

Regulatory Notice

08-79

Expungement

SEC Approves Rules Establishing Procedures for Arbitrators Considering Expungement Requests

Effective Date: January 26, 2009

Executive Summary

Effective January 26, 2009, FINRA will implement new procedures for arbitrators to follow when considering requests for expungement relief under NASD Rule 2130. The SEC approved new FINRA Rule 12805 of the Code of Arbitration Procedure for Customer Disputes and new FINRA Rule 13805 of the Code of Arbitration Procedure for Industry Disputes.¹ Accordingly, arbitrators considering a request for expungement relief under Rule 2130 are required to:

- Hold a recorded hearing session by telephone or in person;
- In cases involving a settlement, review the settlement documents to examine the amount paid to any party and any other terms and conditions of the settlement;
- Provide a brief written explanation of the reasons for ordering expungement; and
- Assess forum fees for hearing sessions held solely for the purpose of considering expungement against the parties requesting the relief.

The text of Rules 12805 and 13805 is set forth in Attachment A. The rules apply to expungement orders issued by arbitrators on or after January 26, 2009.

Questions concerning this *Notice* should be directed to: Richard W. Berry, Vice President and Director of Case Administration, FINRA Dispute Resolution, at (212) 858-4307 or richard.berry@finra.org; or Margo A. Hassan, Counsel, FINRA Dispute Resolution, at (212) 858-4481 or margo.hassan@finra.org.

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Notice Type

- Rule Amendment

Suggested Routing

- Compliance
- Legal
- Registered Representatives
- Registration
- Senior Management

Key Topic(s)

- Arbitration
- Central Registration Depository
- Code of Arbitration Procedure
- Dispute Resolution
- Expungement

Referenced Rules & Notices

- NASD Rule 2130
- FINRA Rule 12800
- FINRA Rule 12805
- FINRA Rule 13800
- FINRA Rule 13805
- NTM 04-16

Background & Discussion

Background

Members of the securities industry, state and federal regulators, and self-regulatory organizations use the Central Registration Depository (CRD® or CRD system). CRD, an online registration and licensing system, contains administrative and disclosure information about broker-dealers and associated persons. Although public investors cannot access CRD, much of the information in that system is available to them through FINRA BrokerCheck.² Accurate and complete reporting in CRD, including the reporting of required customer dispute information, is an important aspect of investor protection.

FINRA operates CRD pursuant to policies developed jointly with the North American Securities Administrators Association (NASAA). FINRA works with the SEC, NASAA, other members of the regulatory community, and broker-dealer firms to establish policies and procedures reasonably designed to ensure that information submitted to and maintained in the CRD system is accurate and complete. These procedures, among other things, cover expungement of information from CRD. FINRA implemented Rule 2130 (effective April 12, 2004) to govern the expungement of customer dispute information from the CRD system.³ In connection with the implementation of Rule 2130, FINRA required all arbitrators on its roster to take mandatory training on the requirements of Rule 2130.

Discussion

FINRA has adopted FINRA Rules 12805 and 13805 to establish specific procedures that arbitrators must follow before ordering expungement of customer dispute information from the CRD system consistent with NASD Rule 2130. The new procedures ensure that arbitrators have the opportunity to consider the facts that support or weigh against a decision to grant expungement. The procedures add transparency to the process and safeguards designed to ensure that the extraordinary relief of expungement is granted only under appropriate circumstances.

The following questions and answers provide more detail on the purpose of the rules and how they will be applied.

What steps must the arbitration panel take before it may order expungement of information related to arbitration cases from an associated person's CRD record?

- ▶ The arbitration panel must hold a recorded hearing session by telephone or in person regarding the appropriateness of expungement.

- In cases involving settlements, the arbitration panel must review the settlement documents, consider the amount paid to any party, and consider any other terms and conditions of the settlement that might raise concerns about the associated person's involvement in the alleged misconduct before awarding expungement.
- The 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.
- The arbitration panel must assess against the parties requesting expungement relief all forum fees for hearing sessions in which the sole topic is the determination of the appropriateness of expungement.

What are the grounds for expungement under Rule 2130(b)(1)(A)-(C)?

- (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.

What will happen if, on the effective date of the rule, arbitrators are about to issue an award containing an order to expunge customer dispute information from the CRD system, but no hearing was held on the expungement issue?

Such an award must comply with the new procedures. In this situation, FINRA will require the arbitrators to convene (or reconvene) the parties for a telephone or in-person hearing to resolve the expungement issue. In cases involving settlements, the arbitrators will be required to review the settlement documents and consider the amount of payments made to any party and any other terms and conditions of the settlement. The arbitrators will be required to assess all forum fees for the hearing session against the parties that requested expungement relief, and to provide a brief written explanation of the reasons for ordering expungement.

What happens when an expungement request is made in a Simplified Arbitration case?

In cases being administered under FINRA Rules 12800 or 13800 (Simplified Arbitration), a hearing on the merits normally is held only at the request of a customer or claimant, respectively. Rules 12805 and 13805 make it clear that, if parties request expungement relief in such cases, the arbitrator will hold a hearing session to determine the appropriateness of the request even if the customer or claimant did not request a hearing on the merits. The arbitrator will assess any forum fees for hearing sessions associated with a request for expungement against the parties making the request.

Do the new rules apply to expungement of non-customer dispute information in intra-industry disputes?

No, the new rules only apply to the expungement of customer dispute information. The rules do not affect FINRA's current practice of permitting expungement, without judicial intervention, of information from CRD as directed by arbitrators in intra-industry arbitration awards in which the arbitration panel states that expungement relief is being granted because of the defamatory nature of the information ordered expunged.⁴

Are arbitrators required to complete training or otherwise familiarize themselves with the new rules (and accompanying procedures) prior to considering a request for expungement relief under Rule 2130?

Yes, FINRA is requiring arbitrators to certify that they have familiarized themselves with new Rules 12805 and 13805. FINRA is revising its online expungement training module and is encouraging every arbitrator to take this free training course. In addition, arbitrators must certify that they have completed one or more of the training methods listed below.

- Reviewing written correspondence with a question and answer that FINRA is sending to every arbitrator explaining the new rules.
- Reviewing a broadcast email with the same content as the written correspondence that FINRA is sending to every arbitrator.
- Listening to the audio workshop on expungement that FINRA broadcasted on December 10, 2008 (available at www.finra.org/ArbitrationMediation/Neutrals/Education/P009530).
- Reading this *Regulatory Notice*.
- Taking the revised online expungement training module that will be available in January 2009.
- Reading an article on expungement that will be published in the arbitrator and mediator newsletter, *The Neutral Corner*, in January 2009.

How will arbitrators certify that they have completed the required training?

FINRA sent a letter to every arbitrator explaining how to fulfill the training requirement concerning the new expungement rules.⁵ Attached to the letter was a certification form for arbitrators to sign and return to FINRA. Arbitrators can also certify online by selecting the "Expungement Refresher Training" certification link located on FINRA's Web site (www.finra.org).

Effective Date Provisions

Rules 12805 and 13805 will become effective on January 26, 2009, and will apply to expungement orders issued by arbitrators on or after the effective date.

Endnotes

- 1 Exchange Act Release No. 58886 (October 30, 2008), 73 Federal Register 66086 (November 6, 2008) (File No. SR-FINRA-2008-010).
- 2 FINRA BrokerCheck (www.finra.org/Investors/ToolsCalculators/BrokerCheck/index.htm) is a free online tool to help investors check the background of current and former FINRA-registered securities firms and brokers.
- 3 See NASD Notice to Members 04-16 (March 2004).
- 4 See Notice to Members 04-16.
- 5 All active arbitrators on FINRA's roster have already completed the online expungement training that has been required since 2004.

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ATTACHMENT A

Code of Arbitration Procedure for Customer Disputes
and
Code of Arbitration Procedure for Industry Disputes

Customer Code**12805. Expungement of Customer Dispute Information under Rule 2130**

In order to grant expungement of customer dispute information under Rule 2130, the panel must:

- (a) Hold a recorded hearing session (by telephone or in person) regarding the appropriateness of expungement. This paragraph will apply to cases administered under Rule 12800 even if a customer did not request a hearing on the merits.
- (b) In cases involving settlements, review settlement documents and consider the amount of payments made to any party and any other terms and conditions of a settlement.
- (c) Indicate in the arbitration award which of the Rule 2130 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 2130 grounds for expungement applies to the facts of the case.
- (d) 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.

Industry Code

13805. Expungement of Customer Dispute Information under Rule 2130

In order to grant expungement of customer dispute information under Rule 2130, the panel must:

- (a) Hold a recorded hearing session (by telephone or in person) regarding the appropriateness of expungement. This paragraph will apply to cases administered under Rule 13800 even if a claimant did not request a hearing on the merits.
- (b) In cases involving settlements, review settlement documents and consider the amount of payments made to any party and any other terms and conditions of a settlement.
- (c) Indicate in the arbitration award which of the Rule 2130 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 2130 grounds for expungement applies to the facts of the case.
- (d) 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.