

March 18, 2020

**VIA ELECTRONIC MAIL**

Vanessa Countryman  
Secretary  
Securities and Exchange Commission  
100 F Street NE  
Washington, DC 20549-1090

**Re: File No. SR-2020-005 – Notice of Filing of a Proposed Rule Change to Amend the FINRA Code of Arbitration Procedure for Customer Disputes and the FINRA Code of Arbitration Procedure for Industry Disputes to Apply Minimum Fees to Requests for Expungement of Customer Dispute Information**

Dear Secretary Countryman:

On February 7, 2020, the Financial Industry Regulatory Authority, Inc. (FINRA) filed for approval with the U.S. Securities and Exchange Commission (SEC) SR-FINRA-2020-005 *Notice of Filing of a Proposed Rule Change to Amend the FINRA Code of Arbitration Procedure for Customer Disputes and the FINRA Code of Arbitration Procedure for Industry Disputes to Apply Minimum Fees to Requests for Expungement of Customer Dispute Information* (the Notice).<sup>1</sup> The Notice solicits comment on FINRA's 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 apply minimum fees to associated persons' requests for expungement of customer dispute information (the Proposal). The Proposal was preceded by FINRA Regulatory Notice 17-42 *Expungement of Customer Dispute Information*, which was issued on December 6, 2017.<sup>2</sup>

The Financial Services Institute (FSI) appreciates the opportunity to comment on this important Proposal. Over the past several years, FINRA has embarked on a broad-ranging effort to improve the hallmarks of efficiency and fairness in its dispute resolution program. Throughout this effort, FSI has been proud to serve as a source of industry expertise and insight to FINRA in order to strengthen the arbitration process and drive better outcomes for firms, advisers, investors and arbitrators alike. Continuing on this course, FSI appreciates the opportunity to comment on the Proposal, and the significant concerns that the Proposal raises for FSI's membership.

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<sup>1</sup> SEC, *Notice of Filing of a Proposed Rule Change to Amend the FINRA Code of Arbitration Procedure for Customer Disputes and the FINRA Code of Arbitration Procedure for Industry Disputes To Apply Minimum Fees to Requests for Expungement of Customer Dispute Information*, 85 Fed. Reg. 11165 (Feb. 16, 2020).

<sup>2</sup> FINRA Regulatory Notice 17-42 is available at [https://www.finra.org/sites/default/files/notice\\_doc\\_file\\_ref/Regulatory-Notice-17-42.pdf](https://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-17-42.pdf).

## **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>3</sup> These financial advisors are self-employed independent contractors, rather than employees of the Independent Broker-Dealers (IBD).<sup>4</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>5</sup>

## **Background on the Proposal**

The Central Registration Depository (CRD) is the central licensing and registration system used by FINRA, the SEC, state securities regulators and other members of the regulatory community. FINRA also makes certain information in the CRD system available publicly through BrokerCheck. An associated person may seek expungement of customer dispute information in the CRD system and disclosed through BrokerCheck 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."<sup>6</sup> FINRA requires associated persons seeking expungement of customer dispute information to (i) go through FINRA arbitration and obtain an order from a court of competent jurisdiction confirming an award recommending expungement relief or (ii) go directly to court (without first going through FINRA arbitration).<sup>7</sup> If an associated person seeks expungement through FINRA arbitration, the associated person may request the expungement during a customer arbitration, or the associated person may file the expungement request against a former or current firm or a customer outside of customer arbitration.

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<sup>3</sup> Cerulli Associates, Advisor Headcount 2016, on file with author.

<sup>4</sup> The use of the term "financial advisor" or "advisor" in this letter is a reference to an individual who is a dually registered representative of a broker-dealer and an investment adviser representative of a registered investment adviser firm. 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>5</sup> Oxford Economics for the Financial Services Institute, The Economic Impact of FSI's Members (2016).

<sup>6</sup> FINRA Rule 2080(b)(1).

<sup>7</sup> FINRA Rule 2080(a).

Among other things, the Proposal amends the Codes with respect to the amount of the member firm surcharge and process fees assessed when associated persons file expungement requests against a former or current firm or customer outside of the customer arbitration proceeding (Straight-in Request).

## **I. Member Firm Surcharge for Straight-in Requests**

The Proposal would require FINRA member firms to pay a minimum surcharge when an associated person files a Straight-in Request for expungement against the member firm and/or a customer. For example, if an associated person files a Straight-in Request against a FINRA member firm, the Proposal would require the firm to pay a firm surcharge for a non-monetary claim of \$1900.<sup>8</sup> In addition, the Proposal would require, for Straight-in Requests for expungement filed against a customer, each FINRA member firm that employed the associated person at the time the customer dispute arose to pay the firm surcharge for a non-monetary claim of \$1,900.<sup>9</sup> If the associated person were to add a separate claim for damages to the Straight-in Request for expungement against the customer or FINRA member firm, the firm would pay a surcharge equal to the firm surcharge for a non-monetary claim or the applicable surcharge under the Codes, whichever is greater.<sup>10</sup>

## **II. Member Firm Process Fees for Straight-in Requests**

The Proposal would also require FINRA member firms to pay a minimum process fee when an associated person files a Straight-in Request for expungement, regardless of whether the member firm is named as a party to the expungement request.<sup>11</sup> If an associated person files a Straight-in Request against a member firm, that member firm would be assessed the process fee for a non-monetary claim of \$3,750. The Proposal also clarifies that, for Straight-in Requests filed against a customer, the member firm that employed the associated person at the time the customer dispute arose would be assessed the process fee for a non-monetary claim of \$3,750.<sup>12</sup> However, if an associated person adds a separate claim for damages to the Straight-in Request against the customer or member firm, the Proposal would require a member firm to pay a process fee equal to (i) the process fee for a non-monetary claim of \$3,750 or (ii) the applicable process fee under the Codes, whichever is greater.<sup>13</sup>

FINRA acknowledges that the majority of expungement requests that it tracked from January 2016 to June 2019 were filed as Straight-in Requests.<sup>14</sup> Under the Proposal, FINRA notes that an associated person filing a Straight-in Request for expungement against a member firm, assuming one prehearing conference and one hearing session on the merits, would result in the associated person and member firm being assessed minimum fees totaling \$9,475.<sup>15</sup> The associated person would be assessed a minimum filing fee of \$1,575 and a minimum hearing

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<sup>8</sup> Proposed Customer Code Rule 12901(a)(3) and Proposed Industry Code Rule 13901(c).

<sup>9</sup> *Id.*

<sup>10</sup> *Id.*

<sup>11</sup> Proposed Customer Code Rule 12903(b) and Proposed Industry Code Rule 13903(b).

<sup>12</sup> Proposed Customer Code Rule 12903(c) and Proposed Industry Code Rule 13903(c).

<sup>13</sup> *Id.*

<sup>14</sup> SEC, *Notice of Filing of a Proposed Rule Change To Amend the FINRA Code of Arbitration Procedure for Customer Disputes and the FINRA Code of Arbitration Procedure for Industry Disputes To Apply Minimum Fees to Requests for Expungement of Customer Dispute Information*, 85 Fed. Reg. 11165, 11169 (Feb. 16, 2020).

<sup>15</sup> *Id.* at 11167 n. 24.

session fee of \$2,250 (\$1,125 for the prehearing conference and \$1,125 for the hearing session on the merits), while the firm would be assessed a minimum surcharge of \$1,900 and a minimum process fee of \$3,750.<sup>16</sup>

As a result, member firms that are respondents or employed the associated person seeking expungement, not the associated person or customer, pay the majority of the expenses through the member surcharge and process fee.

### **Discussion**

FSI appreciates the opportunity to comment on the Proposal. FSI believes that the Proposal raises concerns for FSI members, which are discussed in more detail below.

An associated person's Straight-in Request for expungement to remove customer dispute information from CRD is fundamentally different from any other industry or customer dispute involving a FINRA member firm. Typically, member firms have an interest in participating in industry and customer disputes, and a firm's participation in such disputes is often necessary to protect the firm's interest. However, an associated person's interest, and not necessarily a member firm's interest, is primarily served when the associated person files a Straight-in Request for expungement. FSI recognizes that member firms are ordinarily parties to an associated person's expungement request, whether the expungement request is filed during a customer arbitration or as a Straight-in Request. The Notice will result in member firms bearing the increased costs associated with Straight-in Requests for expungement even though member firms do not have control over whether the associated person files a request for expungement.

FSI recommends amending the Proposal to provide that the Director of the Office of Dispute Resolution will refund the member firm surcharge and process fees when a member firm is required to participate in an associated person's Straight-in Request for expungement, so long as the arbitration panel denies the associated person's expungement request<sup>17</sup> or, more importantly, on the member firm's showing of financial hardship.<sup>18</sup>

We would also urge FINRA to address an underlying concern related to this Proposal which stems from FINRA's requirement (as stated in FINRA Regulatory Notice 08-20) that member firms disclose customer complaints on its representatives CRD even if the representative is not named as a party. As a practical matter, under the Proposal, the firm and its representatives will be responsible for significant amounts in arbitration fees for expunging a complaint where the representative is not named as a party. We urge FINRA to re-consider this issue.

### **Conclusion**

We are committed to constructive engagement in the regulatory process and welcome the opportunity to work with the SEC on this and other important regulatory efforts.

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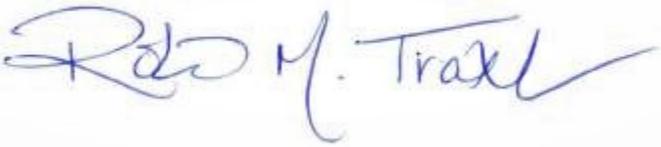
<sup>16</sup> Id. at 11167 n. 24.

<sup>17</sup> See e.g., FINRA Rule 12901(b)(1). Under this rule, the Director of the Office of Dispute Resolution will refund the member surcharge in a customer arbitration if the arbitration panel denies all of the customer's claims against the member or associated person and allocates all hearing session fees against the customer.

<sup>18</sup> See e.g., FINRA Rules 12900(a)(1) and 13900(a)(1). Under these rules, the Director of the Office of Dispute Resolution may defer payment of all or part of an associated person's filing fee on a showing of financial hardship. This waiver also applies to expungement requests.

Thank you for considering FSI's comments. Should you have any questions, please contact me at (202) 393-0022.

Respectfully submitted,

A handwritten signature in blue ink that reads "Robin M. Traxler". The signature is fluid and cursive, with the first name "Robin" being particularly stylized.

Robin M. Traxler, Esq.  
Senior Vice President, Policy & Deputy General Counsel

cc: Patrice Gliniecki, Senior Vice President and Deputy General Counsel, FINRA  
Mignon McLemore, Assistant General Counsel, FINRA