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Elizabeth M. Murphy  
Secretary  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549-1090

**RE: File Number SR-FINRA-2009-008**  
**Proposed Changes Relating to Forms U4 and U5**

Dear Ms. Murphy:

Thank you for the opportunity to comment on the proposal of the Financial Industry Regulatory Authority ("FINRA") to make revisions to Forms U4 and U5 with regard to reporting customer complaints and settlements, and to permit member firms to amend information previously entered into the Central Registration Depository ("CRD") with regard to the date and reason for termination of a registered person's employment (collectively, the "Proposed Changes"). The Cornell Securities Law Clinic (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, see <http://securities.lawschool.cornell.edu>.

Three substantive changes are proposed: (1) Questions 14I(2) and (3) on FormU4 and Questions 7E(2) and (3) on FormU5 would require firms to report, as customer complaints, allegations of sales practice violations made in arbitration claims and civil lawsuits against registered persons who are not named as parties in those proceedings; (2) Questions 14I(1)(c) and 14I(2) on FormU4 and Questions 7E(1)(c) and 7E(2) on FormU5 would require customer complaints to be reported only when they have been settled for \$15,000 or more; and (3) member firms would be permitted to amend the reason for, or date of, termination of a registered person's employment, without need for a court order or arbitration award. For the reasons set forth below, the Clinic supports the proposed changes to Forms U4 and U5, but opposes giving member firms the right to change the date and reason for termination from the CRD except for clerical error.

**The Clinic Supports the Proposed Changes**  
**To Reporting of Customer Complaints**

The Clinic supports the proposed changes to the reporting of customer complaints on Questions 14I(2) and (3) on Form U4 and Questions 7E(2) and (3) on FormU5. Currently, a

written customer complaint (or settlement in response to the written complaint) alleging certain sales practice violations by a registered person is required to be reported, but an arbitration claim or civil court complaint with identical allegations need not be reported unless the registered person is named as a party in the proceeding. This distinction makes no sense. Regulators have an interest in receiving information regarding alleged sales practice violations regardless of whether the private litigant decides to name the registered person as a respondent in a case. The Proposed Changes eliminate this irrational distinction and ensure that alleged sales practice violations are reported.

It makes sense not to rely upon litigation decisions by private litigants in determining whether substantive allegations of sales practice violations are reported. There may be numerous valid legal and tactical reasons why a public customer may choose not to name a registered person in an arbitration or civil court complaint, including but not limited to, the naming of the registered person being legally unnecessary since the member firm is liable for the conduct of its employees within the scope of their employment; difficulty locating the registered person; concerns that having multiple respondents may prolong a hearing; concerns that naming the registered person may result in an uncollectible award solely against the registered person; and concerns that naming the registered person may make it more difficult to settle the case.

Accordingly, there are many instances where public customers choose not to name the registered person as a respondent in a case, for reasons having nothing to do with the regulatory purpose behind the Form U4 and U5 reporting requirements. Nonetheless, this civil litigation decision results in numerous arbitration claims and court complaints not being reported on the CRD. The Clinic supports FINRA's effort to close this loophole.<sup>1</sup>

### **The Clinic Supports the Proposed Changes To Reporting of Customer Complaint Settlements**

Currently, Questions 14I(1)(c) and 14I(2) on Form U4 and Questions 7E(1)(c) and 7E(2) on Form U5 require customer complaints to be reported only when they have been settled for \$10,000 or more. The Proposed Changes raise this threshold for reporting settlement of customer complaints to \$15,000.

The Clinic supports the Proposed Changes because raising the threshold to \$15,000 strikes a fair balance among competing interests. The Clinic acknowledges concerns that raising the dollar threshold for reporting settlements may decrease the reporting of sales practice violations, and thereby impede the regulatory function of the CRD. The answer to this concern would be to have no minimum threshold and to report all allegations of sales practice violations.<sup>2</sup>

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<sup>1</sup> The Clinic neither supports nor opposes the proposal to revise questions on Forms U4 and U5 to better identify persons that may be subject to statutory disqualification based on willful violations. As a result, the Clinic will not comment further on that proposal.

<sup>2</sup> The Clinic would support an elimination of threshold reporting requirements, because the dollar amount of the customer loss does not necessarily reflect the seriousness of the sales practice violation.

In the absence of elimination of a minimum threshold, we see no appreciable regulatory downside from the increase to \$15,000. Additionally, raising the threshold to \$15,000 does not eliminate all reporting of customer complaints that settle for less than that amount. Depending upon the nature of the allegations, alleged sales practice violations may have to be reported at the time of the customer complaint or termination of the registered person, regardless of whether the complaint were settled. (See Question 14I(3) to Form U4, and Question 7F to Form U5.)

Raising the threshold amount to \$15,000 also accurately reflects the change in value of the threshold amount of \$10,000 by adjusting for inflation. Based on our calculations, because the \$10,000 threshold was enacted in 1998, the actual economic value of the threshold has decreased substantially as a result of inflation. Raising the threshold amount to \$15,000 is a reasonable adjustment based on the Consumer Price Index.<sup>3</sup>

Furthermore, raising the threshold to \$15,000 likely will benefit public customers with relatively small dollar claims. Small claims settle for many reasons, including the cost of defense relative to the small dollar amount in dispute. In the experience of the undersigned, the dollar threshold for reporting settlements sometimes is an impediment to settling small claims, since the registered person may not want to settle if the result is a reportable event, even if it makes economic sense to do so.<sup>4</sup> By raising the threshold, member firms and registered persons will have an added incentive to settle small cases for an amount more reflective of the cost of defense, thereby increasing the ability of public investors with small claims to receive compensation without requiring hearings. Since the Clinic primarily represents investors with small claims, the Clinic strongly supports raising the reporting threshold to \$15,000.

### **The Clinic Opposes the Proposed Changes Regarding Amendments and Corrections**

Under current practice, member firms do not have the ability to amend the date of termination or reason for termination after the initial filing of Form U5. Instead, member firms have the ability to place a Registration Comment on the WebCRD to explain “unusual circumstances or irregularities in an individual's registration history that: (1) relate to the date or reason for termination on the Form U5, and (2) cannot be addressed otherwise through a form filing” by submitting “a Registration Comment Request Form asking that FINRA enter a comment on the firm's behalf.”<sup>5</sup> The Clinic would like to make clear that the current system is troublesome because the Registration Comments, although stored in the CRD system, are not publicly available. Alternatively, the member firm or registered persons could follow the expungement procedure set forth in NASD Rule 2130.

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<sup>3</sup> Our calculations indicate that, after adjusting for inflation, \$10,000 in 1998 would have the same economic value as \$13,049.63 in 2009.

<sup>4</sup> The use of a minimum reporting threshold for settlements creates pressure on the public customer to settle for just under the threshold, thereby creating a potential ceiling for settling small claims. Given that there is a threshold currently, however, the Clinic supports raising the threshold to a more meaningful dollar amount.

<sup>5</sup> See <http://www.finra.org/RegulatorySystems/CRD/FilingGuidance/p005227>.

In the Proposed Changes, the FINRA proposes to allow member firms to amend the date of, or reason for, termination. Member firms would have to give a reason for each amendment. FINRA would notify other regulators and the broker-dealer with which the person is currently associated (if the person is associated with another firm) when a date of termination or reason for termination has been amended. However, due to the lack of standards pertaining to these amendments, the process is wide-open to manipulation. To the extent that there are no discernable standards as to when a firm may make an amendment or standards as to what should be stated in the reasons for an amendment, the Clinic opposes this change, except in instances of clerical error.

While the Clinic has specific concerns about permitting member firms to change the date of termination and reason for termination (see below), the Clinic has an overall concern as to both changes. When FINRA originally sent out its proposed changes for comment, we stated that the proposal was unclear as to whether the information pertaining to the original entry would remain in the CRD system. As indicated in the Proposed Changes, it is evident that FINRA, in its rule proposal, clarified that the information pertaining to the original entry would remain in the CRD system in form filing history. However, it is still unclear as to whether the information will be publicly available. FINRA should be required to ensure that the original entry, the amended entry, and the explanation for the change, all are reflected on all versions of the CRD, including Web CRD-generated reports (including agency “snapshots”) and the BrokerCheck Program.

#### A. Date of Termination

The date of termination impacts how certain of the questions on the Form U5 are answered. For example, Questions 7A and 7B each reference whether certain the registered person “[c]urrently is, or at termination was” the subject of certain reportable events. (Emphasis added.) A “Yes” answer to either of these questions triggers the need to fill out a Disclosure Reporting Page, giving the details. Changing the date of termination could affect whether these questions are answered in the affirmative or negative, and whether a further disclosure is required. The date of termination of a registered person also may have relevance in customer arbitrations. Form U5 is one of the documents which must be produced in all customer cases. See FINRA Discovery Guide, List 1, Item 8.

We certainly recognize that there may be a clerical error in the entry of the date of termination, and that it is important that the CRD accurately reflect the actual date of termination. We also understand that there may be legitimate reasons other than clerical error that justifies changing this information in the CRD. However, due to the possibility of manipulation, without discernible standards for the amendment process, we do not believe reasons other than clerical error should justify information changes in the CRD.

We would be very concerned, for example, if the change in date of termination were the result of a negotiation between member firm and registered person in settlement of legal disputes (e.g., perhaps so that the registered person could qualify for certain employment benefits). In

such case, the change would not be to correct the prior entry, but to enter an inaccurate date. Requiring the member firm to give an explanation for the amendment is not an adequate protection, because the Proposed Changes do not provide any standards for amending the date of termination. In the example cited, if the member firm and the registered person were to agree that the termination be “deemed” effective as of a certain date, would that be a valid ground for changing the date of termination on Form U5? Accordingly, to the extent the Proposed Changes lack discernible standards for the amendment process, the Clinic opposes giving member firms the right to change the date of termination, except in the instance of clerical error.

#### B. Reason for Termination

Under current practice, if the termination is involuntary (either permitted to resign or discharged), the member firm must give an explanation. If the termination is voluntary, no explanation is needed. The reason for termination and explanation provide regulators, and public customers in civil actions or arbitrations, with valuable context in which to evaluate the other disclosure items on the Form U5.

If a member firm involuntarily terminates a registered person, the member firm presumably knows why at the time it files the Form U5 (which it has up to 30 days to do). Again, we recognize that there may be a clerical error, and have no objection to an amendment in such circumstances. We also understand that there may be legitimate reasons other than clerical error that justifies changing this information in the CRD. However, as mentioned before, due to the possibility of manipulation, without discernible standards for the amendment process, we do not believe reasons other than clerical error should justify information changes in the CRD. Furthermore, it is hard to understand how a member firm legitimately could change the reason for termination (for example, involuntary to voluntary, or change the explanation for the involuntary termination), except perhaps as part of a negotiation with the registered person in settlement of employment claims or for some other business reason.<sup>6</sup> Yet, abuses of the expungement process pursuant to settlement negotiations are one of the primary reasons FINRA seeks to tighten the expungement process with regard to customer complaints. (See SR-FINRA-2008-010) Similarly, as part of these very same Proposed Changes, FINRA seeks to close loopholes in the reporting of customer dispute information on Form U4. The Proposed Changes, however, do not set forth any standards which would guide the ability to amend the reason for termination. Accordingly, to the extent that the Proposed Changes lack discernible standards for the amendment process, the Clinic opposes allowing member firms to change the reason for termination, except in the instance of clerical error.

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<sup>6</sup> These business reasons may not be favorable to the registered person. An amendment of the reason for termination from voluntary to permitted to resign or discharged, may have substantial negative effect on the registered person’s ability to find new employment.

**Conclusion**

The Clinic supports the proposed changes to the reporting of customer complaints and the threshold for reporting customer complaint settlements. Since the Proposed Changes lack standards as to the amendment process, the Clinic opposes giving member firms power to amend the date or reasons for termination of registered persons, except in instances of clerical error.

Very truly yours,

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