HENNION & WALSH
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VIA EMAIL (rule-comments@sec.gov)
September 6, 2022

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

Re: FILE Number SR-FINRA-2022-024

To Whom It May Concern:

On behalf of Hennion & Walsh, Inc., we are grateful for the opportunity to present our views on the new rules proposed by FINRA pertaining to the Expungement Process. This letter respectfully submits our comments.

Preliminarily, Hennion & Walsh, Inc. supports the arbitration process as a whole. However, it believes that it has strayed from its' original intent to provide a fair, equitable and cost-effective mechanism through which customers and the financial industry may resolve disputes. The recent proposal by FINRA accelerates the dismantling of a process which as stated by FINRA:

> The expungement framework seeks to balance the important benefits of disclosing information about customer disputes to investors and regulators with the goal of protecting brokers from the publication of inaccurate allegations against them.

See https://www.finra.org/rules-guidance/key-topics/expungement

A careful review of the statistics put forth by FINRA in support of the amendments reflect that expungements are rarely sought. To this, we suggest that the costs involved are the deterrent - not the fact that the claim had merit. Accordingly, we respectfully urge the Commission to extend the comment period and invite the small broker dealer community to meaningfully engage in discourse on this topic with both FINRA and the Commission. The unintended consequence of making expungement cost prohibitive is a spill-over effect with interaction on FINRA Rule 4111, acceleration of both representative and broker dealer departure from the industry and further customer reliance on message boards, cyber chats or "artificial intelligence" for investment guidance.

Hennion & Walsh, Inc. is a broker dealer and is categorized as a small firm under FINRA metrics. It has been in business for approximately 30 years and in that time-frame has witnessed the steady and continuous decline in registration of both broker dealers and the registered representatives that work there. Hennion & Walsh, Inc. is aligned with the industry with its general concern about a crisis of interest, engagement and employment from younger generations that want to work in the industry. We support initiatives such as the SIE exam which is intended to create interest and excitement with careers in finance. However, the Firm respectfully suggests that the current proposal by FINRA to amend the arbitration code to further restrict the expungement process will result in the further dismantling of small retail operations as the expungement process for its' employees becomes further out of reach due to expense. Further, it will result in the removal from the industry of registration representatives who lack the knowledge or funds to protect their license by seeking an expungement of meritless claims.

Generally speaking, when a customer complaint is received, a representative is challenged by state authorities when renewing his or her state licenses. Firms are often asked to place the representative on heightened supervision, although the complaint has not been found to have merit. The representative's efforts to grow or maintain his or her business is thwarted by what is often a misguided complaint seeking to lay blame against someone for a product failure or a bad market environment. Firms are reluctant to take on this burden (rightfully so as it increases its's risk for a failure to supervise allegation) and thus all parties lose out. The state loses out from having a qualified individual contribute to its' coffers and invest in its' constituents financial well-being. The individual representative loses out on the opportunity to develop client relationships, grow his or her book of business and hence, stability in his or her career. Finally, the firm loses out due to missed opportunity to develop a lasting relationship with both a representative and a client(s).

Those are the challenges faced by a representative at the state level. However, most complaints also result in a FINRA inquiry. Each such inquiry begins with a boiler-plate request for documents and from there may result in follow-up inquiries. These inquiries pose a burden to any firm but most especially to small firms that typically function with the right number of staff – in exact proportion to meet its' every- day needs.

Most recently, maintaining customer complaints on a representative's license has taken a new turn which may further accelerate the removal of firms and individuals from the marketplace. With the passage of FINRA Rule 4111, the regulatory presumption is that a complaint is valid and it is automatically counted against a Firm on an annual basis for the next five (5) years. Upon hitting a certain threshold, the Firm's ability to continue in business may be called into question and the representative may in fact be "culled" from the firm to save itself. All of this takes place – regardless of whether the complaint had merit or was in fact performance driven.

When FINRA statistics are reviewed, it is apparent that expungements are in fact rare. The Firm attributes this to the sheer expense involved when a representative undertakes an expungement. From an industry perspective, the legal fees for an expungement start typically start at $10,000.00. This is independent of FINRA Dispute Resolution charges which can also total in the thousands. While representatives are not required to be represented by counsel when filing for expungement, practically speaking it would be difficult if not impossible for the representative to accomplish the service requirement, document collection (often to third parties) and effective drafting of the pleading without legal assistance.

In many small firms, representatives are contractually obligated to pay for all of the costs associated with a complaint. For the impact of that please consider the following:

Approximate costs for a FINRA arbitration on a claim seeking $100,000 or less:

- Approximate legal fees on the claim itself $30,000 to 50,000.00+ (outside counsel)
- Expert profit & loss $2, 000+
- Expert witness $5,000+
- Travel expenses for out of state hearing $2,500+
- Mediation fees $5,000+
- FINRA Fees $7,000+

While all numbers are an approximation, they are significant. Should the case go to a hearing, these numbers will in all likelihood triple. When viewed in this context, settled for a "business expense" becomes the unfortunate norm. Unfortunately, in choosing the lesser of two evil and settling the case, the firm and the representative set the stage where that arbitration may be the tipping point where one or both are ultimately ushered out of the industry. A fair and equitable expungement process is the only way to potentially avoid an unwarranted fate.

Notably, FINRA discloses that "[c]urrently, member firms and associated persons are assessed 84 percent of total (arbitration forum) fees, while customers are assessed 15 percent." https://www.finra.org/sites/default/files/Final-DR-task-force-report.pdf Smaller firms generally lack the bargaining power of the larger organizations due to the fact that they do not have a steady stream of complaints to dispense to law firms. Thus, the smaller firms do not qualify for law firm "rate" deals and these costs typically do not include an expungement request. Filing for an expungement entails generally an additional $10,000 in legal costs (conservatively) plus several thousands in expungement related FINRA fees. Consequently, one (1) complaint (whether meritorious or not) can derail a representative's career.

FINRA recognizes the challenges posed by self-representation for customers and provides support – with, for example, referrals to law clinics, reduced fees for small claims and fee waivers in certain instances. No such support is provided to a registered representative that may have been falsely named. Over the years, the argument in support of the fairness and balance provided by arbitrations has been re-framed. The allegations raised by the customer are now deemed by default to be accurate and expungement is an extraordinary remedy warranted only in extremely limited circumstances. However, the statistics just do not support that further amendment to the arbitration code is warranted.

As per FINRA, "[o]f the approximately 35,000 customer dispute information disclosures in the CRD system entered between 2015-2020, approximately 1,550 or 4% have been expunged pursuant to a court order as of May 25, 2021. See https://www.finra.org/rules-guidance/key-topics/expungement#:~:text=Of%20the%20approximately%2035%2C000%20customer,data%20and%20analysis%20regarding%20expungements. Such a small number is generally not deemed to be statistically significant and, as such, it begs the question as to whether more restrictive change is needed

In support of the filing, FINRA relied upon a 2016-2021 timeframe, which lapped the collapse of the Puerto Rico bond market, interest rate disruptions and pandemic related volatility. We respectfully suggest that this shortened time frame presents a skewed time frame under which any statistics could reasonably be drawn. Nonetheless, even by using this time frame the argument supporting the necessity for further change appears tenuous and the statistics referred to de-minimus. Moreover, when the amendments were originally contemplated by NAMC, the committee did not include a representative from a small retail firm (upon belief). Thus, the thoughts, concerns and viewpoint of in-excess of 90% of registered firms and representatives were excluded from the process.

Prior commentary from FINRA on the arbitration process should guide us in this analysis and such commentary includes the following (emphasis added):

- "Arbitration is a method of resolving a dispute between two or more parties. Parties agree in advance to abide by the decision of the arbitrators, who are impartial persons committed to rendering a **fair and impartial decision** after all parties have had an opportunity to present their cases…"
- "In short, arbitration is a **quick, fair, and relatively inexpensive alternative to litigation**.
- Since arbitration is the primary means of resolving disputes in the securities industry, the public **perception of its fairness is of paramount importance**."

- "Equity is justice in that it goes beyond the written law. And it is equitable to prefer arbitration to the law court, for the arbitrator keeps **equity in view**, whereas the judge looks only to the law, and the reason why arbitrators were appointed was that **equity might prevail**." — Domke on Aristotle
- "FINRA pledges to provide impartial, knowledgeable and courteous staff and highly trained, independent arbitrators and mediators committed to delivering **fair, expeditious and cost-effective dispute resolution services for investors, brokerage firms and their employees**."
- **"Therefore, it is particularly important in arbitration that the forum be fair and be perceived to be fair."**

For all citations above please refer to the **FINRA Dispute Resolution Services Arbitrator's Guide**

Arbitration is not just for investor protection but it is for protection of the industry as a whole – this necessarily includes the registered representatives and firms that are mandated by FINRA to engage with customers through its' proprietary dispute resolution process. The whole purpose of the arbitration process is to provide an efficiency of process - to reduce costs and time. It is supposed to be fair - for firms and representatives too.

As FINRA has acknowledged, during the 2015 to 2020 timeframe, "…there were, on average, 632,500 brokers registered with FINRA about whom a customer dispute could have been reported in the CRD system." Of this pool, 1,300 expungements were granted. Respectfully, these numbers do not support the argument that there is any need for a change to make the expungement process more restrictive. Rather, these statistics suggest that the proposed expungement amendments further remove the process from those registered representatives and firms that most need a fair and equitable process – small firms and newly registered representatives.

To avoid creating the impression of bias against the representative and the industry as a whole – if the need for change exists it exists to make expungements more accessible – not less. If the existing roster of arbitrators is deemed to be qualified to determine the merits of the underlying complaint, how are they not qualified to determine whether an expungement is warranted? When viewed in that light, a special roster of arbitrators (who presumably will have to pay FINRA Dispute Resolution for special training) appears to be as unnecessary as tripling the number of arbitrators (and their associated cost) when one arbitrator was deemed sufficient to preside over the underlying case.

The Firm respectfully suggests that an alignment between the customer Code of Arbitration and the Expungement Process is over-due and will serve both the needs of the investing public and the industry. Accordingly, the filing fees and hearing structure provided to customers should also be

available registered representatives seeking expungement and the Firm suggests the following as an important step towards reaching a balance in the current system:

- Time limits for filing an expungement request should mirror those provided to customers (a six-year period of eligibility with expansion for good cause. This will recognize that the filing of a customer complaint does not correlate with a representatives ability to afford the expungement process or other factors were involved such as separation from the Firm (moved into a non-client facing role elsewhere) or temporary departure from the industry (ex. individuals that depart to care for their children or aging parents).
- A simplified expungement process with like fees and an "on the papers" review option by a single arbitrator for written customer complaints and arbitrations under $50,000.00 at the election of the registered representative to mirror the customer code.
- Ability to have an industry arbitrator on any expungement panel where more than one arbitrator was required.
- Ability to strike, rank and stipulate as to arbitrators – given that customers have the same ability.
- Providing the representative with the opportunity to file for an expungement within a six-year time frame – regardless of whether there was a customer filed arbitration in recognition of the fact that representatives may not have been meaningfully involved in the underlying arbitration for a variety of reasons (separation from the Firm, left the industry, subject of only, finances).
- Affording the representative to withdraw and re-file (as customers may).
- Maintaining notification to state regulators regarding the expungement – at the time when they have the ability to become involved- at the state court confirmation level.

Maintaining false and erroneous information on a registered representative's record does not "protect the investing public". It does not serve the interests of an industry that is trying to maintain an interested and informed work force. Moreover, it does not help customers trying to find personal financial advice in an environment that is increasingly offering smaller investors only artificial intelligence options.

In 2005, there were approximately 6,000 customer arbitrations filed – as of 2022 that number was approximately 1,400. While the filings have fluctuated in the interceding years, they are generally on the decline. Declining filings should support the notion that the industry as a whole is functioning well – not signal that the system is somehow flawed. Further, an increase of filings following market events supports the notion that many complaints are market driven and are not necessarily indicative of representative or firm wrong-doing. Often, a representative that

recommended a product that ultimately did not perform in line with expectations is the recipient of multiple complaints. This is due to his or her recommendation of a product that performed poorly to multiple customers and/or an aggressive advertising campaign by the plaintiffs bar. The poor performance of a product does not equate to malfeasance and such a complaint is not and should not be dispositive that a sales practice violation occurred.

From an economic burden, from the standpoint of maintaining a fair and impartial dispute resolution process for all and to prevent any unintended consequences under FINRA Rule 4111, Hennion and Walsh, Inc. respectfully urges the Securities & Exchange Commission to reject FINRA's proposed amendments to the Code of Arbitration Procedure. We also urge the Commission to recognize that the investing public as a whole is currently underserved. A large portion, especially younger investors, are increasingly reliant on chat rooms, message boards, algorithms and marketing ploys for investing advice. Actions, such as the proposed expungement process amendments, may accelerate representative departure from the industry (resignations, Rule 4111 "cullings" or retirements). The changes proposed are most likely to impact younger representatives, representatives who put their careers on pause to care for children or aging parents or those that have not yet reached financial security from a diverse and stable book of business.

An overly restrictive expungement process may also serve to disincentivize new employees from joining the industry. Entering the financial industry typically comes with a significant price tag when quantifying the deferred compensation time from a lengthy study time period and years of prospect interaction as a representative attempts to build a book of business. For many representatives, the first few years in the industry are extremely difficult. Financial support from most firms is minimal and many representatives rely on family support, second jobs and/or loans to get through. Adding an exorbitant expungement expense on top of that is insurmountable for most. The costs to employment in the financial industry (deferred compensation + expenses such as licensing fees) could very well be a significant contributing factor for the industry's low diversity and inclusion metrics, which the proposed expungement changes may worsen.

Unfortunately, the expungement process is already out of reach for many representatives due to the sheer financial burden. Restricting it further has consequences far beyond those contemplated by the amendments and the Firm respectfully urges the Commission to reject the proposed amendments.

Regards,

Jennifer W. Burke, Esq.
On Behalf of Hennion & Walsh, Inc.