitration hearing itself, governing securities industry rules mandate the retention of important customer and account records for several years. If the unavailability of documents and records truly threatened the integrity of the arbitration process, surely FINRA Rule 12504(a)(6) would allow arbitrators to consider pre-hearing motions to dismiss on the grounds that a claim was brought beyond the record retention requirement (and, in many cases, the co-extensive time frame imposed by the eligibility rule), and important documents are no longer available. Arbitrators are well able to determine whether an expungement request is adequately supported and a rule change which forces premature consideration of expungement is ill-advised.

**Rule Change:** The filing fee is \$1,425 or the applicable filing fee provided in Rule 12900(a)(1), whichever is greater.

**FINRA's Rationale:** Associated persons have been adding a monetary claim of less than \$1,000 to reduce the filing fee to \$50. This results in a simplified claim where only one arbitrator would hear and consider a "complex matter" like expungement. Notice 17-42, fn 14.

**Comment:** The filing fee an associated person pays in connection with an expungement request has no bearing on whether the arbitrators will grant his/her request. Raising the filing fee fails to acknowledge that an associated person has inevitably suffered indirect financial harm merely due to the negative notation on their CRD. Arbitrators retain the right to assess costs in connection with an expungement request, and the assessment of costs should be reserved until the arbitrators have heard and considered all of the evidence.

Further, FINRA's concern with having only one arbitrator decide an expungement request is a red herring. If FINRA believes its arbitrators are properly trained and competent to hear and decide full cases in simplified arbitration proceedings, surely arbitrators are well able to consider expungement, a corollary request. And, if one arbitrator, alone, is unable to understand an ostensibly "complex matter" like expungement, how does the inclusion of two additional arbitrators (presumably also unable to understand the issues on their own) enhance the decision-making process?



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**Rule Change:** If a customer case closes by award, the panel must consider and decide the expungement request and “unanimously grant expungement”. The award must identify at least one of the grounds under Rule 2080 and find that “the customer dispute information has no investor protection or regulatory value.” Notice 17-42, p. 6

**FINRA’s Rationale:** “The proposal would clarify for arbitrators that the standard for granting the permanent removal of customer dispute information from the CRD is a finding that the customer dispute information has no investor protection or regulatory value.” Notice 17-42, p. 9

**Comment:** FINRA already cautions arbitrators that expungement is an “extraordinary” remedy that should only be granted in the limited circumstances provided under Rule 2080. In fact, FINRA acknowledges that its previous efforts (establishing Rule 12805 and publishing the Expanded Guidelines) have improved the expungement process.<sup>1</sup> That cautionary language is adequate to inform arbitrators as to a moving party’s burden.

Imposing a “no investor protection or regulatory value” standard is absolute, subjective and excessive. The “extraordinary” remedy language should be balanced by permitting arbitrators to grant expungement if they conclude the customer dispute language has no **reasonable** investor protection or regulatory value. Such an objective standard is in keeping with the equitable nature of the forum.

FINRA prides itself on being an equitable forum. Equitable means fair or just. Permitting customer cases to be decided by a majority, but requiring a unanimous ruling as to expungement requests is contradictory to that ethos. There is absolutely no reason why a customer’s complaint, which can result in an award of hundreds of thousands or millions of dollars, can be decided by only two arbitrators, but an expungement request must be granted by three.

Unanimity simply creates an unjust and unfair hurdle. Beyond the world of FINRA Arbitration, other important decisions do not require unanimity. Civil jury verdicts need not be unanimous; appellate decisions, including the United States Supreme Court, need not be unanimous; and legislators do not require unanimity.

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<sup>1</sup> “Based on FINRA’s review of awards where expungement has been granted, arbitrators appear to be following the practices identified in the Expanded Guidelines and have a heightened awareness that expungement is an extraordinary remedy. FINRA has noticed a marked improvement in the quality of the awards in which expungement is granted.” Notice 17-42, p. 10.



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**Rule Change:** If a customer case closes other than by award (i.e., settlement), the associated person must file a new expungement request against the firm he/she was associated with at the time of the underlying events. The associated person cannot name the customer in the request.

**FINRA's Rationale:** The customer should not be asked to participate in another arbitration hearing that could increase their costs/expenses. Instead, naming the firm is intended to allow a "more robust expungement proceeding". Notice 17-42, p. 6.

**Comment:** Customers are free to participate in expungement proceedings, but are not required to do so. Customers should be free to assess themselves the relative costs and benefits of participating. In most cases, a customer who elects to participate will devote all of approximately one hour on a telephone conference call during which the expungement request is being formally presented. In contrast, the associated person has already suffered a negative notation on their CRD merely due to the assertion of the customer's claim, and expended many months of time and thousands of dollars on attorneys' fees and costs defending a claim he/she believes was without merit. In an equitable world, the balance of harm to the associated person is far greater than the minor inconvenience suffered by the customer – who voluntarily initiated the dispute in the first place.

Allegations of wrongdoing made by a customer against an associated person are serious indeed. In most FINRA arbitrations, fraud and breach of fiduciary duty are routinely pled. Accountability for these allegations is basic to any true system of justice. The ability to allege with impunity, and to avoid accountability for one's accusations, is antithetical to any system seeking to do justice. An aggrieved associated person should be able to name the customer; a truly "robust" expungement proceeding would not mandate the exclusion of the underlying complainant from the process.

**Rule Change:** If a customer case closes other than by award (i.e., settlement), the associated person must seek expungement within one year. If there is no underlying customer case, the associated person must file an expungement request within one year from the date the member firm initially reported the customer complaint to CRD.

**FINRA's Rationale:** The one-year limitation period would ensure that the expungement hearing is held close in time to the underlying case when information is available and the customer's participation in the expungement proceeding is more likely.

**Comment:** FINRA allows customers to file claims up to six years after the occurrence or event giving rise to a dispute but wants to limit an associated person's ability to remedy a perceived meritless claim on their record. There is



Marcia E. Asquith  
February 5, 2018  
Page 5

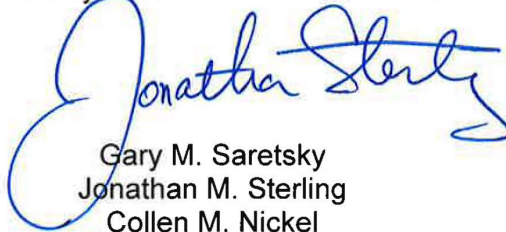
nothing equitable about this. As explained above, arbitrators are capable of determining if an expungement request lacks sufficient documentary support or whether the absence of a customer's testimony should weigh against granting the request. Thus, a restrictive time limit is unnecessary to hold an effective expungement hearing. And, the safeguards to investors afforded through the CRD system are not advanced by a time limit. The longer an associated person waits to seek expungement, the longer a negative CRD notation survives in the public domain. Arbitrators are free to weigh the evidentiary value (if any) of an associated person's undue delay in this regard. Further, FINRA already requires that customers be notified of any expungement request. Thus, customers are always afforded the opportunity to participate in expungement hearings or oppose the request. A time limit does not change this reality.

### Conclusion

Protecting customers is important, but the cornerstone of FINRA arbitration is equity. Equity works both ways. The proposed amendments seem to suggest that FINRA does not fully value the concerns of members of the financial services industry as to the fairness of the expungement process. As a result, we ask FINRA to reconsider the proposed rule amendments.

Very truly yours,

Saretsky Hart Michaels + Gould PC



Gary M. Saretsky  
Jonathan M. Sterling  
Collen M. Nickel

JMS/nah

THE LAW OFFICE OF DANIEL SCHLEIN

800 THIRD AVENUE  
SUITE 2800  
NEW YORK, NEW YORK 10022

TEL: (212) 220-4070

dschleinlaw@gmail.com

FAX: (646) 219-1500

February 3, 2018

**Via Email and Regular Mail**

Ken Andrichik, Esq.  
Senior Vice President  
FINRA  
One Liberty Plaza  
New York, New York 10006

Dear Mr. Andrichik:

As a FINRA arbitrator, I would like to contribute comments on the proposed amendments to the Code of Arbitration Procedure relating to requests to expunge customer dispute information as described in Regulatory Notice 17-42.

It is my understanding that the proposed amendments allow an associated person who is named as a party to file a new claim for expungement within one year after the underlying customer case closes in a manner other than by award. Despite the one-year limitation on filing expungement claims after a case closes in a manner other than by award, associated persons and their counsel may decide in many situations that it is strategically advantageous to pursue settlement in the underlying case and subsequently file for expungement with the expectation that a panel unfamiliar with the case may be more inclined to grant the request. In this fashion, the proposed amendments may have the ancillary and arguably salutary effect of increasing incentives to seek settlement. In a subsequent expungement proceeding, however, the panel might need to base its decision primarily on information the associated person provides. By requiring panels to decide whether expungement is appropriate without the benefits of an adversarial proceeding, the proposed amendments may not readily accomplish their purpose in curbing unwarranted orders for expungement.

While I note that the proposed amendments provide that an associated person filing for expungement would be required to name the firm at which he or she was associated at the time of the events giving rise to the customer dispute, it is not clear how this provision promotes the robust proceedings FINRA envisages. For example, if an associated person decides to leave his or her employer prior to the expungement proceeding or is terminated, the firm may have little or no economic incentive to cooperate in an expungement proceeding. It would also be difficult for the panel to elicit potentially

relevant facts bearing on an expungement request where the economic and reputational interests of the associated person and the employer are aligned, including situations in which the associated person's firm assisted in the associated person's defense in the underlying customer dispute.

It is also clear that an aggrieved customer has no economic incentive to participate in an expungement proceeding that occurs only after the underlying case has concluded. A short filing period undoubtedly would tend to improve the reliability of testimony and increase witness availability. On the other hand, imposing a one-year limitation period for associated persons to file a new claim for expungement does not alter the economic disincentive for the customer to participate in a separate expungement proceeding. FINRA understandably seeks to avoid imposing additional costs upon customers. The proposed amendments could have the unfortunate effect of denying an expungement panel the opportunity to hear directly from the aggrieved customer whose participation could help illuminate the context in which the expungement request arises in significant ways. In this respect, the amendments do not comprehensively meet the concerns of critics of expungement who have raised concern about panels that receive only one-sided information in favor of the associated person seeking expungement.

The extent to which limited information may affect the quality of decisionmaking is particularly important given the fact that in a separate expungement proceeding no party would advocate on behalf of the interests of the investing public or the integrity of the regulatory system. While FINRA's rules do not provide a role for a public advocate in customer disputes either, panelists in that context have the benefit of receiving opposing viewpoints and evidence in an adversarial proceeding.

FINRA could ameliorate the possibility that a panel might receive one-sided information in several ways. For example, where an associated person exercises his or her right to seek expungement within one year after the underlying customer dispute closes other than by award, it would be beneficial for FINRA to provide the expungement panel with significant filings from the underlying customer dispute, including the Statement of Claim, the Answer and dispositive motions. The panel might also be permitted the opportunity to review the parties' settlement papers in the underlying customer dispute to examine the amount paid to any party and any other terms and conditions of the settlement as Rule 12805 and Rule 13805 of the FINRA Code of Arbitration Procedure presently requires for requests for expungement relief raised in the underlying customer dispute under Rule 2130. The associated person, the firm and the customer could also be given the right to provide the panel with transcripts of the underlying customer proceeding.

I note further that under the proposed amendments, a customer may appear in person or by phone. To promote customer participation, FINRA should consider requiring the associated member to bear the cost of the customer's attendance if the customer wishes to participate in person. Requiring the associated person to bear the cost of the customer's attendance at the proceeding would encourage customers to participate. It would also reduce the incentive of associated persons to seek expungement requests by increasing

their costs and reduce the number of meritless requests for relief. So, too, would requiring associated persons to present their case in person rather than by phone or videoconference.

By incorporating one of more of these features into the procedures for expungement proceedings, panels would be more likely to have information useful in facilitating their ability to render informed judgments concerning the propriety of expungement.

I am also concerned about the efficacy of referring an expungement request to a special panel regardless of the stage at which the underlying customer case settles. If the underlying case settles early, such as when the panel chair has only considered discovery issues and the panel as a whole has not had an opportunity to delve into the case in detail, it would be sensible to send an expungement request to a specialized panel. At the other end of the spectrum is the case that settles only on the eve of hearings, by which time the panel in the underlying customer dispute would presumably have thoroughly reviewed the parties' prehearing briefs and exhibits. In that circumstance it may well be both efficient and effective in promoting investor protection to require the panel presiding over the underlying customer dispute to decide the expungement request as well.

Turning to the qualifications of the expungement panelists, I note that FINRA proposes to create a roster of public chairpersons who are attorneys with at least five years of litigation or related experience and who have already completed chairperson training. I support the appointment of experienced attorneys to the Expungement Arbitration Roster. Attorneys with litigation training and experience are proficient in identifying legal issues, weighing the relevancy of proffered evidence and judging the credibility of witnesses. The appointment of panelists who possess those qualities will effectuate the purpose of the amendments in promoting the likelihood that expungement requests are granted only where appropriate.

The proposed amendments, however, do not provide a clear legal standard for how expungement arbitrators should evaluate expungement requests. At present, a panel must identify at least one basis for expungement under Rule 2080(b)(1) before granting an associated person's request for relief. The proposal would add a second requirement that the panel make a specific finding that "the customer dispute information contains no investor protection or regulatory value." This new requirement is problematic since many arbitrators who are lawyers have specialties that do not touch upon securities law. Even attorneys who have worked in the securities field may be long retired from the financial industry. Arbitrators who serve on the Expungement Arbitration Roster should therefore receive supplemental training on the proposed new standard to help them fulfill their responsibilities. Because associated persons would still be required to confirm an expungement award in a court of competent jurisdiction I, I suggest that FINRA offer training or instructional materials to judges as well.

I hope these comments are helpful. Please feel free to contact me with any questions.

Sincerely,

A handwritten signature in blue ink, appearing to read "Daniel Schlein", with a stylized flourish at the end.

DANIEL A. SCHLEIN

Why should the expungement process cost many thousands of dollars to remove meritless claims and now you are proposing making that more difficult or impossible? Frivolous claims on an advisor CRD can ruin a career, please reconsider.

Thank you

Gregory Scrydloff, CFP  
National Securities

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WELLINGTON SHIELDS & CO. LLC  
MEMBER NEW YORK STOCK EXCHANGE  
140 BROADWAY  
NEW YORK, NY 10005

TEL: (212) 732-6800



TEL: (212) 320-3000  
FAX: (212) 320-3040

**Comments Regarding Expungement of Customer Dispute Reg. Notice 17-42  
and Other Issues Related to Arbitration**

February 1, 2018

Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington DC, 20006-1506

Dear Ms. Asquith,

This is an informal comment letter on proposals to the Expungement Rule. In two recent FINRA arbitration cases (attached), Wellington Shields & Co., LLC has been exonerated. In both cases claimant's claims have all been denied and in both cases expungement had been "recommended".

Expungement Process

In the first case, Omega (case #14-02852), expungement proceedings cost the firm \$4,000 in costs and attorney's fees. In the second case, Morello (case #16-02878), expungement is not yet completed but has been accrued at \$5,000. There should be a procedure for FINRA to keep expungement "in house" and streamlined. At the same time FINRA should have a review process in place to confirm the appropriateness of the recommendation. There should be little or no cost to the parties that receive a unanimous "recommendation" of expungement. The cost of going into court and keeping FINRA up to date as well as getting permission from the plaintiff is onerous and when you have been vindicated it is extremely unfair.

Grant

If an expungement is endorsed unanimously, the term "grant" should be retained and honored by FINRA except in rare circumstances cited by FINRA. This would eliminate the need to go to court.

Attorney's Fees

In both the cited cases, Wellington Shields & Co. attorney's fees were denied. It is my understanding that while there is no rule regarding the award of fees by FINRA, it is customary that arbitration panels do not award fees. Panelists have told me they do not do award fees because they will not be chosen to serve again. This is a serious and unfair practice in the FINRA Arbitration system and should be addressed.

Reducing Frivolous Arbitrations

The risk of charging fees against a plaintiff will surely diminish unfounded claims. For example, the two cases previously cited, probably would never have come to arbitration if there had been a risk that the plaintiff would have to pay fees.

Respectfully submitted,



David V. Shields  
Chief Executive Officer

Enclosures:   Omega – case #14-02852  
                  Morello – case #16-02878

**Award**  
**FINRA Office of Dispute Resolution**

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In the Matter of the Arbitration Between:

Claimants  
Anthony Morello  
Donna Morello

Case Number: 16-02878

vs.

Respondent  
Wellington Shields & Co., LLC

Hearing Site: Newark, New Jersey

---

Nature of the Dispute: Customers vs. Member

This case was decided by an all-public panel.

**REPRESENTATION OF PARTIES**

For Claimants Anthony Morello, and Donna Morello: Ross B. Intelisano, Esq. and Jessica Murzyn, Esq., Rich, Intelisano & Katz, LLP, New York, New York.

For Respondent Wellington Shields & Co., LLC: Neil A. Sussman, Esq., Sussman & Frankel, LLP, New York, New York.

**CASE INFORMATION**

Statement of Claim filed on or about: September 29, 2016.  
Donna Morello signed the Submission Agreement: August 31, 2016.  
Anthony Morello signed the Submission Agreement: August 31, 2016.

Statement of Answer filed by Respondent on or about: January 13, 2017.  
Wellington Shields & Co., LLC signed the Submission Agreement: January 9, 2017.

**CASE SUMMARY**

Claimants asserted the following causes of action: breach of applicable securities laws, statutes, rules, regulations, and standards of conduct; common law fraud; misrepresentations and material omissions; breach of fiduciary duty; breach of contract; breach of implied covenant of good faith and fair dealing; negligence; negligent misrepresentation; failure to supervise; and respondeat superior.

Unless specifically admitted in the Statement of Answer, Respondent denied the allegations made in the Statement of Claim and asserted various affirmative defenses.

FINRA Office of Dispute Resolution  
Arbitration No. 16-02878  
Award Page 2 of 5

### **RELIEF REQUESTED**

In the Statement of Claim, Claimants requested compensatory damages in excess of \$113,000.01, attorneys' fees and costs.

In the Statement of Answer, Respondent requested that the Panel render an award:

- a) dismissing the Statement of Claim with prejudice;
- b) recommending expungement from both Respondent and unnamed party Pamela Taylor's CRD records;
- c) imposing forum fees on Claimants; and
- d) granting such other and further relief as appears just and appropriate.

At the close of the hearing, Claimants withdrew their claim for unsuitability and requested compensatory damages in the amount of \$92,392.16.

### **OTHER ISSUES CONSIDERED AND DECIDED**

The Arbitrators acknowledge that they have each read the pleadings and other materials filed by the parties.

The Claimants participated in the expungement hearing and contested Respondent's request for expungement.

In recommending expungement the Panel relied upon the following documentary or other evidence: Claimants' Statement of Claim, Respondent's Statement of Answer, Respondent and unnamed party Pamela Taylor's BrokerCheck® Reports, and the testimony and evidence presented at the hearing.

The Panel made no determination in connection with Respondent's request for expungement since the above-captioned arbitration is not reflected on Respondent's registration records maintained by the Central Registration Depository ("CRD").

The Panel noted that unnamed party Pamela Taylor did not previously file a claim requesting expungement of the same disclosure in the CRD.

The parties present at the hearing have agreed that the Award in this matter may be executed in counterpart copies or that a handwritten, signed Award may be entered.

### **AWARD**

After considering the pleadings, the testimony and evidence presented at the recorded hearing, the Panel has decided in full and final resolution of the issues submitted for determination as follows:

1. Claimants' claims are denied in their entirety.

FINRA Office of Dispute Resolution  
Arbitration No. 16-02878  
Award Page 3 of 5

2. The Panel recommends the expungement of all references to the above-captioned arbitration from registration records maintained by the Central Registration Depository ("CRD"), for unnamed party Pamela Taylor (CRD# 2255299), with the understanding that, pursuant to Notice to Members 04-16, unnamed party Pamela Taylor must obtain confirmation from a court of competent jurisdiction before the CRD will execute the expungement directive.

Unless specifically waived in writing by FINRA, parties seeking judicial confirmation of an arbitration award containing expungement relief must name FINRA as an additional party and serve FINRA with all appropriate documents.

Pursuant to Rule 12805 of the Code, the Panel has made the following Rule 2080 affirmative finding of fact:

The claim, allegation, or information is factually impossible or clearly erroneous.

The Panel has made the above Rule 2080 finding based on the following reasons:

No documentary or testamentary evidence was presented by Claimants to prove their claims. Moreover, Claimants' withdrawal of their suitability claim shows that Claimants have insufficient grounds to prove their claim.

3. Any and all claims for relief not specifically addressed herein, including attorneys' fees and costs, are denied.

### **FEES**

Pursuant to the Code of Arbitration Procedure, the following fees are assessed:

#### **Filing Fees**

FINRA Office of Dispute Resolution assessed a filing fee\* for each claim:

|                          |               |
|--------------------------|---------------|
| Initial Claim Filing Fee | = \$ 1,425.00 |
|--------------------------|---------------|

*\*The filing fee is made up of a non-refundable and a refundable portion.*

#### **Member Fees**

Member fees are assessed to each member firm that is a party in these proceedings or to the member firm that employed the associated person at the time of the events giving rise to the dispute. Accordingly, as a party, Wellington Shields & Co. LLC is assessed the following:

|                    |               |
|--------------------|---------------|
| Member Surcharge   | = \$ 1,700.00 |
| Member Process Fee | = \$ 3,250.00 |

FINRA Office of Dispute Resolution  
 Arbitration No. 16-02878  
Award Page 4 of 5

**Discovery-Related Motion Fee**

Fees apply for each decision rendered on a discovery-related motion.

Two (2) decisions on discovery-related motions on the papers  
 with one (1) arbitrator @ \$200.00/decision =\$ 400.00

Claimants submitted one (1) discovery-related motion  
 Respondent submitted one (1) discovery-related motion

---

Total Discovery-Related Motion Fees =\$ 400.00

The Panel has assessed \$200.00 of the discovery-related motion fees jointly and severally to Claimants.

The Panel has assessed \$200.00 of the discovery-related motion fees to Respondent.

**Hearing Session Fees and Assessments**

The Panel has assessed hearing session fees for each session conducted. A session is any meeting between the parties and the arbitrators, including a pre-hearing conference with the arbitrators, that lasts four (4) hours or less. Fees associated with these proceedings are:

One (1) pre-hearing session with a single arbitrator @ \$450.00/session =\$ 450.00  
 Pre-hearing conference: August 9, 2017 1 session

One (1) pre-hearing session with the panel @ \$1,125.00/session =\$ 1,125.00  
 Pre-hearing conference: March 14, 2017 1 session

Six (6) hearing sessions @ \$1,125.00/session =\$ 6,750.00  
 Hearing Dates: November 1, 2017 2 sessions  
 November 2, 2017 2 sessions  
 November 3, 2017 2 sessions

---

Total Hearing Session Fees =\$ 8,325.00

The Panel has assessed \$4,162.50 of the hearing session fees jointly and severally to Claimants.

The Panel has assessed \$4,162.50 of the hearing session fees to Respondent.

All balances are payable to FINRA Office of Dispute Resolution and are due upon receipt.


FINRA Office of Dispute Resolution  
Arbitration No. 16-02878  
Award Page 5 of 5

**ARBITRATION PANEL**

|                     |   |  |
|---------------------|---|--|
| Martin R. Cramer    | - | Public Arbitrator, Presiding Chairperson |
| Catherine Stewart   | - | Public Arbitrator                        |
| Peter L. Michaelson | - | Public Arbitrator                        |

I, the undersigned Arbitrator, do hereby affirm that I am the individual described herein and who executed this instrument which is my award.

**Concurring Arbitrators' Signatures**

  
\_\_\_\_\_  
Martin R. Cramer  
Public Arbitrator, Presiding Chairperson

12/14/2017  
\_\_\_\_\_  
Signature Date

\_\_\_\_\_  
Catherine Stewart  
Public Arbitrator

\_\_\_\_\_  
Signature Date

\_\_\_\_\_  
Peter L. Michaelson  
Public Arbitrator

\_\_\_\_\_  
Signature Date

December 14, 2017

Date of Service (For FINRA Office of Dispute Resolution office use only)

FINRA Office of Dispute Resolution  
Arbitration No. 16-02878  
Award Page 5 of 5

**ARBITRATION PANEL**

|                     |   |  |
|---------------------|---|--|
| Martin R. Cramer    | - | Public Arbitrator, Presiding Chairperson |
| Catherine Stewart   | - | Public Arbitrator                        |
| Peter L. Michaelson | - | Public Arbitrator                        |

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**Concurring Arbitrators' Signatures**

\_\_\_\_\_  
Martin R. Cramer  
Public Arbitrator, Presiding Chairperson

\_\_\_\_\_  
Signature Date

  
\_\_\_\_\_  
Catherine Stewart  
Public Arbitrator

12/14/2017  
\_\_\_\_\_  
Signature Date

December 14, 2017  
\_\_\_\_\_  
Peter L. Michaelson  
Public Arbitrator

\_\_\_\_\_  
Signature Date

\_\_\_\_\_  
Date of Service (For FINRA Office of Dispute Resolution office use only)

FINRA Office of Dispute Resolution  
Arbitration No. 16-02878  
Award Page 5 of 5

**ARBITRATION PANEL**

|                     |   |  |
|---------------------|---|--|
| Martin R. Cramer    | - | Public Arbitrator, Presiding Chairperson |
| Catherine Stewart   | - | Public Arbitrator                        |
| Peter L. Michaelson | - | Public Arbitrator                        |

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**Concurring Arbitrators' Signatures**

\_\_\_\_\_  
Martin R. Cramer  
Public Arbitrator, Presiding Chairperson

\_\_\_\_\_  
Signature Date

\_\_\_\_\_  
Catherine Stewart  
Public Arbitrator

\_\_\_\_\_  
Signature Date

  
\_\_\_\_\_  
Peter L. Michaelson  
Public Arbitrator

  
\_\_\_\_\_  
Signature Date

December 14, 2017  
Date of Service (For FINRA Office of Dispute Resolution office use only)

**Award**  
**FINRA Office of Dispute Resolution**

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In the Matter of the Arbitration Between:

Claimant  
Omega Facility Services, Solutions & Surety, LLC

Case Number: 14-02852

vs.

Respondents  
John M. Jacobs,  
Jacobs & Company,  
Wellington Shields & Co., LLC, and  
Edward Ian Herbst d/b/a The Herbst Group, LLC

Hearing Site: Charleston, West Virginia

and

Counter-Claimants  
Wellington Shields & Co., LLC and  
Edward Ian Herbst d/b/a The Herbst Group, LLC

vs.

Counter-Respondent  
Omega Facility Services, Solutions & Surety, LLC

---

Nature of the Dispute: Customer vs. Member, Associated Person, and Non-Members

This case was decided by an all-public panel.

**REPRESENTATION OF PARTIES**

For Claimant Omega Facility Services, Solutions & Surety, LLC ("Claimant"): Stephen P. Meyer, Esq., Meyer, Ford & Glasser, PLLC, Charleston, West Virginia and Brandon S. Steele, Esq., Beckley, West Virginia. On or about June 1, 2016, Stephen P. Meyer, Esq. and Brandon S. Steele, Esq., filed a Notice of Withdrawal. Thereafter, Claimant appeared pro se. On or about June 30, 2016, Brandon S. Steele, Esq. filed a Notice of Appearance.

For Respondents John M. Jacobs ("Jacobs") and Jacobs & Company: Herschel H. Rose, III, Esq., Rose Law Office, Charleston, West Virginia.

For Respondents Wellington Shields & Co., LLC ("Wellington Shields") and Edward Ian Herbst d/b/a The Herbst Group, LLC ("Herbst"): Neil A. Sussman, Esq., Sussman & Frankel, LLP, New York, New York.

FINRA Office of Dispute Resolution  
Arbitration No. 14-02852  
Award Page 2 of 6

### **CASE INFORMATION**

Statement of Claim filed on or about: September 11, 2014.  
Claimant signed the Submission Agreement: September 10, 2014.  
Claimant filed an Answer to the Counterclaim on or about: December 29, 2014.

Statement of Answer and Counterclaim filed jointly by Wellington Shields and Herbst on or about: December 10, 2014.  
Wellington Shields signed the Submission Agreement: December 29, 2014.  
Herbst signed the Submission Agreement: December 30, 2014.

### **CASE SUMMARY**

In the Statement of Claim, Claimant asserted the following causes of action: breach of contract, breach of fiduciary duty, respondeat superior, misrepresentations, omissions, negligence, negligent supervision, fraud, violation of FINRA Conduct Rules 2020, 2111, and 3130, violation of the New York Stock Exchange Rules, violation of the Securities Exchange Act of 1933 and 1934, violation of the West Virginia Common Law, violation of the West Virginia Consumer Protection Act, violation of the West Virginia Securities Act, and violation of the Uniform Securities Act. Claimant alleged that Jacobs, Wellington Shields, and Herbst were negligent in the handling of Claimant's account, that Jacobs disregarded Claimant's stop-trade order, and, as a result, Claimant suffered losses in its account.

Unless specifically admitted in their Statement of Answer, Wellington Shields and Herbst denied the allegations made in the Statement of Claim and asserted various affirmative defenses.

In the Counterclaim, Wellington Shields and Herbst asserted the following cause of action: indemnification. Wellington Shields and Herbst alleged that at all times, control over Claimant's account at-issue was vested exclusively in Jacobs & Company, Claimant's investment advisor, agent, and attorney-in-fact. Wellington Shields and Herbst alleged that they exercised due care to fulfill their obligations to Claimant and did not engage in misconduct of any kind.

Unless specifically admitted in its Statement of Answer to the Counterclaim, Claimant denied the allegations made in the Counterclaim and asserted various affirmative defenses.

### **RELIEF REQUESTED**

In the Statement of Claim, Claimant requested:

|                                     |                |
|-------------------------------------|----------------|
| Compensatory Damages (in excess of) | \$1,000,000.00 |
| Punitive Damages                    | Unspecified    |
| Interest                            | Unspecified    |
| Attorneys' Fees                     | Unspecified    |
| Costs                               | Unspecified    |
| Other Monetary Relief               | Unspecified    |

FINRA Office of Dispute Resolution  
Arbitration No. 14-02852  
Award Page 3 of 6

In the Statement of Answer, Wellington Shields and Herbst requested that the claims asserted against them be denied in their entirety that they be awarded their costs and expenses, and other and further relief as appears just.

In the Counterclaim, Wellington Shields and Herbst requested:

|                                     |                |
|-------------------------------------|----------------|
| Compensatory Damages (in excess of) | \$1,000,000.00 |
| Punitive Damages                    | Unspecified    |
| Interest                            | Unspecified    |
| Attorneys' Fees                     | Unspecified    |
| Costs                               | Unspecified    |
| Other Monetary Relief               | Unspecified    |

In the Statement of Answer to the Counterclaim, Claimant requested the dismissal of the Counterclaim and that its claims be granted in their entirety.

#### **OTHER ISSUES CONSIDERED AND DECIDED**

The Arbitrators acknowledge that they have each read the pleadings and other materials filed by the parties.

On or about December 9, 2014, Respondents John M. Jacobs and Jacobs & Company notified FINRA that they are neither members nor associated persons of FINRA and did not voluntarily submit to arbitration. Therefore, the Panel made no determination with respect to Claimant's claims against Respondents John M. Jacobs and Jacobs & Company.

At the final hearing, which was recorded, Wellington Shields and Herbst made oral requests for expungement of all references to this matter from their registration records maintained by the Central Registration Depository ("CRD"). Claimant contested the requests for expungement.

The Panel reviewed the BrokerCheck® Reports for Wellington Shields and Herbst. In recommending expungement, the Panel relied upon the following documentary or other evidence: Investment Management Agreement, Collateral Control Agreement, account information, and the testimony of Claimant and Herbst.

The parties have agreed that the Award in this matter may be executed in counterpart copies or that a handwritten, signed Award may be entered.

#### **AWARD**

After considering the pleadings, the testimony and evidence presented at the hearing, the Panel has decided in full and final resolution of the issues submitted for determination as follows:

1. Claimant's claims, each and all, are denied.

FINRA Office of Dispute Resolution  
Arbitration No. 14-02852  
Award Page 4 of 6

2. The Counterclaim of Wellington Shields and Herbst is denied.
3. The Panel recommends the expungement of all references to the above-captioned arbitration from registration records maintained by the CRD for Respondents Wellington Shields & Co., LLC (CRD #149021) and Edward Ian Herbst (CRD #243580), with the understanding that, pursuant to Notice to Members 04-16, Respondents Wellington Shields & Co., LLC and Edward Ian Herbst must obtain confirmation from a court of competent jurisdiction before the CRD will execute the expungement directive.

Unless specifically waived in writing by FINRA, parties seeking judicial confirmation of an arbitration award containing expungement relief must name FINRA as an additional party and serve FINRA with all appropriate documents.

Pursuant to Rule 12805 of the Code, the Panel has made the following Rule 2080 affirmative findings of fact:

- The claim, allegation, or information is factually impossible or clearly erroneous;
- The registered person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation, or conversion of funds; and
- The claim, allegation, or information is false.

The Panel has made the above Rule 2080 findings based on the following reasons:

The parties remaining in this matter, Wellington Shields and Herbst, entered into specific contractual agreements whereby they would follow specific instructions, which were made in writing. It was clear from both Claimant's and Respondents' evidence that they did this. Any misrepresentations were not made by Wellington Shields or Herbst, but by Mr. Jacobs, who did not submit to this arbitration, but was named in a separate state court lawsuit. Wellington Shields and Herbst played no role in those representations alleged.

4. Other than forum fees, which are specified below, the parties shall each bear their own costs and expenses incurred in this matter.
5. Any and all claims for relief not specifically addressed herein, including punitive damages and attorneys' fees, are denied.

### **FEES**

Pursuant to the Code, the following fees are assessed:

#### **Filing Fees**

FINRA Office of Dispute Resolution assessed a filing fee\* for each claim:

FINRA Office of Dispute Resolution  
 Arbitration No. 14-02852  
Award Page 5 of 6

|                          |               |
|--------------------------|---------------|
| Initial Claim Filing Fee | = \$ 1,800.00 |
| Counterclaim Filing Fee  | = \$ 3,200.00 |

*\*The filing fee is made up of a non-refundable and a refundable portion.*

#### **Member Fees**

Member fees are assessed to each member firm that is a party in these proceedings or to the member firm that employed the associated person at the time of the events giving rise to the dispute. Accordingly, as a party, Wellington Shields & Co., LLC is assessed the following:

|                            |               |
|----------------------------|---------------|
| Member Surcharge           | = \$ 2,800.00 |
| Pre-Hearing Processing Fee | = \$ 750.00   |
| Hearing Processing Fee     | = \$ 5,000.00 |

#### **Adjournment Fees**

Adjournments granted during these proceedings for which fees were assessed:

|  |                      |
|--|----------------------|
| December 8-10, 2015, adjournment requested by Claimant   | = \$ 1,200.00        |
| July 6-8, 2016, adjournment requested by Claimant        | = \$ 1,200.00        |
| September 13-15, 2016, adjournment requested by Claimant | Waived               |
| <b>Total Adjournment Fees</b>                            | <b>= \$ 2,400.00</b> |

The Panel has assessed \$2,400.00 of the adjournment fees to Claimant Omega Facility Services, Solutions & Surety, LLC.

#### **Hearing Session Fees and Assessments**

The Panel has assessed hearing session fees for each session conducted. A session is any meeting between the parties and the arbitrators, including a pre-hearing conference with the arbitrators, that lasts four (4) hours or less. Fees associated with these proceedings are:

|  |                      |
|--|----------------------|
| Three (3) pre-hearing sessions with the Panel @ \$1,200.00/session | = \$ 3,600.00        |
| Pre-hearing conferences: March 20, 2015                            | 1 session            |
| November 23, 2015  | 1 session            |
| April 5, 2016  | 1 session            |
| Seven (7) hearing sessions @ \$1,200.00/session                    | = \$ 8,400.00        |
| Hearing Dates: November 15, 2016                                   | 3 sessions           |
| November 16, 2016  | 2 sessions           |
| November 17, 2016  | 2 sessions           |
| <b>Total Hearing Session Fees</b>                                  | <b>= \$12,000.00</b> |

The Panel has assessed \$12,000.00 of the hearing session fees to Claimant Omega Facility Services, Solutions & Surety, LLC.

All balances are payable to FINRA Office of Dispute Resolution and are due upon receipt.

FINRA Office of Dispute Resolution  
Arbitration No. 14-02852  
Award Page 6 of 6

**ARBITRATION PANEL**

|                         |   |  |
|-------------------------|---|--|
| Thomas H. Barnard, Jr.  | - | Public Arbitrator, Presiding Chairperson |
| Christopher M. McMurray | - | Public Arbitrator                        |
| John C. Aten            | - | Public Arbitrator                        |

I, the undersigned Arbitrator, do hereby affirm that I am the individual described herein and who executed this instrument, which is my award.

**Concurring Arbitrators' Signatures**

/s/ Thomas H. Barnard, Jr.  
Thomas H. Barnard, Jr.  
Public Arbitrator, Presiding Chairperson

November 30, 2016  
Signature Date

/s/ Christopher M. McMurray  
Christopher M. McMurray  
Public Arbitrator

December 1, 2016  
Signature Date

/s/ John C. Aten  
John C. Aten  
Public Arbitrator

December 1, 2016  
Signature Date

December 1, 2016  
Date of Service (For FINRA Office of Dispute Resolution office use only)

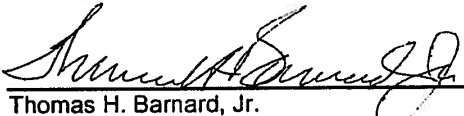
FINRA Office of Dispute Resolution  
Arbitration No. 14-02852  
Award Page 6 of 6

**ARBITRATION PANEL**

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| Christopher M. McMurray | - | Public Arbitrator                        |
| John C. Aten            | - | Public Arbitrator                        |

I, the undersigned Arbitrator, do hereby affirm that I am the individual described herein and who executed this instrument, which is my award.

**Concurring Arbitrators' Signatures**

  
\_\_\_\_\_  
Thomas H. Barnard, Jr.  
Public Arbitrator, Presiding Chairperson

11/30/16  
\_\_\_\_\_  
Signature Date

\_\_\_\_\_  
Christopher M. McMurray  
Public Arbitrator

\_\_\_\_\_  
Signature Date

\_\_\_\_\_  
John C. Aten  
Public Arbitrator

\_\_\_\_\_  
Signature Date

\_\_\_\_\_  
Date of Service (For FINRA Office of Dispute Resolution office use only)

FINRA Office of Dispute Resolution  
Arbitration No. 14-02852  
Award Page 6 of 6

**ARBITRATION PANEL**

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Thomas H. Barnard, Jr.  
Public Arbitrator, Presiding Chairperson

\_\_\_\_\_  
Signature Date

  
\_\_\_\_\_  
Christopher M. McMurray  
Public Arbitrator

  
\_\_\_\_\_  
Signature Date

\_\_\_\_\_  
John C. Aten  
Public Arbitrator

\_\_\_\_\_  
Signature Date

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Date of Service (For FINRA Office of Dispute Resolution office use only)

FINRA Office of Dispute Resolution  
Arbitration No. 14-02852  
Award Page 6 of 6

**ARBITRATION PANEL**

|                         |   |  |
|-------------------------|---|--|
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| Christopher M. McMurray | - | Public Arbitrator                        |
| John C. Aten            | - | Public Arbitrator                        |

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**Concurring Arbitrators' Signatures**

\_\_\_\_\_  
Thomas H. Barnard, Jr.  
Public Arbitrator, Presiding Chairperson

\_\_\_\_\_  
Signature Date

\_\_\_\_\_  
Christopher M. McMurray  
Public Arbitrator

\_\_\_\_\_  
Signature Date

*John C. Aten*  
\_\_\_\_\_  
John C. Aten  
Public Arbitrator

*12/1/16*  
\_\_\_\_\_  
Signature Date

\_\_\_\_\_  
Date of Service (For FINRA Office of Dispute Resolution office use only)

We, the professional advisors, work hard to keep a clean name.  
Some clients are taking advantage of the rules, thinking we are vulnerable & they can use the system for unjust profits.

Protection & justice is for all.

Thank you.

**Rod I. Skaf**, MBA, MSFS, AEP, CFP®, ChFC®, CLU®, CASL®  
Senior Financial Planner, Financial Services Executive, Investment Adviser Representative

Please note my new email address: [rskaf@rodskaf.com](mailto:rskaf@rodskaf.com)



5600 Blazer Parkway, Suite 100, Dublin, Ohio 43017



(614) 726-3726



(614) 726-3750



(614) 332-0811  [www.rodskaf.com](http://www.rodskaf.com)

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\*\*\*\* This message was sent via secure encryption. \*\*\*\*

FINRA

We need a fair system to discount meritless claims. (RE reference Rule 17-42).

Lance W. Slaughter

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[Investment Tools & Insights](#)

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[\[wfasignatures.com\]](#)[\[wfasignatures.com\]](#)[\[wfasignatures.com\]](#)



**Lance Withers Slaughter**  
First Vice President - Investment Officer



**Wells Fargo Advisors, LLC**  
1133 Connecticut Avenue, N.W.  
Suite 900  
Washington, DC 20036-4305  
Tel 202-861-4455  
Toll Free 800-368-5620  
Cell 202-277-7264  
Fax 202-861-4513  
lance.slaughter@wfadvisors.com  
[home.wellsfargoadvisors.com/lance.slaughter](http://home.wellsfargoadvisors.com/lance.slaughter)

[\[home.wellsfargoadvisors.com\]](#)

Click to Add My Info to your Contacts

[\[wfasignatures.com\]](#)

Sincerely,

**Lance Withers Slaughter**

First Vice President - Investment Officer

Wells Fargo Advisors | 1133 Connecticut Avenue, N.W., Suite 900 | Washington, DC 20036-4305  
Tel 202-861-4455 | Toll-free 800-368-5620 | Cell 202-277-7264 | Fax 202-861-4513

[lance.slaughter@wfadvisors.com](mailto:lance.slaughter@wfadvisors.com) |

<http://home.wellsfargoadvisors.com/lance.slaughter>[\[home.wellsfargoadvisors.com\]](#)

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January 31, 2018

FINRA Comment Board

Reference: Rule 17-42

I recently became aware of the proposed Rule 17-42, and would appreciate the opportunity to offer my comments.

To make it more expensive, more rigorous and arbitrarily apply a time limit to the correction of the official record is completely unreasonable. Further, to apply differing standards to the procedures seems to me to be oxymoronic to the goals of the system – that is, to find and fairly reflect the truth. If one party is bound by a majority (rather than unanimous) decision, shouldn't both parties be? To do it any other way is completely unjust, and anathema to the system as conceived.

The truth shouldn't have a time limit, it shouldn't cost more!

The system was conceived to fairly treat all parties to a dispute. This rule does the opposite. The system needs to treat everyone evenhandedly, under the same standards or it will eventually lose its value.

Thank you for the forum to comment.

Sincerely,

Barrick A. Smart

*Barrick A. Smart  
Smart Investments Advisory Inc.  
WBB Securities, LLC  
1849 W. Redlands Blvd., Suite 104  
Redlands CA 92373*

*909-335-8565  
909-335-8573 fax*

*[www.smart-advisory.com](http://www.smart-advisory.com)*



Neil H. Smith  
5705 Pollock Lane  
Knoxville, TN 37914  
865-247-6014  
[neilsmith06@comcast.net](mailto:neilsmith06@comcast.net)

January 26, 2018

Sent Via U.S. Mail

Financial Industry Regulatory Authority  
Attn: Marcia E. Asquith  
Office of the Corporate Secretary  
1735 K Street NW  
Washington, DC 20006-1506

Re: FINRA Regulatory Notice 17-42 (December 6, 2017)

Dear Ms. Asquith:

I appreciate the opportunity to add my comments to those already presented regarding Regulatory Notice 17-42 (December 6, 2017). I have read what I believe to be the majority of comments already submitted regarding the changes FINRA is seeking to make regarding the policies, procedures and rules for Expungement. I will not impose my opinions and beliefs when so many have already made similar, impassioned statements that, for the most part, reflect my own. However there is one topic where I feel compelled to add my two cents: Section III.A, Selection of Panel.

I became a FINRA Arbitrator in 2006 and have been on the Chairperson Roster since 2007. During this time period I have been selected as a panel member or sole Arbitrator on more than 60 cases. Among those I have been selected to participate in eight Expungement hearings: six were granted and two were denied: I was the sole Arbitrator on two out of the eight cases: of the remaining six, four were unanimous decisions with the remaining two being decided by the majority. I cannot state the qualifications for the other Arbitrators involved in those cases, but I can claim this about mine:

- (1) I completed enhanced expungement training;
- (2) I *HAVE NOT* been admitted to practice law in any jurisdiction;
- (3) I *DO NOT* have five years' experience in any one of the following disciplines:
  - (a) litigation;
  - (b) federal or state securities regulation;
  - (c) administrative law;
  - (d) service as a securities regulator; or
  - (e) service as a judge.

So now I have to ask this question: Was I qualified to participate in those eight cases? If an "Expungement Arbitrator Roster" is created I will not be qualified to be on it. Will I? Will these new qualifications mean that I should never have been on the cases I decided as sole arbitrator, or participated in as a member of the Panel? There is an even more pertinent question to consider: Will this open the door for others to claim that their

Expungement hearings were invalid because the Arbitrators who decided their case were unqualified to do so?

As a FINRA Arbitrator I have: read Statements of Claim and the answers responding to them; I have presided over IPHC's, telephonic hearings on Motions, and in-person hearing on the merits; I have decided entire cases only on the papers presented; I have decided Motions only with the papers presented; I have issued Subpoenas and Orders for Appearance; and I have decided cases with multi-million dollar awards affecting the lives of Claimants as well as the Respondents. And I have performed all these responsibilities with a strong dedication to listen to both sides of the case, considering all of the testimony and evidence presented, and have pushed aside any empathy I may have had for the losing party because I am committed to only honoring the merits deciding the case.

Is the responsibility for deciding a claim for Expungement that much greater than those brought by Claimants against Respondents? Customer and Industry cases? Will the creation of a fourth roster, based on RN 17-42.III.A, negatively impact the credibility of a large number of the 3,337 public Arbitrators on FINRA rosters as of December 31, 2017? There will be those who will ask, "If they aren't competent to decide Expungements, are they really competent to decide cases?"

As an Arbitrator who has completed "enhanced expungement training," and who has also participated in Expungement claims, I can say, with no reservations, that there is need for improvement in the training. A good start toward that improvement should involve Arbitrators who have participated in a number of Expungement cases. They can offer insight as to which areas they felt lacked the training and knowledge of the procedures and what was expected of them. Another excellent source of how to improve the training should come from the case administrators who have had to hand-hold the arbitrators through the process. They know the problem areas that arise frequently.

I've said my piece and offered my opinions. Now I will finish with FINRA's own words that shouldn't be brought into question by those who would seek to undermine the credibility of the arbitration process – past, present or future:

*"FINRA arbitrators are a group of **dedicated individuals** serving the investing public and the securities industry. They are **neutral, well-qualified and essential to maintaining a fair, impartial and efficient system of dispute resolution**. FINRA maintains a roster of more than 7,200 arbitrators."* (Emphasis added.)

Respectfully and truly yours,

A handwritten signature in black ink, appearing to read "Neil H. Smith". The signature is fluid and cursive, with the first name "Neil" being the most prominent.

Neil H. Smith  
A33944



W. Alan Smith  
Deputy General Counsel  
JANNEY MONTGOMERY SCOTT LLC  
1717 Arch Street, 19<sup>th</sup> Floor  
Philadelphia, PA 19103  
215.665.6003  
F 215.665.0824

February 5, 2018

Via e-mail: [pubcom@finra.org](mailto:pubcom@finra.org)

Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

Re: Regulatory Notice 17-42 – Public Comment

Dear Ms. Asquith:

Thank you for this opportunity to comment on the proposed amendments (“Proposal”) to the Financial Industry Regulatory Authority (“FINRA”) code of arbitration, rules 12805 and 13805, relating to expungement of customer dispute information on behalf of Janney Montgomery Scott LLC (“Janney”). Janney traces its roots in Philadelphia to 1832 and is one of the oldest full service financial services firms in the country with 116 offices and 779 Financial Advisors.

Janney shares the goal of FINRA to protect investors by facilitating their access to relevant information about their Financial Advisors. Unfortunately, FINRA’s Proposal swings the pendulum past “transparency” toward procedural and equitable imbalance. The Securities Industry and Financial Markets Association (“SIFMA”) will be submitting a detailed comment letter, with which Janney is in agreement. However, given the gravity this issue takes on in context of increasing regulatory reliance on disclosures to drive risk based exam programs, we would like to draw the attention of FINRA to a number of specific concerns.

**I. The Central Registration Depository (“CRD”) is Allegation Driven**

To appreciate the impact of the Proposal it is crucial to recall that a mere sales practice *allegation* creates a permanent CRD black mark, without any regard for underlying *merit*. We know this conclusively because it is common for arbitrations to result in awards of zero, yet the associated disclosures commonly remain for the duration of a Financial Advisor’s carrier.

In 2010 FINRA expanded access to information on BrokerCheck backward ten years and forward ten additional years after a Financial Advisor leaves the industry. At the time, FINRA acknowledged that baseless complaints exist and responded to industry concerns with assurance that they would “*Formalize the process for current and former brokers to dispute the accuracy of factual information disclosed through BrokerCheck.*” As it eventuated, the process defined in FINRA Rule 8312(e) specifies that any such dispute “*must pertain only to factual information and not to information that is subjective in nature or a matter of interpretation.*” Given nearly



W. Alan Smith  
Deputy General Counsel  
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F 215.665.0824

all sales practice matters are subjective in some measure, the proffered dispute process is a procedural dead end, leaving only expungement to offset meritless allegation disclosures.

More recently FINRA has specifically held out expungement as a remedy to meritless disclosures. Senior investor protection rule 2165, which goes into effect the same day comments to the Proposal are due, permits temporary holds on cash disbursements where there is evidence of exploitation. It is certain that sales practice complaints will be filed by clients in response, resulting in black marks on the records of Financial Advisors who protect their clientele. When asked for a carve out from disclosure obligations in this scenario, FINRA declined, but opined that resolution could be sought *through expungement*. In this case, by seeking to narrow access to expungement FINRA creates a conflict between the protection of seniors and CRD records. Recall that utilization of an account freeze is optional. If this Proposal is approved, there will be firms who decline to place an otherwise warranted hold at the risk of Advisor records.

## **II. Further Restrictions on Access to Expungement Are Unnecessary**

FINRA has stated that the Proposal is based in part on data cited by “critics of expungement.” One vocal critic has been the Public Investors Arbitration Bar Association (“PIABA”). When assessing PIABA’s argument, consider that its members are frequently the source of meritless disclosures and that a routine litigation tactic is to cite disclosures in the past as conclusive evidence of bad acts in the present. In sum, the more disclosures that can be alleged into existence the more likely they are to prevail and consequently, be paid.

To demonstrate that expungement is too easy to attain, PIABA often cites the “approval rate when expungement was requested.” For a timely example of this, see the January 30, 2018 comment letter submitted in response to this Proposal by Maddox Hargett & Caruso, P.C. The author states (emphasis added):

*Unfortunately, notwithstanding the fact that expungements have been widely recognized as an "extraordinary" measure with significant "regulatory" and "investor protection" implications, the historical monthly expungement data that I have personally maintained since January 1, 2013 indicates otherwise:*

*Between January 1, 2013 and December 31, 2017, expungements were granted in 1,145 out of the 1,974 arbitration proceedings **in which an expungement was requested** which equates to an expungement approval rate of 73.20%.*

Initially, this arithmetic is simply incorrect and would be an approval rate of 58%. More crucially, it entirely misses the point. Per FINRA, between January of 2013 and December of 2017 there were 19,195 arbitration cases closed in the forum. If we accept the figure of 1,145 expungements as accurate, this means it was granted, as a ratio of all FINRA arbitrations, only



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*5.9% of the time.* Even more telling, expungement is also the only realistically available method of removing a sales practice complaint. Between January 2013 and December of 2016, the last full year of data for which 4530(d) complaint reporting is available, 78,654 sales practice complaints were filed. Accepting the figure of 1,145 expungements granted as accurate, related disclosures were removed in *less than 1%* of combined arbitration and sales practice matters.

Consider a parallel of what PIABA is attempting to argue. The Cleveland Browns were undefeated against the Tampa Bay Buccaneers in 2015, a stratospheric win rate of 100%. Unfortunately for their fans, that tortured logic doesn't mean Cleveland victories are common. In fact, the Browns lost their other fifteen games that season to go one and fifteen, a win percentage of .0625. So arbitrations since 2013 ending with an expungement are already less common than a Browns win. Once complaints are included, they become rarer still.

FINRA has already offered sufficient rulemaking and guidance around the expungement process to ensure legitimate consumer protection or regulatory interests. With expungements resulting in a minute percentage of all matters, it is a sufficiently "extraordinary" remedy.

### **III. Expungement Awards Must Not Require a Unanimous Panel Decision**

All current FINRA arbitration panel decisions are based on a majority finding, whereas the Proposal would require unanimity. Taken to logical conclusion, this requires FINRA to have determined that the barrier to expungement should be higher than the standard required for the same panel to Order a multi-million-dollar award or refer a Financial Advisor directly to Enforcement. There does not appear to be any articulated justification for a paradigm that makes a material award more easily attainable than the removal of a meritless CRD filing.

### **IV. Expungement Awards Must Not Be Subject to a One Year Limitation Period**

As with the Proposed unanimous decision criteria, there appears to be no basis for subjecting expungement to a one-year limitation. Recall that FINRA rules 12504 and 13504 already provide a six-year eligibility period. There appears to be no regulatory benefit in shortening the expungement eligibility period by five years to offset the potential harm to a Financial Advisor unnecessarily carrying the burden of a meritless disclosure.

### **V. Requiring a Finding of No Investor Protection or Regulatory Value is Conflicted**

In order to grant an expungement, the Proposal requires the Panel unanimously reach two potentially conflicting findings. First, the Panel must find that the disclosure is "factually impossible or clearly erroneous," the "registered person was not involved" or "the claim, allegation or information is false."



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Deputy General Counsel  
JANNEY MONTGOMERY SCOTT LLC  
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F 215.665.0824

Second, the Panel must find that the “dispute information has no investor protection or regulatory value.” It is difficult to imagine a scenario where a disclosure might concern a claim that meets one of the initial three criteria, yet still has a valid investor protection or regulatory value. What can be anticipated is that at least one of three Panel members concludes that FINRA believes all disclosures have regulatory value, regardless of merit, thereby making expungement a de facto impossibility.

It must also be noted that this evaluation places arbitration panelists in the role of FINRA in determining “regulatory value.” Arbitrators are, by definition, neutral and should not be asked to reach this subjective determination. Recall that *guidance* to this effect was already promulgated in September of 2017 in a Notice to Arbitrators.

**VI. The Proposed Filing Fees and Requirement to Name Employers as Arbitration Respondents Are Unwarranted**

The Proposal calls for a filing fee of a least \$1,425 dollars and, where a case is closed by any method other than award, Financial Advisors must name their employer as Respondent. A firm so named would be assessed a member fee in turn. There is no regulatory justification for this set of policies other than generating another set of burdens, this time transparently monetary. Placement of financial stumbling blocks in the path of removing meritless disclosures, a request made in less than 1% of sales practice matters, could be justified only by a grave investor protection deficiency. No such deficiency has been evidenced.

Again, Janney concurs that investor access to relevant complaint and arbitration history is a vital component of consumer and market protection. However, those seeking to make expungement more difficult have already succeeded to a more than adequate degree. Arguments to the contrary fail to either recognize how rare expungement is or offer a regulatory gap that calls out for redress at the expense of due process. As FINRA continues to increase its reliance on ascertaining who a “recidivist” actually is, FINRA should share the goal of removing meritless disclosure records that harm market confidence by confusing investors and obscuring the actual bad actors.

Best Regards,

W. Alan Smith  
Deputy General Counsel

To whom it may concern:

The Rule 17-42 is going to cause un-needed hardship on those advisors who are subjected to meritless claims.

I personally have only one mark on my U-4, FROM MY SISTER IN LAW, after more than 18 years in the business. I was pulled into a family squabble as leverage against my wife. The claim was meritless and was denied by my firm after they investigated. She was able to claim a loss of the magic number (over \$5000) in spite of the fact her account was actually positive.

I submitted comments years ago to counter her claims, but it appears that those notes never made it to my U-4.

Currently in the process of trying to get the mark expunged.

It is un-fair that the costs of filing as case has increased.

It is just not right that a customer only needs a majority in arbitration for a bogus case, while the Financial Advisor will need a unanimous decision to have it expunged.

Finally, taking the ability to expunge off the table for those cases over 12 months is just plain wrong.

Personally, the last thing I wanted to do, or had the ability to do, early in my career when I was living on credit cards trying to build a book, was to reengage in a legal situation, especially when the cost of doing so is now \$10,000 +.

These changes are going to negatively affect the next generation of advisor much more than those of us who are now established.

Thank you for your time,

*Click on my business card and its tabs to learn more.*

|   |                                     |                                   |                                     |
|---|-------------------------------------|-----------------------------------|-------------------------------------|
| <a href="#">Schedule a consultation</a> | <a href="#">[wfesignatures.com]</a> | <a href="#">Are you on track?</a> | <a href="#">[wfesignatures.com]</a> |
| <a href="#">Make an introduction</a>    | <a href="#">[wfesignatures.com]</a> |                                   |                                     |





**Jeff Speicher**  
Managing Director - Investment Officer

**Wells Fargo Advisors**  
1129 Main Ave.  
Durango, CO 81301  
Tel: 970-385-3985  
Toll-free: 800-234-3390  
Fax: 970-259-4514

[jeffrey.speicher@wfsadvisors.com](mailto:jeffrey.speicher@wfsadvisors.com)

[www.speicherfg.com](http://www.speicherfg.com)

[\[speicherfg.com\]](http://speicherfg.com)



Save details to address book

[\[wfasignatures.com\]](http://wfasignatures.com)

Sincerely,

**Jeff Speicher**

Managing Director - Investment Officer  
Speicher Financial Group of Wells Fargo Advisors

Wells Fargo Advisors | 1129 Main Ave. | Durango, CO 81301  
Tel 970-385-3985 | Toll-free 800-234-3390 | Fax 970-259-4514

[jeffrey.speicher@wfadvisors.com](mailto:jeffrey.speicher@wfadvisors.com) | <http://www.speicherfg.com>[\[speicherfg.com\]](http://speicherfg.com)

Hello:

My name is Denise Stephens and I have been a Registered Representative since 1994. I have ALWAYS been a fiduciary for my clients – putting their best interests above all else. In 2009 I was asked by my broker/dealer – Voya Financial Advisors, to take over some clients from an advisor that they terminated. He was terminated because he wasn't doing his job and had had no contacts with his clients in over a year.

I sent letters of introduction to all the clients I was able to get information from Voya on over the course of a couple of months from July-Oct 2009. I made contact with the son of one of these clients in Sept 2009. **He had power of attorney** over his father and mother's accounts. He provided me with the POA documentation. I told him that a large portion of his father's account was currently unmanaged, as several changes had occurred in the managed account he was in at the time. I sent forms for him to sign to add a manager to that portion of the father's account, but I never received them back. I sent emails reminding the son that these forms were needed. I never heard back.

In 2010, I was made aware of a complaint against me regarding this account. The complaint was made by someone, who to this day, I have no idea of their relationship with the account. According to what is on my U-4, Voya says it was the Power of Attorney. It was NOT the power of attorney, the client's son, who made this claim. The claim was also with regard to the time I was NOT the advisor. I was told by Voya that it had to be on my record, since I was the current rep.

This is a COMPLETELY UNFAIR situation. The changes that you are wanting to make regarding expungements would be severely detrimental to good advisors, like me, who DID NOTHING WRONG!

I want to actively attempt to get this claim off my record. It never belonged there in the first place. Only giving reps 12 months to work through something like this is way too short of a time. Please do not make this change.

*Denise Stephens*



Please consider the environment before printing this e-mail!

Denise M. Stephens, CFP  
Financial Advisor  
Princeton Financial Services, Inc.  
13330 SW 111 Avenue  
Miami, FL 33176  
305-253-9604  
Fax: 1-305-501-4952

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**BARITZ & COLMAN LLP**

OFFICES IN FLORIDA & NEW YORK

ATTORNEYS AT LAW  
The Woolworth Building  
233 Broadway, Suite 2020  
New York, New York 10279

212.886.1693 (phone)  
212.886.1694 (fax)  
www.baritzcolman.com

JOHN D. STEWART  
jstewart@baritzcolman.com  
Direct Dial: 646.376.7053

February 5, 2018

**VIA EMAIL**

Financial Industry Regulatory Authority  
Attn: Marcia E. Asquith  
Office of the Corporate Secretary  
1735 K Street, NW  
Washington, DC 20006-1506  
pubcom@finra.org

**Re: FINRA Regulatory Notice 17-42, December 6, 2017**

Dear Ms. Asquith:

We write in response to FINRA's request for comment on proposed amendments to the Codes of Arbitration Procedure relating to requests to expunge customer dispute information, as set forth in Regulatory Notice 17-42, dated December 6, 2017 (the "Proposal").

This law firm represents financial advisers and broker dealers on legal matters concerning the financial services industry, including FINRA Dispute Resolution arbitration proceedings. FINRA Dispute Resolution plays an essential role as an impartial arbiter of disputes involving the financial services industry, and the organization's function as a protector of the rights of customers is especially important. One significant manner by which FINRA Dispute Resolution protects the integrity of and ensures due process and fairness to the participants in the process, including the financial advisers and their customers, is through the expungement process. The expungement process contemplates and ensures that information reported on the Central Registration Depository ("CRD") is a truthful, accurate and reliable indicator of a financial adviser's history.

Member firms are required to report any and all customer complaints of alleged industry sales practice violations, regardless of their truth or falsity, before it is determined by either the

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firm or a FINRA Dispute Resolution arbitration panel whether such complaints ultimately have merit. Often, such complaints subject a financial adviser to considerable expense and inconvenience, despite the fact that the customer has alleged no wrongdoing by that individual financial adviser. Although this process may result initially in the inclusion of misleading and inaccurate disclosures on a financial adviser's CRD record, FINRA's current expungement procedures ensure that those misleading (and at times, completely false) customer complaints are removed from the CRD record in order to provide an accurate record. Current FINRA Rule 2080 not only ensures a fair process for financial advisers but, more importantly, it ensures the accuracy and reliability of the CRD system.

The Proposal purportedly seeks to fill a perceived regulatory need of increased customer participation. While that is a worthy goal, it is one which has already been addressed by FINRA's September 2017, Notice to Arbitrators and Parties on Expanded Expungement Guidance. Since the dissemination of this Notice, arbitrators have been ordering customer notification and have sought participation from those customers. The proposed creation of an Expungement Arbitrator Roster is also a sensible proposal that will ensure only arbitrators experienced in the intricacies of the expungement rules make these important decisions.

However, most of the proposed amendments would not only fail to increase customer participation, but instead would needlessly increase the expense and decrease the accessibility to the expungement process which is plainly prejudicial to the financial adviser. The logical result of this decreased accessibility would be a corresponding decrease in expungement requests by financial advisers whose CRD records include false, misleading or inaccurate customer claims. Correspondingly, the CRD system would therefore be less accurate and would not adequately serve customers' needs.

Specifically, the following proposed amendments would make expungement less accessible to financial advisers:

1. In-Person Hearing Requirement

The requirement of an in-person hearing will significantly increase the cost to financial advisers. This increased cost, in attorneys' fees as well as work time lost by the financial advisers, will do nothing to improve the process. Stated differently, there is no demonstrable evidence that the current telephonic hearings fail to administer a fair outcome. The added cost will make it more onerous for those with false or incorrect disclosures to expunge such matters from their CRD records. As such, fewer financial advisers will seek expungement of misleading disclosures, and inaccuracies will necessarily remain in the CRD records.

2. Three-Person Panel Requirement

Similarly, the requirement of a three-person panel will also significantly increase the cost for financial advisers seeking expungement. The time necessary to rank and choose a Panel for these matters would increase threefold under this proposed rule change. In addition to the added

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expense, such a requirement would significantly delay the process. All cynicism aside, other than the increase in filing fee revenues for FINRA Dispute Resolution, who would benefit from this proposed change?

Instead, by creating an Expungement Arbitrator Roster, FINRA can ensure that expungement requests are heard by arbitrators who are skilled and experienced in the nuances of the expungement rules.

### 3. Higher Burden of Proof

The Proposal, if enacted, would alter the purpose of Rule 2080 in a way which is counter to FINRA's stated goal of "maintaining a CRD system that provides public investors and regulators access to accurate information about firms and brokers..." See FINRA Notice to Members 04-16. As stated above, we fail to see the demonstrable evidence of failures in the current system. While the consequence to the financial adviser is plainly evident, it is not at all clear how the public would be better protected.

The proposed requirement that an arbitrator find expungement appropriate under both Rule 2080(b)(1)(A) **AND** Rule 2080(b)(1)(B) is not only unduly burdensome, but also alters Rule 2080 beyond its stated goal. This is a notable departure from the current provision which, pursuant to Rule 2080(b)(1)(A), already requires the Arbitrator to make a specific, reasoned determination regarding the propriety of expungement. Rule 2080(b)(1)(B) provides a safeguard by allowing for expungement of customer complaints in situations where fairness dictates such a result even if none of the Rule 2080(b)(1)(A) elements strictly apply. While it is the rare situation in which expungement would be appropriate under (A) but not (B), Rule 2080 purposely leaves open such a possibility in order to ensure the integrity of the CRD system.

Further, the standard for a finding under Rule 2080(b)(1)(B) would become more onerous under the Proposal – changing the requirement from a finding of "meritorious" requests that pose "no material adverse effect on investor protection, the integrity of the CRD system or regulatory requirements" to requiring a finding that "the customer dispute information has **no investor protection or regulatory value.**" (emphasis added). The Proposal thus contradicts the stated goal of maintaining an accurate CRD System, which depends on the removal of false, misleading and inaccurate disclosures.

### 4. One-Year Statute of Limitations

Limiting to one year the time to file expungement requests that do not result in an arbitration claim would also constitute an unnecessarily harsh restriction on the rights of financial advisers who are subjects of misleading CRD disclosures. FINRA's stated goal for the Proposal is to increase customer participation; however, to the extent such participation may be limited due to stale expungement requests, a one year limit is unnecessary. State law statutes of limitation, which are enacted for similar reasons, primarily provide from three to six years to file an action. FINRA's proposal of a fraction of that time unduly prejudices financial advisers.

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Additionally, such a short period is a disservice to all participants in the process, including customers, who necessarily rely on the integrity of the CRD system. A one year time limit for filing expungement claims would reduce the number of financial advisers filing expungement claims. As such, false, inaccurate and misleading disclosures, which imply wrongdoing on the part of a financial adviser when no such wrongdoing in fact occurred, would remain on the CRD record, making the CRD system less accurate and eroding customer confidence. Repeating a common theme from above, the Proposal fails to demonstrate flaws in the current system warranting this limitation.

### Conclusion

Financial advisers seeking expungement of customer disputes on their CRD record are entitled to, and have come to expect, fair treatment by the FINRA Dispute Resolution system. It is therefore axiomatic that fair treatment of individual financial advisers serves investors by ensuring that expungement claims are thoroughly and objectively analyzed and that any disclosures allowed to remain on the CRD record truthfully and accurately reflect the misconduct they imply. The proposed amendments threaten the accuracy of this system, thus fundamental fairness dictates the rejection of the Proposal.

For all the reasons set forth above, we strongly recommend that the Proposal be rejected.

Very truly yours,



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John D. Stewart  
Baritz & Colman LLP

I would like to express my request for a fair system to remove meritless claims on broker check regarding representative CRDs.

These claims are costly and difficult for advisers to remove meritless claims and should be off the record after they are deemed meritless and dismissed .

This is against all aspects of due process and affects and follows the reputation of the rep indefinitely into the future of their career with a brokerage firm .

These claims as well should expunged from the record if they are meritless ,submitted without merit or dismissed claims by the brokerage firm after review.

Nancy Stewart

CRD 1085029

From the IPHONE of Nancy Stewart



## PUBLIC INVESTORS ARBITRATION BAR ASSOCIATION

2415 A Wilcox Drive | Norman, OK 73069  
Toll Free (888) 621-7484 | Fax (405) 360-2063  
[www.piaba.org](http://www.piaba.org)

February 2, 2018

Via email to [pubcom@finra.org](mailto:pubcom@finra.org)

Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

Re: FINRA Regulatory Notice 17-42  
Expungement of Customer Dispute Information

Dear Ms. Asquith:

I write on behalf of the Public Investors Arbitration Bar Association (“PIABA”), an international, not-for-profit, voluntary bar association that consists of attorneys who represent investors in securities and commodities arbitration proceedings. Since its formation in 1990, PIABA’s mission has been to promote the interests of the public investor in arbitration by, amongst other things, seeking to protect such investors from abuses in the arbitration process, seeking to make the arbitration process as just and fair as possible, and advocating for public education related to investment fraud and industry misconduct. Our members and their clients have a fundamental interest in the rules promulgated by the Financial Industry Regulatory Authority (“FINRA”) that relate to investor protection.

We welcome the opportunity to comment on the proposed changes to the procedures for expungement of customer dispute information from an associated person’s Central Registration Depository (“CRD”) record. PIABA has studied this issue extensively over the past decade.<sup>1</sup> In its October 2015 study, PIABA found that cases involving stipulated awards or settled customer claims between 2012 and 2014,

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<sup>1</sup>See, e.g., “PIABA Study: Stockbroker Arbitration Slates Wiped Clean 9 out of 10 Times When “Expungement” Sought in Settled Cases,” October 2013, <https://piaba.org/piaba-newsroom/piaba-study-stockbroker-arbitration-slates-wiped-clean-9-out-10-times-when-0>; “Update to the 2013 Expungement Study of the Public Investors Arbitration Bar Association,” (“PIABA 2015 Study”), October 2015, <https://piaba.org/piaba-newsroom/report-update-2013-expungement-study-public-investors-arbitration-bar-association>.

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expungements were granted in 87.8% of such cases.<sup>2</sup> These findings are consistent with FINRA's own review of cases filed between 2014 and 2016, where expungement was granted in 88% of settled cases.<sup>3</sup>

FINRA has taken steps to attempt to ensure that customer dispute information only be expunged when it has "no meaningful investor protection or regulatory value"<sup>4</sup> and that expungement of customer dispute information be awarded solely as an extraordinary remedy. To this end, FINRA has increased arbitrator guidance and training related to expungement requests.<sup>5</sup> FINRA has also prohibited firms from preventing customers from participating in the expungement proceedings.<sup>6</sup> Notwithstanding FINRA's actions, expungement is granted far too frequently for it to be considered an extraordinary remedy.

In setting standards for expungement, FINRA should proceed carefully to ensure the protection of the public's interest in relevant information.<sup>7</sup> FINRA's embrace of widespread pre-dispute arbitration agreements currently acts to conceal public access to information about many disputes because records from FINRA proceedings are not available to the public on the same terms as public court proceedings.<sup>8</sup> As such, FINRA must only promulgate rules and policies that facilitate the removal customer complaints from the CRD in the most extraordinary circumstances, because that removal diminishes the ability of reputation to police business misconduct.<sup>9</sup> If a lax expungement process removes information customers could use to protect themselves, more customers will be harmed by associated persons they could have avoided if the complaint information had not been suppressed through FINRA's expungement process.

PIABA applauds FINRA for continuing to examine this issue and attempting to find solutions to the issues PIABA has previously identified. PIABA looks forward to FINRA taking further steps to ensure that customer dispute information is not improperly expunged from associated persons' public records.

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<sup>2</sup> See PIABA 2015 Study at 3.

<sup>3</sup> See FINRA Regulatory Notice 17-42 at 14, [http://www.finra.org/sites/default/files/notice\\_doc\\_file\\_ref/Regulatory-Notice-17-42.pdf](http://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-17-42.pdf).

<sup>4</sup> See FINRA, "Notice to Arbitrators and Parties on Expanded Expungement Guidance," ("Notice on Expanded Expungement Guidance"), updated September 2017, <http://www.finra.org/arbitration-and-mediation/notice-arbitrators-and-parties-expanded-expungement-guidance>.

<sup>5</sup> See PIABA 2015 Study at 2, *supra* n. 2.

<sup>6</sup> See *id.*

<sup>7</sup> See Christine Lazaro, *Has Expungement Broken Brokercheck?*, 14 J. BUS. & SEC. L. 125, 149 (2014) ("FINRA has a statutory obligation to ensure that the information it provides through BrokerCheck is accurate and complete. It can only meet that obligation if the expungement process is handled with integrity and if expungement is granted as a remedy only in extraordinary circumstances").

<sup>8</sup> Cf. *Union Oil Co. of California v. Leavell*, 220 F.3d 562, 568 (7th Cir. 2000) ("People who want secrecy should opt for arbitration. When they call on the courts, they must accept the openness that goes with subsidized dispute resolution by public (and publicly accountable) officials.").

<sup>9</sup> See Benjamin P. Edwards, *Conflicts & Capital Allocation*, 78 OHIO ST. L.J. 181, 209 (2017) ("Even if a retail investor becomes dissatisfied and brings an arbitration proceeding against a financial advisor, the financial advisor will often be able to remove the complaint from public records, further inhibiting the reputation consequence").

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Below, PIABA comments on the questions specifically raised by FINRA:

1. FINRA Rules 12805 and 13805 provide, in relevant part that, in order to grant expungement of customer dispute information under Rule 2080, the panel must comply with the requirements stated in the rule. FINRA notes, however, that if a panel issues an arbitration award containing expungement relief, the award must be confirmed by a court of competent jurisdiction and FINRA could decide to oppose the confirmation. Thus, as the associated person is required to complete additional steps after the arbitrators make their finding in the award before FINRA will expunge the customer dispute information, FINRA believes the word “grant” may not be an appropriate description of the panel’s authority in the expungement process. FINRA is considering changing the word to “recommend.” Please discuss whether the rule should retain “grant” or change to “recommend” or some other description to more accurately reflect the panel’s authority in the expungement process.

PIABA agrees that the operative word in FINRA Rules 12805 and 13805 should be changed from “grant” to “recommend.” As an initial matter, PIABA notes that this change is appropriate based on the plain meaning of the two words. Merriam-Webster defines “grant” in this context as follows: “to consent to carry out for a person; allow fulfillment of.”<sup>10</sup> It defines “recommend” as follows: “to suggest an act or course of action.”<sup>11</sup>

FINRA rule 2080 does not confer upon the Panel the power to “grant” or “allow fulfillment of” an expungement request on its own. Rather, the Panel only has the authority to “recommend” or “suggest” expungement. If the Panel issues an award with a recommendation for expungement, the member or associated person subsequently “must obtain an order from a court of competent jurisdiction...confirming an arbitration award containing expungement relief.”<sup>12</sup> The member or associated person must then take the Court order to FINRA, which actually “carries out” the expungement.

PIABA further notes that this change would be consistent with language used in FINRA’s *Notice to Arbitrators and Parties on Expanded Expungement Guidance*, which states:

FINRA adopted FINRA Rules 12805 and 13805 to establish procedures that arbitrators must follow before **recommending** expungement of customer dispute information related to arbitration

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<sup>10</sup> See Merriam-Webster’s online dictionary, available at <https://www.merriam-webster.com/dictionary/grant>.

<sup>11</sup> See Merriam-Webster’s online dictionary, available at <https://www.merriam-webster.com/dictionary/recommend>.

<sup>12</sup> See FINRA Rule 2080.

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cases or customer complaints from a broker's Central Registration Depository (CRD) record.

\* \* \* \*

Expungement is an extraordinary remedy that should be **recommended** only under appropriate circumstances.

\* \* \* \*

Arbitrators have a unique, distinct role when deciding whether to **recommend** a request to expunge customer dispute information from a broker's CRD record.

\* \* \* \*

Given this significant role, arbitrators should ensure that they have all of the information necessary to make an informed and appropriate **recommendation** on expungement.

\* \* \* \*

Arbitrators **recommending** expungement should ensure that the explanation is complete and not solely a recitation of one of the Rule 2080 grounds or language provided in the expungement request. Specifically, arbitrators should identify in the award the reason(s) for and any specific documentary or other evidence relied on in **recommending** expungement.<sup>13</sup>

For these reasons, PIABA agrees that the word "grant" should be replaced with "recommend."

2. Would named associated persons request expungement in every case to preserve the right to have the expungement claim heard and decided, either in the Underlying Customer Case or as a new claim under the Industry Code? If so, what would be the potential costs and benefits of a named person requesting expungement in every case?

According to FINRA's own statistics, it appears associated persons make expungement requests in approximately 20% of the cases filed.<sup>14</sup> PIABA does not believe that the number of expungement requests made will increase following a change in the rules. With heightened standards applicable to expungement requests, and a clear process for requesting an expungement following the close of the customer case, associated persons may be more deliberate in making expungement requests.

3. Should FINRA consider bifurcating the expungement request from the customer's claim in all cases relating to customer disputes? What would be the costs and benefits of such an approach?

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<sup>13</sup> See Notice on Expanded Expungement Guidance, *supra* n. 4.

<sup>14</sup> FINRA Regulatory Notice 17-42 states that 2,232 customer cases filed between 2014 and 2016 contained requests for expungements. See, Regulatory Notice 17-42 at 13, *supra* n. 3. According to FINRA statistics, 10,938 customer cases were filed between 2014 and 2016. See, FINRA Dispute Resolution Statistics, <http://www.finra.org/arbitration-and-mediation/dispute-resolution-statistics>.

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FINRA should consider bifurcating expungement requests from customer claims. The decision a panel is asked to make with respect to expungement is different than deciding whether or not to find liability on a customer claim. For example, a panel may determine that a customer has not provided sufficient evidence to win on the merits of her underlying case for various reasons. However, expungement may still be inappropriate because the associated person may not have established that the claim was “factually impossible or clearly erroneous,” or “false,” or that the associated person was “not involved” in the alleged conduct at issue<sup>15</sup>

Moreover, FINRA proposes to establish a specially trained arbitrator pool to consider expungement requests, referred to as Expungement Arbitrators. If expungement requests are not bifurcated from the underlying customer case, some expungement requests may be considered by arbitrators who are not Expungement Arbitrators. Failing to bifurcate the proceeding potentially undermines the benefits of creating a pool of Expungement Arbitrators.

4. What are the costs and benefits of requiring the unanimous consent of a three-person panel to grant all requests for expungement of customer dispute information?

As stated above, expungement should be an extraordinary remedy which is only granted when “it has no meaningful investor protection or regulatory value.”<sup>16</sup> Unanimous consent will help ensure that this standard is met. If one of the arbitrators believes the customer dispute information has some meaningful investor protection or regulatory value, the information should remain on the associated person’s record.

5. Is the one-year limitation on being able to request expungement of customer dispute information appropriate? Should the time period be longer or shorter? Please discuss.

PIABA strongly supports a definite cut-off date for requests for expungement. A customer is far more likely to participate in an expungement hearing when it takes place in close proximity to the resolution of the underlying arbitration proceeding. A more stringent timeline will also lead to a higher quality of evidence for the Panel to consider, both in terms of testimony and documentary evidence, both which become less reliable and available with the passage of time. In cases where the arbitration panel in the underlying customer arbitration does not decide an expungement request as part of the award, FINRA proposes a one-year deadline as follows: In cases where a complaint is made but no arbitration is initiated, expungement requests would be permitted to be filed up to one year from the time a customer complaint is submitted to the CRD. In cases where an arbitration is initiated and no award is issued (e.g. settlement of the case, or withdrawal), expungement requests would be permitted to be filed up to one year from the time the underlying case closes.

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<sup>15</sup> See FINRA Rule 2080 (b)(1).

<sup>16</sup> See Notice on Expanded Expungement Guidance, *supra* n. 4.

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PIABA believes that, at a maximum, a one-year time frame is acceptable for the above-described situations. But for those situations in which an arbitration is carried through an evidentiary hearing, and an award is issued, PIABA believes a shorter time frame of 90 days from the resolution of the case is appropriate. Not only is 90 days reasonable, but it is more in line with adjudicatory procedures already familiar to litigants under the Federal Arbitration Act, and would result in a more transparent and meaningful proceeding.

The one-year time limit also poses a real danger of the arbitrators' understanding of the underlying facts going stale. According to FINRA statistics through November 2017, the average time that passes from a customer initiating a FINRA arbitration proceeding to receiving a hearing decision is 16.9 months (and 6.5 months in simplified cases).<sup>1718</sup> Many cases settle near the time of the scheduled hearing. This means that customers may be litigating a case for over a year, and *then* have *another* year to wait to see if an associated person named (or not named but required to submit information to the CRD) in the case will submit a request for expungement. Likewise, customers in a simplified arbitration may have a faster resolution, either through early settlement or an award issued on average in six months. It is fair to require customers to wait a full *year* for a potential expungement request when an expedited resolution has taken place.

The Federal Arbitration Act, 9 U.S.C. § 12, provides that notice of a motion to vacate an arbitration award must be served and the motion filed in court within 3 months after the award is filed or delivered. This three month deadline is also a reasonable amount of time for a party to decide whether or not to move to vacate an award, and provides certainty to the litigants that an arbitration award is final and that the corresponding proceeding is resolved. Surely a similar 90-day deadline for an associated person to request expungement is a reasonable amount of time. PIABA urges FINRA to consider a shorter deadline of 90 days following the award or settlement for filing the expungement request in cases where an arbitration claim has been initiated.

6. Should the associated person who is requesting expungement be required to appear in person or by videoconference, rather than by phone, at the expungement hearing?

FINRA should require associated persons to appear either in person or by videoconference at expungement hearings. Telephonic appearances diminish the arbitrators' ability to observe the associated person and effectively gauge his or her credibility and veracity. Recent research found that the type of communication

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<sup>17</sup> The ABA has adopted model time standards for disposition of cases – 90 percent of all general civil cases should be tried or disposed within 12 months after filing. A number of states have adopted standards consistent with the ABA model. See National Center for State Courts, "Model Time Standards for State Trial Courts," at 12, August 2011, <http://www.ncsc.org/Services-and-Experts/Technology-tools/~media/Files/PDF/CourtMD/Model-Time-Standards-for-State-Trial-Courts.ashx>.

<sup>18</sup> See FINRA Dispute Resolution Statistics, *supra* n. 14.

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technology used affects how often persons will lie. Notably, one study found that persons “are more likely to lie (and to be lied to) on the telephone than in any other medium.”<sup>19</sup>

Allowing associated persons to appear telephonically introduces additional risks into the expungement hearing. With a telephonic appearance, the arbitrators cannot observe whether the associated person is reading prepared remarks or looking to another person for coaching and signals about how to answer questions. These risks diminish with in person or videoconference appearances.

Requiring videoconference appearances for an associated person does not create an undue burden because videoconference technology is widely available at a low cost. When an associated person seeks extraordinary relief, and it is not unreasonable to require that person to “appear.”

FINRA should also ensure that customers associated with the underlying complaint or arbitration have the right to participate in expungement hearings. Although it would be inappropriate to name customers as parties in expungement proceedings, legitimate expungement processes must notify customers of the proceedings and facilitate their ability to provide information to arbitrators. As FINRA modifies its rules, it should also enshrine the rights provided in its current guidance.<sup>20</sup> FINRA’s current guidance provides that customers should be allowed to appear with counsel at any expungement hearing and provide testimony telephonically, in person, or by any other method.<sup>21</sup> The guidance also makes clear that customers should be able to introduce documents, cross-examine witnesses, and present opening and closing arguments on the same terms as any other person appearing at the expungement hearing.<sup>22</sup>

7. Should the arbitrators on the Expungement Arbitrator Roster have specific qualifications? If so, are the proposed additional qualifications appropriate or should FINRA consider other qualifications?

FINRA proposes that only chair-qualified public arbitrators, with the following additional qualifications, be included on the Expungement Arbitrator Roster: (1) completed enhanced expungement training; (2) admitted to practice law in at least one jurisdiction; and (3) five years’ experience in any of the following (a) litigation; (b) federal or state securities regulation; (c) administrative law; (d) service as a securities regulator; or, (e) service as a judge.

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<sup>19</sup> Jeffrey T. Hancock, *et al*, *Deception and Design: The Impact of Communication Technology on Lying Behavior*, Proceedings of the 2004 Conference on Human Factors in Computing Systems (pp. 129-134), <https://pdfs.semanticscholar.org/7ac6/4e54d377d2e765158cb545df5013e92905da.pdf>.

<sup>20</sup> Notice on Expanded Expungement Guidance, *supra* n. 4.

<sup>21</sup> *Id.*

<sup>22</sup> *Id.*

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As proposed, the Neutral List Selection System (NLSS) would randomly select three names from the Expungement Arbitrator Roster, with no strikes by the parties permitted, but allowing the parties to challenge an arbitrator for cause.

PIABA supports the FINRA Dispute Resolution Task Force's recommendation that arbitrators on a special expungement hearing panel be chair-qualified public arbitrators, with additional training on expungement. The training should emphasize the importance of the CRD and BrokerCheck and their relationship to investor protection. As FINRA itself has stated, "[e]nsuring that CRD information is accurate and meaningful is essential to investors, who may rely on the information when making decisions about brokers with whom they may conduct business; to regulators, who rely on the information to fulfill their regulatory responsibilities; and to prospective broker-dealer employers, who rely on the information when making hiring decisions."<sup>23</sup>

PIABA is concerned, however, that some areas of the country would have difficulty filling the proposed Expungement Arbitration Rosters with local chair-qualified arbitrators. PIABA has previously identified the "traveling arbitrator" problem in general panel selection, resulting in arbitrators assigned to cases unfamiliar with local securities laws and complicating case scheduling. PIABA in no way suggests reducing the additional qualifications proposed by FINRA, but FINRA must continue to make significant efforts in recruiting chair-qualified arbitrators in underserved areas to bolster the local Expungement Arbitration Roster.

In addition, PIABA supports FINRA's proposal that the Expungement Arbitrator panel be randomly selected. Random selection will reduce the risk of arbitrators being concerned about ruling against an associated person for fear they may not be selected for another panel.

8. Should the arbitrators on the Expungement Arbitrator Roster be lawyers only or could the experience of serving on three arbitrations through award be a sufficient substitute?

PIABA believes that Expungement Arbitrators should be licensed attorneys. This is a practical consideration – requiring service on three arbitrations through award would likely reduce the number of arbitrators qualified to be on the Expungement Arbitration Roster, exacerbating the issue of "traveling arbitrators" in certain areas of the country and as such, it would not be a sufficient substitute to an attorney-only roster.

Because the Rule 2080 grounds for expungement require a different weighing of evidence than deciding the merits of the underlying claim, arbitrators with legal training may be better equipped to make the distinction. For example, as mentioned above, even though a panel may determine that a claimant has not provided sufficient evidence to win on the merits of his or her underlying case, the evidence presented

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<sup>23</sup> Notice on Expanded Expungement Guidance, *supra* n. 4.

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may still be insufficient to prove that the claim was “factually impossible or clearly erroneous,” or “false,” or that the associated person was “not involved.”<sup>24</sup> Legal training may assist the arbitrator in understanding the differences in these evidentiary burdens, and be a benefit to protecting the integrity of the CRD and BrokerCheck systems.

9. How would the proposed amendments affect the granting or denying of expungement requests? Which aspect of the proposed amendments would have the largest impact on expungement determinations? Why?

FINRA’s codification of its own guidance on expungement is very important to improving the expungement process. Currently, FINRA Rule 12805 requires that the arbitrators “[i]ndicate in the arbitration award which of the Rule 2080 grounds for expungement serve(s) as the basis for its expungement order and provide a brief written explanation of the reason(s) for its finding that one or more Rule 2080 grounds for expungement applies to the facts of the case.” However, FINRA Rule 2080 does not set forth expungement standards; it sets forth standards that must be met if an associated person is requesting that FINRA waive the obligation within the rule to name FINRA as a party in a court action to confirm an arbitration award recommending expungement.

PIABA supports amendments to the rules that would clarify that an arbitration panel may not recommend expungement on grounds other than those set forth in Rule 2080, and that the panel must also determine whether the customer dispute information has any meaningful investor protection or regulatory value before recommending expungement.

Clarifying the standards governing expungement in the rules, in conjunction with training a special pool of arbitrators to consider the requests, may lead to some success in ensuring expungement is only recommended when appropriate. In addition, ensuring that expungement requests are made in a timely fashion encourage customer participation in the process, allowing the arbitrators to make a more informed decision.

10. The proposal would establish a one-year limitation period for associated persons to expunge customer dispute information that arose from a customer complaint. The limitation period would start on the date that the member firm initially reported the customer complaint to CRD. Should the one-year limitation period be based on a different milestone? If so, what should it be?

PIABA has concerns about commencing the limitation period on the report date because FINRA’s member firms and associated persons control the date when reports

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<sup>24</sup> See FINRA Rule 2080 (b)(1).

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are made. This liberal commencement date introduces risks that member firms or associated persons might benefit from delaying the reporting of complaints to the CRD. PIABA believes that the one year limitation period should run from the shorter of (i) a month after the associated person received notice of the customer complaint or (ii) from the date the member firm initially reported the customer complaint to the CRD.

11. The proposal would clarify for arbitrators that the standard for granting the permanent removal of customer dispute information from CRD is a finding that at least one of the Rule 2080(b)(1) factors applies and that the customer dispute information has “no investor protection or regulatory value.” Are there specific factors that arbitrators should consider when making a finding that the customer dispute information has “no investor protection or regulatory value”?

The current factors set forth in Rule 2080 may help inform the arbitration panel as to whether or not customer dispute information has any investor protection or regulatory value. Unfortunately, in practice, it appears that arbitration panels often believe the Rule 2080 standards are easily met. There seems to be some confusion amongst arbitration panels as to the burden of establishing whether a claim was “factually impossible or clearly erroneous,” or “false,” or that the associated person was “not involved.”<sup>25</sup> Further, it seems that Panels often do not grasp the fact that a customer may not have met his or her burden for purposes of establishing liability, or that an affirmative defense was available to limit liability, but this does not mean the claim is factually impossible or false. Yet, that is often the reason used by arbitration panels to support their recommendation of expungement. It must be clear that the standards set forth in Rule 2080 are high standards, distinct from those employed to determine liability.

Requiring that an arbitration panel to find that customer dispute information does not have any investor protection or regulatory value because it fits into one of the categories set forth in Rule 2080 emphasizes the notion that arbitrators’ actions have significant repercussions on investor protection. Moreover, enhanced training should further reinforce the importance of the disclosure of customer dispute information, regardless of the outcome of the underlying arbitration.

12. In a simplified arbitration case, if a customer requests a hearing, should the single arbitrator be permitted to decide an expungement request, if a request is filed?

PIABA supports FINRA’s proposal to require that a request for an expungement in a simplified case not be considered during the underlying arbitration, but rather that a claim be filed pursuant to proposed Rule 13805(a). FINRA’s proposal addresses flaws in the current process, whereby a hearing is held to consider the expungement request even though the customer chose not to elect a hearing under Rule 12800. It will also

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<sup>25</sup> See FINRA Rule 2080 (b)(1).

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eliminate delays in securing an award in the simplified case because the arbitrator is considering the request for expungement.

However, PIABA contends that a single arbitrator should not be permitted to decide an expungement request in a simplified arbitration case. The proposed amendments regarding expungement recognize, among other things, that expungement of CRD information is “an extraordinary measure” and that “the integrity and reliability of CRD information is *critical* to the needs of the stakeholders,” including investors, the SEC, FINRA, employers, and state and other regulators.<sup>26</sup> The proposed amendments are designed, in part, to make the stakeholders “more confident in the reliability” of CRD information and to make the CRD information “more meaningful and valuable” to stakeholders.<sup>27</sup>

These goals should not be affected—and the proposed amendments should not be diminished—simply because a given incident of misconduct involved \$50,000 or less (and therefore was governed by FINRA’s Simplified Arbitration procedure).<sup>28</sup> If FINRA were to permit a single arbitrator to decide an expungement request, that request would not be decided with the benefit of the additional safeguards put in place by the proposed amendments, including:

- (1) that the request be decided unanimously by a three-person, randomly selected, panel of public chairpersons;<sup>29</sup> and
- (2) that the members of the panel be selected from FINRA’s Expungement Arbitrator Roster, which ensures that the panel members have certain qualifications, including:
  - a. completed enhanced expungement training;
  - b. admitted to practice law in at least one jurisdiction; and
  - c. five years’ experience in any one of the following disciplines:
    - i. litigation;
    - ii. federal or state securities regulation;
    - iii. administrative law;
    - iv. service as a securities regulator; or
    - v. service as a judge.<sup>30</sup>

That the amount in dispute in an arbitration proceeding is \$50,000 or less should not have any effect on the manner in which a member’s or associated person’s request for

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<sup>26</sup> See FINRA Regulatory Notice 17-42 at 3, 13, *supra* n. 3.

<sup>27</sup> See FINRA Regulatory Notice 17-42 at 15, *supra* n. 3.

<sup>28</sup> See FINRA Rules 12800 and 13800.

<sup>29</sup> See proposed FINRA Rule 13806(b)(1).

<sup>30</sup> See proposed FINRA Rule 13806(b)(2).

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expungement is handled. There must be uniformity in the expungement process to ensure that all stakeholders maintain their confidence in the system.

Generally, PIABA supports the proposed changes to the expungement rules. However, PIABA believes that expungement requests would be best handled separate from the arbitration process. Whether customer dispute information should be disclosed is a determination that should be made by FINRA itself, in conjunction with its oversight of the CRD system. It is not a determination that should be made by an arbitrator, whose purpose is to determine whether an associated person is liable to a customer. While the proposed changes should improve the process, PIABA is hopeful that FINRA will continue to examine these issues and consider other means by which expungement requests may be considered.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Andrew Stoltmann". The signature is fluid and cursive, with a long horizontal stroke at the end.

Andrew Stoltmann  
PIABA President

Feel free to contact me. I think the system/process is broken to start with. I have 4 disclosures...all frivolous and how have prospective new clients judging me, not the claimants, based on the disclosure alone, not on the merits/facts of the claims.

Request for Comment FINRA is interested in receiving comments on all aspects of the proposed amendments. In particular, FINRA seeks comment on the following questions:

1. FINRA Rules 12805 and 13805 provide, in relevant part that, in order to grant expungement of customer dispute information under Rule 2080, the panel must comply with the requirements stated in the rule. (Emphasis added.) FINRA notes, however, that if a panel issues an arbitration award containing expungement relief, the award must be confirmed by a court of competent jurisdiction and FINRA could decide to oppose the confirmation. Thus, as the associated person is required to complete additional steps after the arbitrators make their finding in the award before FINRA will expunge the customer dispute information, FINRA believes the word “grant” may not be an appropriate description of the panel’s authority in the expungement process. FINRA is considering changing the word to “recommend.” Please discuss whether the rule should retain “grant” or change to “recommend” or some other description to more accurately reflect the panel’s authority in the expungement process. “Grant” should be retained and that should be what is REQUIRED if awarded by a court of competent jurisdiction (i.e. the law).
2. Would named associated persons request expungement in every case to preserve the right to have the expungement claim heard and decided, either in the Underlying Customer Case or as a new claim under the Industry Code? If so, what would be the potential costs and benefits of a named person requesting expungement in every case?
3. Should FINRA consider bifurcating the expungement request from the customer’s claim in all cases relating to customer disputes? Yes. What would be the costs and benefits of such an approach?
4. What are the costs and benefits of requiring the unanimous consent of a three-person panel to grant all requests for expungement of customer dispute information? Costs, yes. Benefits, no.
5. Is the one-year limitation on being able to request expungement of customer dispute information appropriate? No. I currently still have two “Pending” cases one full year after completion. I’m not sure what sort of statute of limitation consumers have to file a complaint...but seems to be advisors should have similar time to consider and choose to expunge. Should the time period be longer or shorter? Longer. Please discuss. Regulatory Notice 17 December 6, 2017 17-42
6. Should the associated person who is requesting expungement be required to appear in person or by videoconference, rather than by phone, at the expungement hearing? No. Cost would be my reason.
7. Should the arbitrators on the Expungement Arbitrator Roster have specific qualifications? Yes. If so, are the proposed additional qualifications appropriate or should FINRA consider other qualifications?

8. Should the arbitrators on the Expungement Arbitrator Roster be lawyers only or could the experience of serving on three arbitrations through award be a sufficient substitute? I cringe at this...but feel they should be lawyers.

9. How would the proposed amendments affect the granting or denying of expungement requests? Unsure. Which aspect of the proposed amendments would have the largest impact on expungement determinations? Unsure Why?

10. The proposal would establish a one-year limitation period for associated persons to expunge customer dispute information that arose from a customer complaint. The limitation period would start on the date that the member firm initially reported the customer complaint to CRD. Should the one-year limitation period be based on a different milestone? If so, what should it be? See my answer to #5. Should be more than a year...should be based on "close" of case, not initial complaint. Mine took forever due to client lack of organization and couldn't figure out what to even go after us over.

11. The proposal would clarify for arbitrators that the standard for granting the permanent removal of customer dispute information from CRD is a finding that at least one of the Rule 2080(b)(1) factors applies and that the customer dispute information has "no investor protection or regulatory value." Are there specific factors that arbitrators should consider when making a finding that the customer dispute information has "no investor protection or regulatory value"? Yes – what was the outcome of the case (i.e. withdrawn, settled, denied, etc.) I find it absolutely abhorrent that claims remain on record regardless of outcome. I'm all for protecting the public from legitimate "Award/Judgement" cases but cannot understand, in a nation where you are innocent until proven guilty, that an advisor remains "guilty" by implied FINRA brokercheck disclosure in spite of the outcome of the case. In our society void of personal responsibility and suit happy legal system I am shocked this has yet to be challenged.

12. In a simplified arbitration case, if a customer requests a hearing, should the single arbitrator be permitted to decide an expungement request, if a request is filed? Yes...based on merits of the case.

Jason S. Tinklenberg, Partner

7401 S. Bitterroot Place Suite 100  
Sioux Falls, SD 57108  
Office: (605) 271-1386  
Fax: (605) 271-2561

Mobile: (605) 351-2867

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VOICE OF INDEPENDENT  
FINANCIAL SERVICES  
FIRMS AND INDEPENDENT  
FINANCIAL ADVISORS

**VIA ELECTRONIC MAIL**

February 5, 2018

Ms. Marcia E. Asquith  
Office of the Corporate Secretary  
The Financial Industry Regulatory Authority, Inc.  
1735 K Street, NW  
Washington, DC 20006-1506

Re: Regulatory Notice 17-42 | Expungement of Customer Dispute Information (Notice)

Dear Ms. Asquith:

On December 6, 2017, the Financial Industry Regulatory Authority, Inc. (FINRA) published its request for public comment on proposed amendments to FINRA's rules governing expungement of customer related dispute information (Proposed Amendments).<sup>1</sup> The Proposed Amendments, which make substantive changes to the expungement process,<sup>2</sup> are part of a series of changes FINRA is considering.<sup>3</sup>

The Financial Services Institute<sup>4</sup> (FSI) appreciates the opportunity to comment on this important proposal. FSI has supported, and continues to support, restrictions on financial advisors' ability to expunge truthful and accurate disparaging information from the Central Registration Depository (CRD) and, consequently, from FINRA's BrokerCheck system. The absence of such restrictions would pose a risk to investors because, among other things, it would make it easier for high-risk or recidivist brokers to move through the industry undetected. It would also impede regulators' ability to execute their oversight responsibilities and would deny investors access to important information.

FSI believes, however, that any restrictions imposed should be unambiguous, reasonable, tied to an articulable regulatory objective, and balanced with financial advisors' needs to eradicate information that is misleading, meaningless, or that has no regulatory or investor protection value.

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<sup>1</sup> See, generally, Regulatory Notice 17-42 (December 6, 2017) (Notice).

<sup>2</sup> See, generally, Notice.

<sup>3</sup> *Id.* at p.1.

<sup>4</sup> The Financial Services Institute (FSI) is an advocacy association comprised of members from the independent financial services industry, and is the only organization advocating solely on behalf of independent financial advisors and independent financial services firms. Since 2004, through advocacy, education and public awareness, FSI has been working to create a healthier regulatory environment for these members so they can provide affordable, objective financial advice to hard-working Main Street Americans.

### **Background on FSI Members**

The independent financial services community has been an important and active part of the lives of American investors for more than 40 years. In the US, there are more than 160,000 independent financial advisors, which account for approximately 52.7 percent of all producing registered representatives.<sup>5</sup> These financial advisors are self-employed independent contractors, rather than employees of the Independent Broker-Dealers (IBD).<sup>6</sup>

FSI's IBD member firms provide business support to independent financial advisors in addition to supervising their business practices and arranging for the execution and clearing of customer transactions. Independent financial advisors are small-business owners and job creators with strong ties to their communities. These financial advisors provide comprehensive and affordable financial services that help millions of individuals, families, small businesses, associations, organizations, and retirement plans. Their services include financial education, planning, implementation, and investment monitoring. Due to their unique business model, FSI member firms and their affiliated financial advisors are especially well positioned to provide Main Street Americans with the affordable financial advice, products, and services necessary to achieve their investment goals.

FSI members make substantial contributions to our nation's economy. According to Oxford Economics, FSI members nationwide generate \$48.3 billion of economic activity. This activity, in turn, supports 482,100 jobs including direct employees, those employed in the FSI supply chain, and those supported in the broader economy. In addition, FSI members contribute nearly \$6.8 billion annually to federal, state, and local government taxes. FSI members account for approximately 8.4% of the total financial services industry contribution to U.S. economic activity.<sup>7</sup>

### **Discussion**

FSI appreciates the opportunity to comment on the Proposed Amendments. As stated above, FSI supports reasonable restrictions on financial advisors' ability to expunge customer dispute information from CRD. To that end, FSI believes that the Proposed Amendments should provide more flexibility with respect to how long an advisor has to initiate an expungement request. Further, FSI is concerned that participants on the Expungement Arbitrator Roster are not required to have securities industry experience and, thus, may fail to appreciate the factual nuances that gave rise to the customer's allegations against the advisor. FSI also has concerns that the arbitrators' standard of review, i.e., that the expunged information has no investor protection or regulatory value, is overly subjective and open to multiple and inconsistent interpretations. Therefore, FSI suggests that the Proposed Amendments eliminate that standard of review. Alternatively, FSI suggests that the Proposed Amendments include specific events that would meet that standard of review. These concerns and recommendations are discussed in greater detail below.

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<sup>5</sup> Cerulli Associates, Advisor Headcount 2016, on file with author.

<sup>6</sup> The use of the term "financial advisor" or "advisor" in this letter is a reference to an individual who is a registered representative of a broker-dealer, an investment adviser representative of a registered investment adviser firm, or a dual registrant. The use of the term "investment adviser" or "adviser" in this letter is a reference to a firm or individual registered with the SEC or state securities division as an investment adviser.

<sup>7</sup> Oxford Economics for the Financial Services Institute, The Economic Impact of FSI's Members (2016).

## I. FSI's Comments

### A. Introduction & Background

CRD has several important functions. First, investors rely on CRD information, made available to them through FINRA's BrokerCheck, to assist them in deciding whether to do business with a particular financial advisor.<sup>8</sup> Regulators use CRD to execute regulatory oversight and, at times, to identify industry trends.<sup>9</sup> Broker dealers use CRD information as a basis for its hiring decisions.<sup>10</sup> For those reasons, information contained in CRD, if it is inaccurate or confusing, may cause regulators to misidentify trends and, important to FSI's advisor members, may directly result in advisors losing clients, new business opportunities or employment opportunities.

Notably, in addition to collecting information regarding fully adjudicated customer-related matters, CRD also contains other customer dispute information, such as customer claims that have been settled. It is important to keep in the mind that every settlement is not tantamount to admission of guilt. In fact, financial advisors frequently agree to settle claims as part of an overall settlement agreed to by the broker dealer they are associated with at the time of the alleged misconduct. Financial advisors also, individually, decide to settle an action, even ones they believe are without merit, to avoid the cost and expense associated with arbitration or litigation or due to the unpredictable nature of the same.

In these cases, the financial advisor may not have engaged in any wrongdoing. This is why the need to balance investor protection and regulatory value, with advisors' rights, becomes so important. Hence, in implementing its series of changes to the expungement to the process, FINRA should consider these financial advisors; and not only the high risk, recidivist, or other advisors who pose an inherent threat to investor protection.

### B. Financial Advisors Should Have Three Years to Bring Expungement Proceedings

Financial advisors may seek to have customer dispute information removed from CRD, pursuant to FINRA Rule 2080, if the claim, allegation or information is factually impossible, clearly erroneous, false or the financial advisor "was not involved in the alleged investment related sales practice violation, forgery, theft, misappropriation or conversion of funds."<sup>11</sup> Thus, there are limitations on the circumstances in which expungement may be appropriate. This aligns with FINRA's philosophy that "expungement of customer dispute information is an extraordinary measure."<sup>12</sup>

The Proposed Amendments would require that expungement requests be made at the conclusion of a case.<sup>13</sup> If the matter concludes by means other than an award (i.e., the matter is settled), the Proposed Amendments would require financial advisors to make expungement requests within one-year of FINRA closing the arbitration or, if there was no arbitration, within one

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<sup>8</sup> See FINRA Office of Dispute Resolution Arbitrator's Guide, at p. 72 available at <http://www.finra.org/sites/default/files/arbitrators-ref-guide.pdf>.

<sup>9</sup> *Id.*

<sup>10</sup> *Id.*

<sup>11</sup> See FINRA Rule 2080 (b)(1) (A) – (C).

<sup>12</sup> See Notice at p. 4.

<sup>13</sup> See Proposed Rule 13800(f).

year of the information being reported to CRD.<sup>14</sup> According to the Notice, these time limitations are designed to ensure that information regarding the underlying allegations would still be available and that customers would be more likely to participate in the expungement proceedings.<sup>15</sup> FSI agrees there should be some time limitations imposed, but suggests three years as a more reasonable alternative.

Broker dealers are required to maintain books and records related to their business for time periods prescribed by FINRA rules and by rules promulgated by the US Securities and Exchange Commission. Thus, it is unlikely that a longer delay would substantially impair access to pertinent information. Also, in the event that the arbitrators determine that, after the three-year period, there is not sufficient available information to rule in the advisor's favor, the arbitrators may simply rule against the advisor.

With respect to customers' participation in expungement proceedings, that participation is at the customer's discretion. There is no guarantee that the one-year limitation, versus a three-year limitation (or longer), would make customers want to expend the time and financial resources necessary to attend the expungement proceedings. On the other hand, the one-year limitation undoubtedly impacts financial advisors by imposing additional hurdles to the expungement process. It also inserts imbalance in the system since the Code of Arbitration Procedures gives customers six years to bring claims.<sup>16</sup>

Advisors should not be unfairly prejudiced based upon the mere chance that a customer may decide he or she wants to appear at the proceeding. This is particularly true since there are no additional factors, other than the customer's desire to do so, that would impede the customer from attending the proceeding three years later. Nonetheless, this additional time would give financial advisors the opportunity to, among other things, assess how the information will impact the advisor's ability to do business, retain appropriate legal representation, and work with the advisor's attorney to determine litigation strategy. At times, the impact on the advisor's ability to do business may not be immediately apparent.

C. Qualifications for Arbitrators to Appear on the Expungement Arbitrator Roster Should be Broadened to Include Persons Who Have Worked in the Securities Industry in a Registered Capacity

Three public chairpersons chosen from an Expungement Arbitrator Roster (Roster) would decide certain expungement cases. Selection is random.<sup>17</sup> To be included on the Roster, public chairpersons must receive enhanced training, be licensed attorneys, and have five-years' experience either in litigation, state or federal securities regulation, serving as a judge, in administrative law or serving as a securities regulator.<sup>18</sup> FINRA believes that these requirements will help it "maintain the integrity of its CRD records and ensure that expungement is only granted in appropriate circumstances."<sup>19</sup> Based on these requirements, and the random selection process, it

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<sup>14</sup> See Proposed Rule 13805(a)(3).

<sup>15</sup> See Notice at p. 7.

<sup>16</sup> See Sec. 12206, FINRA Code of Arbitration.

<sup>17</sup> See Proposed Rule 13806 (b)(1)

<sup>18</sup> See Proposed Rule 13806 (b)(2).

<sup>19</sup> See Notice at p. 10.

is possible to have a panel consisting of three licensed attorneys, who are trained in expungements, but who lack any meaningful securities industry experience.<sup>20</sup>

FSI is concerned that while these persons may understand the importance of maintaining public records, they may not understand the securities industry. Without this understanding, it may be difficult to appreciate whether information has regulatory significance or investor protection value. FSI, therefore, suggests that industry participants who have worked as a general securities principal for a least five consecutive years, in the prior seven-year period, be eligible for inclusion on the Roster. Persons meeting those requirements would be eligible for inclusion regardless of whether they are attorneys, providing however, that they do not have any disciplinary history. While this would, in certain cases, mean that the panel would be semi-public, as noted, this person would be able to speak to, and access, the integrity of the underlying facts.

FSI also suggests that, at least one person on each three-person panel be required to have securities industry experience either as general securities principal that meets the qualifications outlined above; or as an attorney who has the requisite five years' experience in state or federal securities regulation or as a securities regulator. This will help ensure that one person on the panel not only understands the general importance of maintaining records, but also understands the factual nuances that gave rise to the customer dispute, as well as whether the information has regulatory and investor protection value.

D. The Proposed "No Investor Protection or Regulatory Value" Standard Is Subjective and Ambiguous

Under the Proposed Amendments, arbitrators must agree unanimously and in the arbitration award:

1. include findings that one or more of the grounds for expungement set forth in Rule 2080(b)(1)<sup>21</sup> apply;
2. provide a written explanation for its determination that the grounds apply; and
3. determine that "the customer dispute information has no investor protection or regulatory value."<sup>22</sup>

Perhaps, this requires clarification; however, it appears that this is a multi-part test requiring that arbitrators both determine that: (i) one of the enumerated grounds in Rule 2080(b)(1) apply; and (ii) independently, determine that the information has no investor protection or regulatory value. Thus, conceivably, even in the presence of one of the grounds set forth in 2080(b)(1), arbitrators may deny a request for expungement if the information has investor protection or regulatory value. This is confusing as it is difficult to imagine a scenario where information that is false, clearly erroneous, factually impossible or did not involve the advisor, would have regulatory or investor protection value.

To the extent that the investor protection or regulatory value standard, was meant to be an independent standard of review, while FSI unequivocally supports this as a *concept*; it is concerned that, as a rule-based standard of review, it is subjective, ambiguous and open to

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<sup>20</sup> *Id.*

<sup>21</sup> The available defenses under FINRA Rule 2080 (b)(1) are that the claim, allegation or information is factually impossible, clearly erroneous or false or that the registered person was not involved in the conduct.

<sup>22</sup> See Proposed Rule

multiple and inconsistent interpretations. More specifically, the grounds set forth in Rule 2080(b)(1) (e.g., the information is demonstrably false, clearly erroneous, impossible, etc.), creates an objective standard of review that can be easily understood by financial advisors and applied by arbitrators. Conversely, whether information has value is subjective, ambiguous and, consequently, renders that review process patently unpredictable. This would likely lead to various rulings based on facts that are the same, or substantially similar. Thus, FSI suggests that language be eliminated, or that FINRA consider including supplementary material in the rule clarifying how that portion of the standard or review should be applied.

## II. Disclosure by Unnamed Parties

Firms are required to report, as customer complaints, allegations of sales practice violations made in arbitration claims and civil lawsuits against financial advisors who are not named as parties in those proceedings. This, often, results in a lack of due process for the unnamed advisor as it results in the unnamed financial advisor with a negative mark on his Form U-4 even though the advisor did not have the opportunity to participate in the arbitration. Also, without the advisor having been present to offer his narrative of the events, with respect to the advisor, the arbitration panel is left with a one-sided presentation of the facts. Hence, any regulatory value of disclosing these on the Form U-4 is greatly diminished. Thus, FSI suggests that FINRA no longer require advisors to disclose arbitration, settlements in which the advisor was not named.

### Conclusion

We are committed to constructive engagement in the regulatory process and welcome the opportunity to work with FINRA on this and other important regulatory efforts.

Thank you for considering FSI's comments. Should you have any questions, please contact me at (202) 393-0022.

Respectfully submitted,



Vice President, Regulatory Affairs & Associate General Counsel



VIA ELECTRONIC MAIL

February 5, 2018

Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

**Re: Regulatory Notice 17-42, Modifications to Expungement Process**

Dear Ms. Asquith:

In its Regulatory Notice 17-42, the Financial Industry Regulatory Authority, Inc. ("FINRA") solicited comments regarding proposed changes to rules affecting the expungement process.

Commonwealth Financial Network® ("Commonwealth") is an independent broker/dealer and an SEC-registered investment adviser with home office locations in Waltham, Massachusetts, and San Diego, California, and more than 2,000 registered representatives ("RRs") who are independent contractors conducting business in all 50 states.

For the reasons set forth below, Commonwealth joins the many other individuals and firms that have already expressed concerns with the proposed modifications.

**The Proposed Rules Have no Real Benefit**

Nothing contained in the new rules will make the industry more transparent, create more investor confidence, or stop scoundrels from being scoundrels. Rather, the proposed rules simply make it harder for reputable RRs to deal with spurious allegations lodged by irrational customers who understand that a written complaint can be used as leverage to demand compensation for the slightest perceived wrong.

The system, as presently constituted: (i) already sufficiently accommodates customers who want to lodge complaints; (ii) already requires disclosure of minor complaints that serve no public purpose; and (iii) already requires a RR to make a substantial outlay of money and time to seek expungement – with no guarantee that it will succeed.

If FINRA believes that expungement is being granted at too frequent a rate, it should consider first studying the merits of the cases that are being expunged before it determines that expungement is being granted too liberally. It is much more likely that the FINRA-trained arbitrators granting the expungement awards (who are required to be chairperson certified) have

29 Sawyer Road  
Waltham, MA 02453-3483  
800.237.0081  
781.736.0793 fax

110 West A Street, Suite 1800  
San Diego, CA 92101-3706  
877.347.1982  
619.471.9701 fax

[commonwealth.com](http://commonwealth.com)

Member FINRA/SIPC

Marcia E. Asquith  
February 5, 2018  
Page 2 of 2

determined that the disclosures are unwarranted than it is that the expungement standards aren't high enough.

### **FINRA Should Change U4 Criteria Before Considering Expungement Modifications**

FINRA needs to amend the criteria for disclosure of customer complaints on RR U4s. The bar for disclosure is so low that almost any written complaint requires disclosure. Particularly, the \$5,000 threshold should be drastically increased. It is an amount so de minimis that it is essentially superfluous.

Many frivolous and meritless complaints are required to be disclosed on RR U4s under the current rubric. These complaints are unduly prejudicial in this day and age when anyone with internet access can view RR's disclosures. Most customers that avail themselves of online disclosure information likely do not understand how easy it is for a customer complaint to become disclosable. Therefore, their assumption is that the disclosure must reflect something serious. This is unnecessarily prejudicial to RRs that bear the brunt of such complaints through no fault of their own.

Although some disclosures may be relevant to the consumer in choosing a RR, complaints should be acknowledged as an expected cost of doing business – not be treated as out of the ordinary “scarlet letters” that taint a customer's opinion of a RR because of an outdated standard.

If FINRA chooses to make it more difficult to expunge complaints it should ensure that only legitimate and warranted complaints are disclosed in the first place. This would include, at a minimum: (i) drastically increasing the alleged damages threshold; (ii) narrowing the definition of “sales practice violation”; and (iii) modifying the process such that clearly false or uncorroborated allegations do not require disclosure.

### **FINRA Should Change Brokercheck Criteria Before Considering Expungement modifications**

Similar to the U4 concerns above, FINRA's Brokercheck site also unfairly publicizes certain RR disclosures. Although to a large extent the U4 and Brokercheck are one and the same, it is noteworthy to recall that the U4 requires only disclosure of certain customer complaints that have been lodged within the most recent 24 months. Yet those same complaints apparently remain on Brokercheck in perpetuity. This is also unnecessarily prejudicial to RRs as these complaints remain publicly available well beyond the time they are of any public benefit.

Sincerely,



Joe Tally  
Assistant General Counsel

February 5, 2018

Financial Industry Regulatory Authority  
Attn: Marcia E. Asquith  
Office of the Corporate Secretary  
1735 K Street NW  
Washington, DC 20006-1506

Re: FINRA Regulatory Notice 17-42

Dear Ms. Asquith:

Please accept this public comment to FINRA's Proposed Amendments to the Codes of Arbitration Procedure Relating to Requests to Expunge Customer Dispute Information. I am an attorney who has represented clients seeking expungement of customer dispute information from their CRD and BrokerCheck Reports. I have firsthand knowledge of the difficult position these associated persons often find themselves in, and the already uphill battle they face to ensure their BrokerCheck Report accurately reflects their record, provides sufficient investor protection, and has regulatory value. The proposed amendments would render this process even more cumbersome, timely, and difficult for these clients – clients who do merit this “extraordinary measure” of customer dispute expungement.

I would like to provide you with a few real examples of client cases I have handled:

- 1) One client was erroneously named in a dispute that was actually meant for his father. The father and son had the same names, and the customer mistakenly named the son instead of the father. This matter went on the son's record, despite the subsequent discovery that he had been mis-named.
- 2) One client provided sound investment advice to his customer, given the customer's stated investment objectives and risk tolerance. However, unbeknownst to our client or to many other brokers and broker-dealer firms, the company that issued this particular note, and its executives, were engaging in securities fraud, misconduct, running a Ponzi scheme, and selling unregistered securities. The company's executives later pleaded guilty to numerous securities fraud allegations and the company soon went bankrupt. As such, the customer had no remedy with the company and filed a complaint against our client and our client's firm, in an effort to recoup some of the money lost. This matter went on our client's record, despite that he had no involvement in the securities fraud allegations and had justifiably relied on the performance of the company at the time the recommendations were made to the customer.
- 3) One client provided sound investment advice to his customer, given the customer's stated investment objectives and risk tolerance. The customer invested in a Limited Partnership. However, years later, the tax code was amended, which negatively affected the customer's investment in the Limited Partnership. As the customer certainly could not file a complaint against the IRS, the customer filed a complaint against our client.

- 4) One client provided sound investment advice to his customer (a married couple), given the customer's stated investment objectives and risk tolerance. Auction Rate Securities (ARS) were highly successful at that time and our client recommended the customer purchase ARS. The couple later divorced, with each receiving half of the ARS purchases pursuant to the divorce arrangement. The wife subsequently transferred her accounts to another firm, and our client was no longer her broker. The ARS market later failed as a result of the 2008 financial crisis. Although our client's firm offered to repurchase ARS from many affected customers, the wife was not eligible for repurchase under the firm's repurchase terms because she was no longer a customer. She filed a complaint against our client in an effort to force the firm to repurchase her ARS.
- 5) One client provided sound investment advice to his customer, given the customer's stated investment objectives and risk tolerance. The customer invested in a Real Estate Investment Trust (REIT). At the time of the customer's investment, general industry practice was to use the offering price of REIT securities as the per share estimated value during the offering period. The offering price generally remained constant on a customer's account statements during the entire offering period, even though fees had actually reduced investors' principal and value of the underlying assets may have decreased. In order to address this concern, in January 2015, the SEC approved a rule change to require inclusion in customer account statements a per share estimated value for a REIT. The rule change mandated disclosure of the "net investment" amount on customer account statements. Despite our client's efforts to explain the effects of this rule change on the customer's statements, the customer did not understand and perceived that her REIT had dropped in price per share. She subsequently filed a complaint against our client.

These are merely a few examples of the hundreds of brokers who have had to spend thousands of dollars in an effort to expunge matters from their public BrokerCheck Reports that never should have been on their reports in the first place. Each of these clients certainly had an extraordinary circumstance warranting expungement. FINRA now proposes to make an already burdensome and costly back-end expungement process even more burdensome and costly. It does so without easing the front-end reporting obligations that force these disclosures onto BrokerCheck Reports. Firms' compliance departments are inclined to over-report customer disputes because firms are not willing to take the risk in not reporting these matters.

**Proposed Requirement That an Associated Person Seek Expungement Within One Year.** FINRA proposes to impose a one-year statute of limitations upon an associated person seeking expungement of a customer dispute that did not result in an arbitration claim. There seems to be no reason for this requirement, other than to further restrict an associated person's ability to expunge matters from BrokerCheck. In fact, the requirement seems to fly in the face of FINRA's desire for BrokerCheck to provide accurate investor protection and regulatory value. If FINRA is concerned with investors having accurate information regarding associated persons, and providing associated persons with expungement remedy for extraordinary circumstances, such as those outlined above, this time limit should not be imposed. When a member firm "initially" reports a customer complaint on an associated person's CRD, the member firm has not even had time to investigate or resolve the complaint. Member firms do – and should – conduct thorough investigations into customer complaints. These investigations and the resolution of the complaint can often take months, up to a year. It would be impossible for the associated person to begin the expungement process while the complaint is still being investigated. Furthermore,

the associated person must have the funds available to pay for the costly process of expungement. The associated person may not have those funds immediately available, and may need more time to file for expungement. Finally, in many cases, an associated person has left a member firm and a complaint is subsequently filed after the associated person's departure. In those cases, the member firm and the associated person are not in close communication and there is an even greater lag time before the associated person becomes aware of the disclosure. For all of these reasons, a one-year time limit is unnecessary, unfair, and not practical. It appears to fly in the face of the intent of BrokerCheck.

**Proposed Requirement That a Three-Person Panel Hear Expungement Requests.** FINRA arbitrators are well-equipped to read Statements of Claim, review evidence, hear testimony, and apply FINRA Rule 2080(b)(1) to the facts of an expungement request. Certainly, if the proposed rule to create a roster of arbitrators with additional qualifications to decide expungement requests is passed, a single arbitrator with these special qualifications will be more than qualified to make a determination as to expungement. Imposing a burden of having three "specially qualified" arbitrators hear a single expungement case would be unnecessarily burdensome to all involved, and provides no additional value to the process. Even criminal proceedings presided over by a single judge are less onerous than what is being proposed by this rule change. Having to coordinate the schedules of three arbitrators will delay the proceedings and will impose unnecessarily high additional arbitration costs on all parties involved. Seemingly, this proposed requirement is also creating a proposed increase in arbitration cost, as reflected in the proposed minimum filing fee of \$1,425. Associated persons spend thousands of dollars to expunge frivolous matters from their records. The process should be less burdensome, not more burdensome, and there is no value in having three "specially qualified" arbitrators review the case, doing the job of what a single "specially qualified" arbitrator with tailored training to hear expungement matters can do.

**Conclusion.** In sum, there are a number of reasons why a customer may file a false, frivolous, or erroneous complaint against an associated person. Associated persons cannot control who files a complaint, why they file a complaint, and what resolution the member firm chooses. Furthermore, associated persons cannot control the reporting of these complaints on BrokerCheck. Associated persons often have done everything right for their clients and will now have an even more difficult (and costly) time being able to have a report that consistently reflects that. I urge FINRA to reconsider these additional restrictions being placed on associated persons, which will have huge ramifications for them and their livelihood, and to keep the ultimate goal of investor protection in mind.

Respectfully,



Leslie M. Walter, JD

[leslie.m.walter@gmail.com](mailto:leslie.m.walter@gmail.com)

C: (512) 659-9628

For those who have been unjustly tarred by un-valid complaints and wish to clear our names, I'm disgusted that FINRA has chosen to increase the fee and to do so by over a thousand dollars. The fee by FINRA as it exists, is already 1500 dollars per complaint. That alone is extortion, but to raise that fee any further is unconscionable. It's behavior expected of loan sharks. There are many Financial advisors who are targeted by bad actors for a number of reasons. We need a fair and reasonable system to clear our names. At one point ,FINRA used to remove complaints that were unfounded. Staining someone's name forever by forcing them to pay extortion and go to court is a cheesy way to collect income from people who are already victims. Thanks FINRA. Now we can be victimized twice.

Stacie Weinerf  
Vice President- Financial Advisor  
RBC Wealth Managementpeople who are already victims  
Fax (413) 528-7159  
[Stacie.weiner@rbc.com](mailto:Stacie.weiner@rbc.com)  
NMLS # 140813 through City National Bank

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Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

Re: FINRA Regulatory Notice 17-42, December 6, 2017  
Comments on Proposed Rule Changes Regarding Expungement of Customer Dispute Information

Dear Ms. Asquith:

I am a FINRA public arbitrator. I have been a Chairperson and sole arbitrator in expungement arbitration proceedings in numerous customer and industry cases. My experience has included expungement proceedings following evidentiary proceedings, as well as stand-alone expungement proceedings. I am a practicing lawyer.

I share the viewpoint that arbitrators are not infrequently disadvantaged in hearing a customer expungement case when the arbitrator or panel has not had the benefit of additional information beyond the initial pleadings. When the customer settles the claim in advance of the evidentiary hearing and there has been no motion practice nor discovery conference, even the Chairperson has no knowledge besides the initial pleadings. Complicating this, the claimant may after settlement, send a one-line objection to the expungement request, and decline to participate directly, or through counsel, in the expungement proceeding. The panel or arbitrator must decide based upon the record of the expungement hearing only created by the broker seeking expungement, particularly when the notional past or current firm Respondent does not oppose the expungement. While the arbitrator or panel will challenge the broker's allegation of compliance with one of the 2080 standards, in the absence of the customer's involvement, this often done in a vacuum. For economic reasons, the customer generally does not appear or have his or her counsel file a brief or statement supporting the objection to the expungement. If the customer chooses to object it would be helpful if it was mandated that the customer participate in the hearing or file a substantive statement or brief opposing expungement. I don't see the proposed Rule changes under Regulatory Notice 17-42 making this a condition of customer objection to expungement. The proposed Rule changes, in my view, will not solve the problem that the Regulatory Notice aims to correct.

With regard to the specific proposals I offer a few general comments.

I. A. As a general matter, I have found that expungement is pled when the broker is a named party in the underlying action and is aware of it. On occasion I have seen a request made years after the underlying event, but the customer usually has long lost interest, if the customer can be located. Rule enhancement through time limitation and fees as expressed in the proposed Rule changes may benefit staff and limit these occasional issues but in my view, they do not address the stated purpose for this Regulatory Notice. As an arbitrator this is not a major concern. I leave to other commentators whether one-year is an appropriate time period.

I.B. Unnamed Persons: As an arbitrator I tend to see these matters in a separate expungement proceeding brought after the conclusion of the underlying dispute. Intervention is a strategic decision for counsel, although the expungement proceeding might change if the broker is a named party, and if

the customer ultimately participates in the expungement proceeding. The latter being the more relevant point.

II. Telephonic Hearing Session: Although I have a conceptual preference that aligns with live or video-conference hearings, I recognize that the latter may not be available and telephonic might be acceptable in limited circumstances. I believe arbitrators can make this determination and the Rule should not limit their flexibility to do so.

Unanimity and Additional Findings: I think both of these changes are harmful.

While there is a high bar for granting expungement, given that the hearing can often occur without evidence from the customer, the “unanimity” would still be based upon a limited record. Unanimity creates a veto power. It can cut both ways. Persuasion based upon majority decision is a better vehicle. Unanimity will create inefficiency if the panel deadlocks and will not improve the basis for the award.

Imposing the vague standard (“2) find that the customer dispute information has no investor protection or regulatory value”) on arbitrators would encourage the use of experts in expungement hearings who could testify on the record as to compliance with such standards. Given the potential of little information beyond the initial pleadings, it would be hard for arbitrators (or an expert) to make such a finding.

III.

Selection of the Panel: Notwithstanding that I would meet the proposed experience standards, I don’t think they are necessary. I have had panels composed of those who would qualify. Some have been well-qualified and diligent, and others less so. I think a capable non-lawyer could handle an expungement proceeding. I don’t think a separate Roster is needed. Oddly, litigation is listed as an experience skill, but not arbitration.

I previously commented on proposed changes repeated in III.B. and C.

IV. Simplified Arbitration.

I think it best that the arbitrator hearing the underlying claim hear the expungement request, if the broker was a named party. If unnamed, the same panel should hear the expungement arbitration if available, and only if not, should new arbitrators be substituted. The panel should, upon its request, have selected documents or testimony from the underlying proceeding made available to it in the separate expungement arbitration of an unnamed person.

Respectfully submitted,

Brooks White, Esq.  
FINRA Arbitrator

Dated: January 15, 2018

I urge you to please keep in place a process to expunge meritless claims against honest advisors. Our careers shouldn't be open to being harmed by meaningless claims that we have no ability to remove.

Thank you,  
Greg

*Greg Zanolli*  
*Sr. Financial Advisor – Wealth Management*  
*Senior Vice President - Investments*  
Wells Fargo Advisors

**Exhibit 2d**

**FINRA ARBITRATION**

**Request for Expungement of Customer Dispute Information on Behalf of an Unnamed Person**

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Case ID and Caption

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Name of Party Requesting Expungement

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Name of Associated Person Who is an Unnamed Person

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**Party Requesting Expungement**

1. The undersigned party (“party”) hereby notifies FINRA of the party’s intent to request expungement of customer dispute information on behalf of an associated person who is an unnamed person, pursuant to Rule 12805(a)(2).
2. The party requesting expungement of customer dispute information on behalf of the associated person agrees to represent the associated person for the purpose of requesting expungement during the investment-related, customer-initiated arbitration.
3. The requesting party may withdraw or not pursue the expungement request only with the written consent of the unnamed person. If the requesting party withdraws or does not pursue the expungement request, the arbitrator or panel shall deny the expungement request with prejudice.

**Associated Person Who is the Unnamed Person**

1. The undersigned associated person who is an unnamed person, as defined under Rule 12100(ff), consents to the party's expungement request on his or her behalf during the above-captioned case.
2. By signing the Form, the associated person agrees to maintain the confidentiality of any documents and information from the investment-related, customer-initiated arbitration to which the unnamed person is given access and to adhere to any confidentiality agreements or orders associated with the customer-initiated arbitration. Failure of the associated person to comply with these requirements could subject the associated person to a claim for damages by an aggrieved party.
3. The associated person agrees to be bound by the arbitrator's or panel's decision regarding the request for expungement of customer dispute information that the party to the arbitration filed on behalf of the associated person.
4. If the customer arbitration closes by award after a hearing, the associated person agrees that he or she will be barred from filing an expungement request for the same customer dispute information in a subsequent proceeding.

---

Party Name or Representative of Party Requesting Expungement on behalf of Associated Person  
(**please print**)

---

Party Name or Representative of Party Requesting Expungement on behalf of Associated Person  
(**signature**) **Date**

---

Name of Associated Person (**please print**)

---

Associated Person (**signature**) **Date**

## **EXHIBIT 5**

Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.

\* \* \* \* \*

### **12000. CODE OF ARBITRATION PROCEDURE FOR CUSTOMER DISPUTES**

\* \* \* \* \*

#### **12100. Definitions**

Unless otherwise defined in the Code, terms used in the Code and interpretive material, if defined in the FINRA By-Laws, shall have the meaning as defined in the FINRA By-Laws.

(a) through (ee) No Change.

#### **(ff) Unnamed Person**

For purposes of Rules 12800 and 12805, the term “unnamed person” means an associated person, including a formerly associated person, who is identified in a Form U4, Form U5, or Form U6, as having been the subject of an investment-related, customer-initiated arbitration claim that alleged that the associated person or formerly associated person was involved in one or more sales practice violations, but who is not named as a respondent in the arbitration claim.

\* \* \* \* \*

#### **12203. Denial of FINRA Forum**

(a) No Change.

(b) The Director shall decline the use of the FINRA arbitration forum if the Director determines that the expungement request is ineligible for arbitration under Rule 12805.

[(b)](c) Disputes that arise out of transactions in a readily identifiable market may be referred to the arbitration forum for that market, if the claimant agrees.

\* \* \* \* \*

### **12307. Deficient Claims**

(a) The Director will not serve any claim that is deficient. The reasons a claim may be deficient include the following:

(1) through (5) No Change.

(6) The claimant did not pay all required filing fees, unless the Director deferred the fees; [or]

(7) The claim does not comply with the restrictions on filings with personal confidential information under Rule 12300(d)(1);

(8) A request to expunge information from the CRD system arising from a customer dispute does not include the CRD number of the party requesting expungement;

(9) A request to expunge information from the CRD system arising from a customer dispute does not include the CRD occurrence number that is the subject of the request;

(10) A request to expunge information from the CRD system arising from a customer dispute does not include the case name and docket number of the arbitration that gave rise to the customer dispute information, if applicable; or

(11) A request to expunge information from the CRD system arising from a customer dispute does not include an explanation of whether expungement of the same customer dispute information was (i) previously requested and, if so (ii) how it was decided.

(b) through (c) No Change.

\* \* \* \* \*

**PART VIII SIMPLIFIED ARBITRATION, [AND] DEFAULT, AND  
EXPUNGEMENT PROCEEDINGS**

\* \* \* \* \*

**12800. Simplified Arbitration**

(a) through (c) No Change.

**(d) Requests to Expunge Customer Dispute Information**

**(1) When an Associated Person is Named as a Respondent**

(A) An associated person named as a respondent in a simplified investment-related, customer-initiated arbitration may request expungement during the arbitration of that customer dispute information arising from the customer's statement of claim, provided the request is not barred pursuant to Rule 12805(a)(1)(B).

(B) If an associated person named as a respondent requests expungement during the simplified investment-related, customer-initiated arbitration:

(i) the request must be filed in the answer or a pleading requesting expungement and meet the requirements of Rule

12805(a)(1)(C)(ii). If the associated person requests expungement in a pleading other than an answer, the request must be filed within 30 days after the date FINRA notifies the associated person of the appointment of the arbitrator or panel; and

(ii) the arbitrator or panel from the arbitration shall consider and decide the expungement request.

(C) If the associated person named as a respondent withdraws or does not pursue an expungement request after filing the request during the simplified investment-related, customer-initiated arbitration, the arbitrator or panel shall deny the expungement request with prejudice.

**(2) On Behalf of an Unnamed Person**

(A) A party to a simplified investment-related, customer-initiated arbitration may request expungement on behalf of an unnamed person during the arbitration of the customer dispute information arising from the customer's statement of claim with the written consent of the unnamed person, provided the request is not barred pursuant to Rule 12805(a)(1)(B).

(B) If a party requests expungement on behalf of an unnamed person during a simplified investment-related, customer-initiated arbitration:

(i) the request must be filed: (a) in compliance with Rules 12805(a)(1)(C)(ii), 12805(a)(2)(C)(ii), and 12805(a)(2)(D); and (b)

within 30 days after the date FINRA notifies the party of the appointment of the arbitrator or panel; and

(ii) the arbitrator or panel from the simplified arbitration shall consider and decide the expungement request.

(C) If the party, with the written consent of the unnamed person, withdraws or does not pursue an expungement request after filing the request during a simplified investment-related, customer-initiated arbitration, the arbitrator or panel shall deny the expungement request with prejudice.

**(e) Deciding Expungement Requests**

(1) If an associated person named as a respondent, or a party on behalf of an unnamed person, requests expungement during a simplified investment-related, customer-initiated arbitration, the expungement request shall be decided by the arbitrator or panel from the arbitration, as follows:

(A) No Hearing or Option Two Special Proceeding – If a customer requests no hearing pursuant to Rule 12800(c)(2), or an Option Two special proceeding pursuant to Rule 12800(c)(3)(B), the arbitrator or panel shall hold a separate expungement hearing pursuant to Rule 12805(c) to consider and decide the expungement request and issue the decision on the expungement request in a separate, subsequent award in accordance with Rule 12805(c)(8).

(B) Option One Hearing – If a customer requests an Option One hearing pursuant to Rule 12800(c)(3)(A), the arbitrator or panel shall consider and decide the expungement request, as follows:

(i) If the simplified arbitration closes by award after a hearing, the arbitrator or panel shall consider and decide the expungement request during the hearing pursuant to Rule 12805(c) and issue the decision on the request in the award in accordance with Rule 12805(c)(8).

(ii) If the arbitration closes other than by award or by award without a hearing, the arbitrator or panel shall hold a separate expungement hearing, pursuant to Rule 12805(c), to consider and decide the expungement request. At the conclusion of the expungement hearing, the arbitrator or panel shall issue an award in accordance with Rule 12805(c)(8).

(2) If an associated person named as a respondent, or a party on behalf of an unnamed person, does not request expungement of the customer dispute information arising from the customer's statement of claim during the simplified investment-related, customer-initiated arbitration, the associated person may request expungement pursuant to Rule 13805 after the simplified arbitration has closed, provided that the request is not barred by Rule 13805(a)(2).

**(f) FINRA Notifications**

(1) FINRA shall notify state securities regulators, in the manner determined by FINRA, of an expungement request within 30 days of receiving a complete expungement request.

(2) The Director shall notify all customers from the simplified customer arbitration of an expungement hearing conducted pursuant to Rules 12800(e)(1)(A), 12800(e)(1)(B)(ii) or 13805.

**[(d)](g) Discovery and Additional Evidence**

No Change.

**[(e)](h) Increases in Amount in Dispute**

No Change.

**[(f)](i) Arbitrator Honoraria**

No Change.

\* \* \* \* \*

**12805. Expungement of Customer Dispute Information under Rule 2080**

This Rule applies to all requests for expungement of customer dispute information under Rule 2080, except that when a party requests expungement of customer dispute information during a simplified arbitration pursuant to Rule 12800(d), only those sections of this Rule that are specifically referenced in Rule 12800(d) through (f) shall apply. Except as otherwise provided in this Rule, all other provisions of the Code apply to such expungement requests.

**(a) Requesting Expungement Under the Customer Code**

**(1) Requesting Expungement When Named as a Respondent**

**(A) Applicability**

An associated person named as a respondent in an investment-related, customer-initiated arbitration may request expungement during the arbitration of that customer dispute information arising from the customer's statement of claim, unless barred by Rule 12805(a)(1)(B). If the associated person does not request expungement in the arbitration, the associated person shall be prohibited from seeking to expunge the customer dispute information arising from the customer's statement of claim in any subsequent proceeding.

**(B) Limitations**

An associated person shall not file a request for expungement of customer dispute information if:

(i) an arbitrator or panel held a hearing to consider the merits of the associated person's request for expungement of the same customer dispute information; or

(ii) a court of competent jurisdiction previously denied the associated person's request to expunge the same customer dispute information.

**(C) Expungement Request**

(i) An associated person must include the expungement request in the answer or a pleading requesting expungement. If the associated person requests expungement in a pleading other than an answer, the request must be filed no later than 30 days before the first scheduled hearing; otherwise, pursuant to Rule 12309(b),

the associated person must file a motion pursuant to Rule 12503, seeking an extension to file the expungement request.

(ii) The expungement request must include:

a. the applicable filing fee;

b. the CRD number of the party requesting expungement;

c. each CRD occurrence number that is the subject of the request;

d. the case name and docket number that gave rise to the customer dispute information, if applicable; and

e. an explanation of whether expungement of the same customer dispute information was (i) previously requested and, if so (ii) how it was decided.

**(D) Arbitrator or Panel Decides Expungement Request**

(i) During Investment-Related, Customer-Initiated Arbitration

If an associated person requests expungement pursuant to Rule 12805(a)(1)(C) and the investment-related, customer-initiated arbitration claim closes by award after a hearing, the arbitrator or panel shall consider and decide the expungement request during the arbitration and issue its decision on the expungement request in the award, in accordance with Rule 12805(c)(8). If the associated person withdraws or does not pursue the expungement request, the

arbitrator or panel shall deny the expungement request with prejudice.

(ii) Investment-Related, Customer-Initiated Arbitration Closes Other Than by Award or By Award Without a Hearing

If an associated person requests expungement pursuant to Rule 12805(a)(1)(C) and the investment-related, customer-initiated arbitration closes other than by award or by award without a hearing:

a. the arbitrator or panel shall not consider the associated person's request for expungement of customer dispute information;

b. the associated person may file a request for expungement of the customer dispute information as a new claim under Rule 13805(a) against the member firm at which he or she was associated at the time the customer dispute arose, provided the expungement request is not barred pursuant to Rule 13805(a)(2); and

c. the associated person shall not file a request for expungement of the customer dispute information as a new claim against a customer.

**(2) Requesting Expungement on Behalf of an Unnamed Person**

**(A) Applicability**

A party to an investment-related, customer-initiated arbitration may request expungement of the customer dispute information arising from the customer's statement of claim on behalf of an unnamed person only with the written consent of the unnamed person.

**(B) Limitations**

A party to an investment-related, customer-initiated arbitration shall not request expungement on behalf of an unnamed person if the request is barred pursuant to Rule 12805(a)(1)(B).

**(C) Expungement Request**

(i) A party requesting expungement on behalf of an unnamed person must file the request with the Director in accordance with Rule 12805(a)(1)(C)(ii).

(ii) The request must include the Form Requesting Expungement on Behalf of an Unnamed Person, signed by the party filing the request and the unnamed person who seeks to have customer dispute information expunged from his or her Form U4, Form U5, or Form U6.

(iii) The request must be served on all parties as soon as practicable, but no later than 30 days before the first scheduled hearing; otherwise, pursuant to Rule 12309(b), the requesting party must file a motion pursuant to Rule 12503, seeking an extension to file the expungement request.

**(D) Form Requesting Expungement on Behalf of an Unnamed Person**

(i) By signing the Form Requesting Expungement on Behalf of an Unnamed Person, the unnamed person agrees that he or she shall be bound by the arbitrator's or panel's decision on the expungement request.

(ii) By signing the Form Requesting Expungement on Behalf of an Unnamed Person, the unnamed person agrees to maintain the confidentiality of any documents and information from the investment-related, customer-initiated arbitration to which the unnamed person is given access and to adhere to any confidentiality agreements or orders associated with the customer-initiated arbitration.

(iii) By filing and serving an expungement request, the requesting party agrees to represent the unnamed person for the purpose of requesting expungement during the investment-related, customer-initiated arbitration.

**(E) Deciding Expungement Request**

(i) Investment-Related, Customer-Initiated Arbitration Closes by Award After a Hearing

If the investment-related, customer-initiated arbitration claim closes by award after a hearing, the arbitrator or panel shall consider and decide the expungement request during the

investment-related, customer-initiated arbitration and issue its decision on the expungement request in the award, in accordance with Rule 12805(c)(8). If the requesting party, with the written consent of the unnamed person, withdraws or does not pursue the expungement request, the arbitrator or panel shall deny the expungement request with prejudice.

(ii) Investment-Related, Customer-Initiated Arbitration Closes Other than by Award or by Award Without a Hearing

If the investment-related, customer-initiated arbitration closes other than by award or by award without a hearing:

a. the arbitrator or panel shall not consider the party's request for expungement of customer dispute information on behalf of the unnamed person;

b. the unnamed person may file a request for expungement of the customer dispute information as a new claim under Rule 13805(a) against the member firm at which he or she was associated at the time the customer dispute arose, provided the filing of the request is not barred pursuant to Rule 13805(a)(2); and

c. the unnamed person shall not file a request for expungement of the customer dispute information as a new claim against a customer.

(iii) Unnamed Person May Not Intervene in the  
Investment-Related, Customer-Initiated Arbitration

a. If a party to the investment-related, customer-initiated arbitration does not request expungement on behalf of the unnamed person, the unnamed person shall not file a motion to intervene in the investment-related, customer-initiated arbitration and request expungement of customer dispute information arising from the customer's statement of claim.

b. The unnamed person may file a request for expungement of the customer dispute information as a new claim under Rule 13805(a) against the member firm at which he or she was associated at the time the customer dispute arose, provided the filing of the request is not barred pursuant to Rule 13805(a)(2).

**(b) FINRA Notifications**

FINRA shall notify state securities regulators, in the manner determined by FINRA, of an expungement request within 30 days of receiving a complete expungement request.

**(c) Expungement Hearing**

In order to [grant]recommend expungement of customer dispute information [under Rule 2080], the arbitrator or panel must comply with the following requirements[:].

**(1) Recorded Hearing Sessions**

[(a)] The arbitrator or panel must [H]hold one or more [a]recorded hearing sessions [(by telephone, [or]in person[)], or by video conference regarding the [appropriateness of]expungement request. [This paragraph will apply to cases administered under Rule 12800 even if a customer did not request a hearing on the merits.]

**(2) Associated Person's Appearance**

The associated person whose Form U4, Form U5, or Form U6 would be expunged of customer dispute information must personally appear at the expungement hearing. A party requesting expungement on behalf of an unnamed person must also appear at the expungement hearing. The panel shall decide the method of appearance.

**(3) Customer's Appearance**

**(A) Entitled to Appear**

All customers whose investment-related, customer-initiated arbitrations, civil litigations, and customer complaints gave rise to the customer dispute information that is a subject of the expungement request are entitled to appear at the expungement hearing. The customer may provide his or her position on the expungement request in writing.

**(B) Method of Appearance**

All customers whose investment-related, customer-initiated arbitrations, civil litigations, and customer complaints gave rise to the customer dispute information that is a subject of the expungement request

may appear at the expungement hearing by telephone, in person, or by video conference.

**(4) Representation of Parties**

All parties from the investment-related, customer-initiated arbitrations or civil litigations, and customers whose customer complaints gave rise to the customer dispute information that is the subject of the expungement request shall have the right to be represented at the expungement hearing pursuant to Rule 12208.

**(5) Customer and Customer's Representative Participation during the Expungement Hearing**

**(A) Customer's Testimony**

The arbitrator or panel must allow the customer to testify at the expungement hearing and be questioned by the customer's representative.  
If a customer testifies during the expungement hearing, the associated person or party requesting expungement on behalf of an unnamed person may cross-examine the customer.

**(B) Customer Introduces Evidence**

If the customer or customer's representative introduces evidence during the expungement hearing, the associated person or party requesting expungement on behalf of an unnamed person may state objections to the introduction of any evidence at the expungement hearing pursuant to the Code. The arbitrator or panel shall decide all objections.

**(C) Associated Person's or Others' Testimony**

The arbitrator or panel must allow the customer or the customer's representative to cross-examine the associated person, the party requesting expungement on behalf of an unnamed person and any witnesses called by the associated person or party requesting expungement on behalf of an unnamed person during the expungement hearing.

**(D) Opening and Closing Arguments by Customer or Customer's Representative**

The arbitrator or panel must allow the customer or the customer's representative to present opening and closing arguments if the arbitrator or panel allows any party to present such arguments.

**(6) Arbitrator or Panel Requests Additional Documents or Evidence**

The arbitrator or panel may request from the associated person, or party requesting expungement on behalf of an unnamed person, any documentary, testimonial or other evidence that it deems relevant to the expungement request.

**(7) Review Settlement Documents**

[(b) In cases involving settlements,] The arbitrator or panel must review the settlement documents and consider the amount of payments made to any party and any other terms and conditions of [a]the settlement. In addition, the panel should inquire and fully consider whether a party conditioned a settlement of the arbitration upon agreement not to oppose the request for expungement in cases in which the customer does not participate in the expungement hearing or the requesting party states that a customer has indicated that he or she will not oppose the expungement request.

**(8) Award**

[(c)] The arbitrator or panel must [I]indicate in the arbitration award which of the Rule 2080(b)(1) grounds for expungement serve[(s)] as the basis for its expungement [order]recommendation. [and]The arbitrator or panel must also provide a[brief] written explanation of the reason(s) for its finding that one or more Rule 2080(b)(1) grounds for expungement [applies]apply to the facts of the [case]request, and identify any specific documentary, testimonial or other evidence on which the arbitrator or panel relied in recommending expungement.

**(9) Forum Fees**

[(d)] The arbitrator or panel must [A]assess all forum fees for hearing sessions in which the sole topic is the determination of the appropriateness of expungement against the party or parties requesting expungement[relief].

\* \* \* \* \*

**13000. CODE OF ARBITRATION PROCEDURE FOR INDUSTRY DISPUTES**

\* \* \* \* \*

**13203. Denial of FINRA Forum**

(a) No Change.

(b) The Director shall decline the use of the FINRA arbitration forum if the Director determines that the expungement request is ineligible for arbitration under Rule 13805.

[(b)](c) Disputes that arise out of transactions in a readily identifiable market may be referred to the arbitration forum for that market, if the claimant agrees.

\* \* \* \* \*

**13307. Deficient Claims**

(a) The Director will not serve any claim that is deficient. The reasons a claim may be deficient include the following:

(1) through (4) No Change.

(5) The claimant did not pay all required filing fees, unless the Director deferred the fees; [or]

(6) The claim does not comply with the restrictions on filings with personal confidential information under Rule 13300(d)(1);

(7) A request to expunge information from the CRD system arising from a customer dispute does not include the customer's current address, unless the panel determines that extraordinary circumstances make such disclosure impracticable;

(8) A request to expunge information from the CRD system arising from a customer dispute does not include the CRD number of the party requesting expungement;

(9) A request to expunge information from the CRD system arising from a customer dispute does not include each CRD occurrence number that is the subject of the request;

(10) A request to expunge information from the CRD system arising from a customer dispute does not include the case name and docket number of the arbitration that gave rise to the customer dispute information, if applicable; or

(11) A request to expunge information from the CRD system arising from a customer dispute does not include an explanation of whether expungement of

the same customer dispute information was (i) previously requested and, if so (ii) how it was decided.

(b) though (c) No Change.

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**PART VIII SIMPLIFIED ARBITRATION; DEFAULT PROCEEDINGS;  
STATUTORY EMPLOYMENT DISCRIMINATION CLAIMS; [AND]  
INJUNCTIVE RELIEF; EXPUNGEMENT PROCEEDINGS; AND  
PROMISSORY NOTE PROCEEDINGS**

\* \* \* \* \*

**13805. Expungement of Customer Dispute Information under Rule 2080**

This Rule applies to all expungement requests of customer dispute information under Rule 2080. Except as otherwise provided in this Rule, all provisions of the Code apply to such expungement requests.

**(a) Filing an Expungement Request against a Member Firm**

**(1) Applicability**

An associated person may request expungement of customer dispute information by filing a statement of claim under Rule 13302 against a member firm at which he or she was associated at the time the customer dispute arose, unless barred by Rule 13805(a)(2).

**(2) Limitations**

(A) An associated person shall not file a claim requesting expungement of customer dispute information against the member firm at which he or she was associated at the time the customer dispute arose if:

(i) an arbitrator or panel held a hearing to consider the merits of the associated person's request for expungement of the same customer dispute information;

(ii) a court of competent jurisdiction previously denied the associated person's request to expunge the same customer dispute information;

(iii) the investment-related, customer-initiated arbitration, civil litigation or customer complaint that gave rise to the customer dispute information is not closed;

(iv) more than two years have elapsed since the investment-related, customer-initiated arbitration or civil litigation that gave rise to the customer dispute information has closed; or

(v) there was no investment-related, customer-initiated arbitration or civil litigation that gave rise to the customer dispute information, and more than six years have elapsed since the date that the customer complaint was initially reported to the CRD system.

(B) Subject to the six-year eligibility requirement of Rule 13206(a), an associated person is not barred from requesting expungement of customer dispute information pursuant to Rule 13805(a)(2) if:

(i) the request for expungement is made pursuant to Rule 13805 within two years of [insert the effective date of the proposed rule change], and the disclosure sought to be expunged arises from

an investment-related, customer-initiated arbitration or civil litigation that closed on or prior to [insert the effective date of the proposed rule change]; or,

(ii) the request for expungement is made pursuant to Rule 13805 within six years of [insert the effective date of the proposed rule change], and the disclosure sought to be expunged arises from a customer complaint initially reported to the CRD system on or prior to [insert the effective date of the proposed rule change].

### **(3) Expungement Request**

The expungement request must be filed with the Director, pursuant to Rule 13302, and include:

(A) the applicable filing fee;

(B) the CRD number of the party requesting expungement;

(C) each CRD occurrence number that is the subject of the request;

(D) the case name and docket number that gave rise to the customer dispute information, if applicable; and

(E) an explanation of whether expungement of the same customer dispute information was (i) previously requested and, if so (ii) how it was decided.

### **(4) Panel Decides Expungement Request**

A three-person panel selected pursuant to Rule 13806 must hold an expungement hearing, pursuant to Rule 13805(c), to consider and decide the

expungement request. At the conclusion of the expungement hearing, the panel must issue an award in accordance with Rule 13805(c)(8). If the associated person withdraws or does not pursue the expungement request, the panel shall deny the expungement request with prejudice.

**(b) Notifications**

(1) Before the first scheduled hearing session is held, the associated person shall:

(A) Provide all customers whose investment-related, customer-initiated arbitrations, civil litigations, and customer complaints gave rise to customer dispute information that is a subject of the expungement request with notice of the expungement request by serving on the customers a copy of the statement of claim requesting expungement, unless the panel determines that extraordinary circumstances make such service impracticable;

(B) Serve the customers by first-class mail, overnight mail service, overnight delivery service, or hand delivery; and

(C) File with the panel all documents provided by the associated person to the customers, including proof of service, and any responses received by the associated person from the customers.

(2) The Director shall notify all customers whose investment-related, customer-initiated arbitrations, civil litigations, and customer complaints gave rise to the customer dispute information that is a subject of the expungement request

of the time, date and place of the expungement hearing using the customers' current address provided by the party seeking expungement.

(3) FINRA shall notify state securities regulators, in the manner determined by FINRA, of an expungement request within 30 days of receiving a complete expungement request filed pursuant to Rule 13805(a)(3).

**(c) Expungement Hearing**

In order to [grant]recommend expungement of customer dispute information [under Rule 2080], the panel must comply with the following requirements[:].

**(1) Recorded Hearing Sessions**

[(a)] The panel must [H]hold one or more [a]recorded hearing sessions [(by telephone, [or]in person)], or by video conference regarding the [appropriateness of]expungement request. [This paragraph will apply to cases administered under Rule 13800 even if a claimant did not request a hearing on the merits.]

**(2) Associated Person's Appearance**

The associated person who seeks to have customer dispute information expunged from his or her Form U4, Form U5, or Form U6 must personally appear at the expungement hearing. The panel shall decide the method of appearance.

**(3) Customer's Appearance**

**(A) Entitled to Appear**

All customers whose investment-related, customer-initiated arbitrations, civil litigations, and customer complaints gave rise to the customer dispute information that is a subject of the expungement request

are entitled to appear at the expungement hearing. The customer may provide his or her position on the expungement request in writing.

**(B) Method of Appearance**

All customers whose investment-related, customer-initiated arbitrations, civil litigations, and customer complaints gave rise to the customer dispute information that is a subject of the expungement request may appear at the expungement hearing by telephone, in person, or by video conference.

**(4) Representation of Parties**

All parties from investment-related, customer-initiated arbitrations or civil litigations, and customers whose customer complaints gave rise to the customer dispute information that is a subject of the expungement request shall have the right to be represented at the expungement hearing pursuant to Rule 13208.

**(5) Customer and Customer's Representative Participation during the Expungement Hearing**

**(A) Customer's Testimony**

The panel must allow the customer to testify at the expungement hearing and be questioned by the customer's representative. If a customer testifies during the expungement hearing, the associated person requesting expungement may cross-examine the customer.

**(B) Customer Introduces Evidence**

If the customer or customer's representative introduces evidence during the expungement hearing, the associated person requesting

expungement may state objections to the introduction of any evidence at the expungement hearing pursuant to the Code. The panel shall decide all objections.

**(C) Associated Person's or Others' Testimony**

The panel must allow the customer or the customer's representative to cross-examine the associated person requesting expungement and any witnesses called by the associated person during the expungement hearing.

**(D) Opening and Closing Arguments by Customer or Customer's Representative**

The panel must allow the customer or the customer's representative to present opening and closing arguments if the panel allows any party to present such arguments.

**(6) Panel Requests Additional Documents or Evidence**

The panel may request from the associated person requesting expungement, and from the member firm at which he or she was associated at the time the customer dispute arose, any documentary, testimonial or other evidence that it deems relevant to the expungement request.

**(7) Review Settlement Documents**

[(b) In cases involving settlements,] The panel must review the settlement documents and consider the amount of payments made to any party and any other terms and conditions of [a]the settlement. In addition, the panel should inquire and fully consider whether a party conditioned a settlement of the arbitration upon

agreement not to oppose the request for expungement in cases in which the customer does not participate in the expungement hearing or the requesting party states that a customer has indicated that he or she will not oppose the expungement request.

**(8) Award**

[(c)] The panel must [I]indicate in the arbitration award which of the Rule 2080(b)(1) grounds for expungement serve[(s)] as the basis for its expungement [order]recommendation. [and] The panel must also provide a[brief] written explanation of the reason(s) for its finding that one or more Rule 2080(b)(1) grounds for expungement [applies]apply to the facts of the [case]request, and identify any specific documentary, testimonial or other evidence on which the panel relied in recommending expungement.

**(9) Forum Fees**

[(d)] The panel must [A]assess all forum fees for hearing sessions in which the sole topic is the determination of the appropriateness of expungement against the party or parties requesting expungement[relief].

**13806. Panel to Decide Requests for Expungement of Customer Dispute**

**Information Filed by an Associated Person under Rule 13805**

**(a) Applicability**

This Rule applies to claims that request expungement of customer dispute information filed by an associated person against a member firm, pursuant to Rule 13805. Except as otherwise provided in this Rule, all provisions of the Code apply to such claims.

**(b) Selection of Panel**

(1) The Neutral List Selection System shall randomly select three public arbitrators who are eligible for the chairperson roster and have the additional qualifications described in Rule 13806(b)(2) to decide a request for expungement of customer dispute information filed by an associated person pursuant to Rule 13805. The parties shall not be permitted to stipulate to the use of pre-selected arbitrators.

(2) Each arbitrator selected for the panel must have fully met the following additional qualifications:

(A) evidenced successful completion of, and agreement with, enhanced expungement training provided by FINRA; and

(B) service as an arbitrator through award on at least four customer-initiated arbitrations administered by FINRA pursuant to the Rule 12000 Series or another self-regulatory organization, in which a hearing was held, except a hearing pursuant to Rule 12800(c)(3)(B).

(3) The first arbitrator selected by the Neutral List Selection System shall be the chairperson of the panel.

(4) The associated person requesting expungement of customer dispute information shall not be permitted to strike any arbitrators selected by the Neutral List Selection System nor stipulate to their removal, but shall be permitted to challenge any arbitrator selected for cause pursuant to Rule 13410. If an arbitrator is removed, the Neutral List Selection System shall randomly select a replacement.

(5) Notwithstanding Rules 13401(b) and (c), the parties shall not be permitted to stipulate to fewer than three arbitrators on the panel to hear the expungement request.

**[13806] 13807. Promissory Note Proceedings**

No Change.

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