

Cornell University
Cornell Law School

William A. Jacobson, Esq.
Associate Clinical Professor
Director, Securities Law Clinic
G57 Myron Taylor Hall
Ithaca, New York 14853
t. 607.254.8270
f. 607.255.3269
waj24@cornell.edu

June 17, 2008

Via Electronic Filing

Ms. Nancy M. Morris
Secretary
United States Securities and Exchange Commission
100 F. Street, NE
Washington, DC 20549-1090

**RE: SR-FINRA-2008-010
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**

Dear Ms. Morris:

The Cornell Securities Law Clinic (the "Clinic") submits this letter in furtherance of the Clinic's Comment Letter, dated April 23, 2008 (the "Clinic's Comment Letter") with regard to SR-FINRA-2008-010 (the "Proposed Rule"). We submit this letter to respond to one issue addressed by the Financial Industry Regulatory Authority ("FINRA") in its letter to the SEC dated June 11, 2008 (the "FINRA Response Letter").

In the Clinic's Comment Letter, we pointed out that the Proposed Rule may have the negative unintended consequence that arbitrator findings on expungement may be used against the public customer in later proceedings under the doctrine of collateral estoppel. This is of grave concern because the expungement hearing under the Proposed Rule is unlike any other procedure under the NASD Code of Arbitration Procedure (the "NASD Code"), in that the substantive findings do not affect the rights of the parties vis-à-vis each other. Rather, expungement findings affect the associated person's rights vis-à-vis the regulatory record. Indeed, the expungement procedure under the Proposed Rule is structured in such a way that the public customer has little or no incentive to actively participate in the expungement hearing.

The Proposed Rule thus creates a trap for the unwary public customer, who having settled or otherwise disposed of her claim, either does not participate in the expungement hearing or does not actively oppose expungement. Nonetheless, such public customer may find herself the recipient of a lawsuit alleging malicious prosecution based upon the expungement findings. Under the current NASD Code, such a result is highly unlikely because arbitrators do not normally issue the sort of detailed findings which are mandated by the Proposed Rule.

In the Clinic's Comment Letter, we requested that FINRA address this problem through the simple mechanism of incorporating language in the Proposed Rule that the expungement findings may be used only for the purpose of obtaining expungement. In the FINRA Response Letter, FINRA treats this issue dismissively. In pertinent part, FINRA responds as follows:

"FINRA does not believe that it is appropriate to revise the proposal in such a manner because (1) FINRA does not have the authority to dictate how parties may use an arbitral finding after the arbitration has concluded; (2) other forums, particularly state and federal courts, are not bound to accept FINRA's determination with respect to the collateral use of arbitral findings even if it made recommendations in this area; and (3) expungement findings should be treated in the same manner as any other arbitral findings." (FINRA Response Letter, at 2)

None of the grounds raised by FINRA holds up to scrutiny. First, FINRA points to nothing which prohibits it from exercising the power to limit the use of expungement findings. FINRA has the authority to limit its members' access to the courts on a variety of issues, including issues relating to arbitration, and has done so in the past. *E.g.*, IM-12000 (prohibiting member firms from failing to submit a dispute to arbitration or from causing associate persons to waive arbitration under the Code); NASD Code Rule 12209 (prohibiting parties from filing in court any action which would resolve the matters pending in arbitration). Since FINRA is creating a wholly new procedure – the expungement hearing – FINRA certainly has the power to define and limit the purpose of the hearing.

Second, the fact that a court may not be "bound" by FINRA's determination of the use of expungement findings is beside the point. Courts are not "bound" by any FINRA rules, but that has not stopped FINRA from promulgating reams of rules and interpretations as to the parties' rights which may or may not be enforced by a court. *E.g.*, NASD Code Rule 12413 (vesting sole authority in panel to interpret NASD Code); NASD Code Rule 12206(b)(providing that dismissal under six-year eligibility rule allows party to pursue claim in court). Rather, the NASD Code is an expression of the parties' agreement to arbitrate. *E.g.*, NASD Code Rule 12010(b) ("When a dispute is submitted to arbitration under the Code pursuant to an arbitration agreement, the Code is incorporated by reference into the agreement"). As part of the parties' agreement, the NASD Code is enforceable under the Federal Arbitration Act and state arbitration statutes. A limitation on the use of expungement findings may not "bind" a court, but such limitation likely will be enforced by a court as a reflection of the arbitration agreement.

Finally, there is no valid reason to treat expungement findings "in the same manner as any other arbitral findings." The expungement process, as discussed above, is unique in that expungement addresses regulatory record keeping, not the substantive rights of the parties. It is in the public interest to restrict the scope of expungement findings to the expungement process.

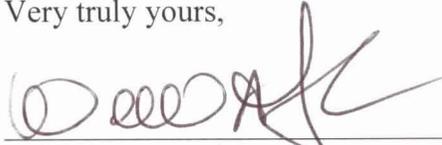
Ms. Nancy M. Morris

June 17, 2008

Page 3

We thank you for the opportunity to comment further. While the Clinic believes that the Proposed Rule has many valuable aspects, the potential damage to public investors from the lack of restriction on the use of expungement findings is so great that the Clinic opposes the Proposed Rule *as drafted*.

Very truly yours,

A handwritten signature in black ink, appearing to read 'W. A. Jacobson', written over a horizontal line.

William A. Jacobson, Esq.
Associate Clinical Professor of Law
Director, Cornell Securities Law Clinic