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April 3, 2023

Ms. Vanessa Countryman  
Secretary  
U.S. Securities and Exchange Commission  
100 F Street, N.E.  
Washington, DC 20549-1090

**RE: File No. SR-FINRA-2022-024 (Proposed Rule Change to Amend the Codes of Arbitration Procedure to Modify the Current Process relating to the Expungement of Customer Dispute Information) – Response to Comments No. 2**

Dear Ms. Countryman:

This letter is being submitted by the Financial Industry Regulatory Authority, Inc. (“FINRA”) in response to comments received by the Securities and Exchange Commission (“SEC” or “Commission”) regarding the above-referenced rule filing. The proposed rule change would 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 modify the current process relating to the expungement of customer dispute information from the Central Registration Depository (CRD®) system (“Proposal”).<sup>1</sup>

Specifically, the Proposal would amend the Codes to impose requirements on expungement requests (a) filed by an associated person during an investment-related, customer-initiated arbitration (“customer arbitration”), or filed by a party to the customer arbitration on behalf of an associated person (“on-behalf-of request”), or (b) filed by an associated person separate from a customer arbitration (“straight-in request”). Specifically, the Proposal would: (1) require that a straight-in request be decided by a three-person panel that is randomly selected from a roster of experienced public arbitrators with enhanced expungement training (“Special Arbitrator Roster”); (2) prohibit parties to a straight-in request from agreeing to fewer than three arbitrators to consider their expungement requests, striking any of the selected arbitrators, stipulating to an arbitrator’s removal or stipulating to

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<sup>1</sup> See Securities Exchange Act Release No. 95455 (August 9, 2022), 87 FR 50170 (August 15, 2022) (Notice of Filing of File No. SR-FINRA-2022-024) (“Initial Filing”).

the use of pre-selected arbitrators;<sup>2</sup> (3) provide notification to state securities regulators of all expungement requests and a mechanism for state securities regulators to attend and participate in expungement hearings in straight-in requests; (4) impose strict time limits on the filing of straight-in requests; (5) codify and update the best practices in the Notice to Arbitrators and Parties on Expanded Expungement Guidance applicable to all expungement hearings, including amendments to establish additional requirements for expungement hearings, to facilitate customer attendance and participation in expungement hearings and to codify the panel's<sup>3</sup> ability to request any evidence relevant to the expungement request;<sup>4</sup> (6) require the unanimous agreement of the panel to issue an award containing expungement relief; and (7) establish procedural requirements for filing expungement requests, including for on-behalf-of requests. The Proposal would also amend the Customer Code to specify procedures for requesting expungement of customer dispute information during simplified arbitrations.

The Commission published the Proposal for public comment in the Federal Register on August 15, 2022, and received 45 comments in response. On November 10, 2022, FINRA responded to the comments and filed Partial Amendment No. 1 to the Proposal to propose amendments based on the comments received by the SEC.<sup>5</sup>

On November 16, 2022, the SEC published a notice and order in the Federal Register to solicit comments on the Proposal and to institute proceedings pursuant to Section 19(b)(2)(B) of the Securities Exchange Act of 1934 ("SEA") in the above-referenced rule

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<sup>2</sup> Proposed Rule 13806(b)(4) provides, in relevant part, that the associated person requesting expungement of customer dispute information shall not be permitted to strike any arbitrators selected by the list selection algorithm nor stipulate to their removal, but shall be permitted to challenge any arbitrator selected for cause pursuant to Rule 13410. The intent of the proposed rule is to prohibit *all parties* to a straight-in request from striking or stipulating to the removal of any arbitrator on the panel, not solely the associated person. Thus, FINRA is proposing a clarifying change in Partial Amendment No. 2 that would replace "associated person" with "parties" in proposed Rule 13806(b)(4).

<sup>3</sup> Under the Codes, the term "panel" means the arbitration panel, whether it consists of one or more arbitrators. See Rules 12100(u) and 13100(s). Unless otherwise specified, FINRA uses the term "panel" to mean either a panel or single arbitrator.

<sup>4</sup> See FINRA Dispute Resolution Services, Notice to Arbitrators and Parties on Expanded Expungement Guidance ("Guidance"), <https://www.finra.org/arbitration-and-mediation/notice-arbitrators-and-parties-expanded-expungement-guidance> (last updated September 2017).

<sup>5</sup> See Letter from Mignon McLemore, Associate General Counsel, FINRA, to Vanessa Countryman, Secretary, SEC, dated November 10, 2022 ("Response Letter") and Partial Amendment No. 1 to SR-FINRA-2022-024 filed on November 10, 2022 ("Partial Amendment No. 1"), <https://www.finra.org/rules-guidance/rule-filings/sr-finra-2022-024>.

filing to determine whether to approve or disapprove the Proposal.<sup>6</sup> The SEC received seven comment letters in response to the Order.<sup>7</sup> PIABA and PIABA Foundation stated their support for the Proposal and recommended that the SEC approve the Proposal. NASAA generally supported the Proposal, but also suggested one additional modification. Grebenik supported some aspects of the Proposal, but opposed other aspects of the Proposal and suggested modifications. Del Toro and SIFMA opposed the Proposal and suggested further modifications or that the SEC disapprove the Proposal. Wagner did not indicate whether he supported the Proposal.

FINRA submits this response to the commenters' material concerns.

### **I. Opposition to Key Changes in the Proposal**

FINRA is concerned that the current expungement process is not working as intended—as a remedy that is appropriate only in extraordinary circumstances in accordance with the narrow standards in FINRA rules. FINRA filed the Proposal to address concerns that FINRA and other interested parties have identified with the current expungement process.<sup>8</sup> The Proposal includes key changes that would make substantial enhancements to the current expungement process and, thereby, would help protect the integrity of the information in the CRD system, the central licensing and registration system used by the U.S. securities industry and its regulators.<sup>9</sup> These key changes are intended to balance the competing interests of providing regulators with broad access to information about customer disputes to fulfill their regulatory obligations, providing a fair process that recognizes an associated person's interest in protecting their

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<sup>6</sup> See Securities Exchange Act Release No. 96298 (November 10, 2022), 87 FR 68779 (November 16, 2022) (Order Instituting Proceedings to Determine Whether to Approve or Disapprove File No. SR-FINRA-2022-024) (“Order”).

<sup>7</sup> See Letter from Tosh Grebenik, Founder, Judex Law, LLC, dated November 21, 2022 (“Grebenik”); letter from Andrew Hartnett, President, North American Securities Administrators Association, Inc., to J. Matthew DeLesDernier, Assistant Secretary, SEC, dated December 7, 2022 (“NASAA”); letter from Hugh D. Berkson, President, Public Investors Advocate Bar Association, to Vanessa Countryman, Secretary, SEC, dated December 7, 2022 (“PIABA”); letter from Celiza P. Bragança, Past-President & Director, & Jason R. Doss, Past-President & Founding Director, The PIABA Foundation, Inc., to J. Matthew DeLesDernier, Assistant Secretary, SEC, dated December 7, 2022 (“PIABA Foundation”); letter from Kevin M. Carroll, Managing Director & Associate General Counsel, SIFMA, to Vanessa Countryman, Secretary, SEC, dated December 7, 2022 (“SIFMA”); letter from Allen Wagner, dated December 7, 2022 (“Wagner”); and letter from Russell Del Toro, Esq., TCM, P.S.C., to Vanessa Countryman, Secretary, SEC, dated December 21, 2022 (“Del Toro”). The PIABA Foundation is a separate entity from PIABA.

<sup>8</sup> See Proposal, supra note 1, 87 FR 50170, 50174.

<sup>9</sup> See Proposal, supra note 1, 87 FR 50170, 50172.

reputation, and ensuring investors have access to accurate information about associated persons with whom they may decide to do business.

However, Grebenik and Del Toro opposed many of the key changes in the Proposal. For example, Grebenik recommended: removing the requirement that the panel from the Special Arbitrator Roster consist of three public chairpersons; removing the requirement that arbitrators on the Special Arbitrator Roster must take the enhanced expungement training or alternatively, ensuring that the training is “neutral/informative”;<sup>10</sup> removing the prohibition on striking arbitrators when selecting a panel from the Special Arbitrator Roster; permitting an authorized state representative to participate only in an “observer role” in straight-in requests; and removing the requirement that arbitrators unanimously agree to issue an award containing expungement relief. Also, Grebenik opposed “codify[ing the] best practices” contained in the Guidance, suggesting that “the ‘best practices’ are actually just practices that limit expungement” and recommended that the best practices “should be neutral/informative instead of persuasive and advocating.”

Del Toro similarly opposed the requirement that the panel from the Special Arbitrator Roster consist of three public chairpersons who would not be required to have experience hearing and deciding expungement requests, the prohibition on ranking and striking arbitrators selected from the Special Arbitrator Roster, and the requirement that the arbitrators agree unanimously to issue an award containing expungement relief.<sup>11</sup>

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<sup>10</sup> Grebenik suggested that the training would include “coercive language to convince expungement panels to stop granting expungements,” and suggested that “[t]he training should be made public.” FINRA notes that, like other arbitrator training provided by FINRA’s Dispute Resolution Services (“DRS”), the proposed training will be neutral and informative, and it will be publicly available on FINRA’s website. See Arbitrator Training, <https://www.finra.org/arbitration-mediation/arbitrator-training>; see also Response Letter, supra note 5, Section XI.B.1., “Eligibility Requirements for the Special Arbitrator Roster.”

<sup>11</sup> Del Toro stated that these proposed changes, along with others, would make it difficult for the Proposal “to withstand constitutional scrutiny.” It is well-settled that FINRA, as a self-regulatory organization, is not a state actor. Instead, FINRA is a private entity – it was not created by the government, its board is not appointed by the government, and it does not receive federal funding. Accordingly, the actions FINRA takes in furtherance of its self-regulatory responsibilities, such as engaging in rule making, are private actions, not governmental actions. Because FINRA is not a state actor and does not engage in governmental actions, its conduct is not subject to the requirements of the U.S. Constitution and other provisions of federal law that apply only to governmental actors. See, e.g., Letter from Marcia E. Asquith, Corporate Secretary, EVP, Board & External Relations, FINRA, to Vanessa M. Countryman, Secretary, SEC (Comment on File No. S7-05-15), dated September 27, 2022, Section VI., “The Re-Proposal Would Not Transform FINRA Into a State Actor.”

In addition, Del Toro opposed “disallowing expungement requests from [unnamed associated persons] to be withdrawn prior to final hearing if requested in the underlying action[,] imposing non-substantive technical requirements on the participation of [associated persons] while specifically making those same requirements inapplicable to other participants[ and] prohibiting [associated persons] from initiating FINRA proceedings against customers to seek expungement relief . . . .”<sup>12</sup> Del Toro also opposed “deny[ing] an affected intervening [associated person] the chance to have their expungement request heard before the panel with the presence of the customers and their counsel” and “requir[ing] an [associated person] who is a named party to request expungement in the original case and see that request through should the case go to final hearing.” Del Toro also expressed concern about the Proposal’s requirement that the party seeking expungement include the customer’s current address, stating that it “creates further unnecessary risks of error.” He also opined that the Proposal should not limit an associated person’s method of appearance “if other reasonable methods of participation are available.”<sup>13</sup> Finally, Del Toro suggested changes to the “time limits on filing straight-in expungement requests, [the] requirement that named parties seek expungement during the [customer arbitration], and limitations to seeking expungement in certain circumstances.”

Commenters to the Initial Filing raised a number of the same comments. FINRA considered and addressed those comments in the Response Letter and, therefore, incorporates those responses herein.<sup>14</sup> For those comments by Grebenik and Del Toro not raised on the Initial Filing, FINRA provides its responses below.

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<sup>12</sup> With respect to Del Toro’s opposition to “disallowing expungement requests from [unnamed associated persons] to be withdrawn prior to final hearing if requested in the underlying action,” Del Toro also stated that “[t]here are [a] number of valid and practical reasons for why a[n unnamed associated person’s] request for expungement may be withdrawn prior to final hearing, the most common being time and costs.” FINRA notes it is not in a position to determine or assess, on a case-by-case basis, the legitimacy of an associated person’s reason for withdrawing an expungement request during a customer arbitration. See also infra note 14 and accompanying text.

<sup>13</sup> See Del Toro (stating that “the panel should also have discretion to decide the appropriateness of the manner and form of the requesting [associated persons’] participation given the circumstances”).

<sup>14</sup> For example, FINRA incorporates its previous responses regarding concerns about:

- the eligibility criteria for the Special Arbitrator Roster, including arbitrator classification and the training requirement, Response Letter, supra note 5, Section XI.B.1., “Eligibility Requirements for the Special Arbitrator Roster”;
- the inability to strike and rank arbitrators, Response Letter, supra note 5, Section XI.B.2., “Composition of a Panel”;

In response to Grebenik's concern about codifying the Guidance, FINRA notes that the Guidance explains the requirements of Rules 12805 and 13805 and provides arbitrators with best practices and recommendations to follow when deciding expungement requests.<sup>15</sup> FINRA believes the provisions of the Guidance would be more effective if they were included in the Codes.

In response to Del Toro's opposition to the prohibition in the Proposal on associated persons filing straight-in requests against a customer, FINRA disagrees with the commenter. FINRA does not believe that customers should be compelled to attend or participate in a separate proceeding to decide an expungement request after the customer has resolved their arbitration claim or civil litigation.<sup>16</sup> Based on FINRA's experience with straight-in requests filed in the DRS arbitration forum, associated persons typically file their straight-in requests against the member firm at which the associated person is currently employed. However, the Proposal's

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- permitting the states to participate in straight-in requests, Response Letter, supra note 5, Section II., "State Attendance and Participation in Straight-In Requests";
  - requiring arbitrators to unanimously agree to award expungement, Response Letter, supra note 5, Section V., "Unanimous Decision to Issue an Award Containing Expungement Relief";
  - prohibiting an expungement request from being withdrawn once filed, Response Letter, supra note 5, Section XII.C., "Prohibiting Expungement Requests from Being Withdrawn";
  - prohibiting a nonparty from intervening in a customer's arbitration, Response Letter, supra note 5, Section XII.D.1., "Intervention in a Customer Arbitration by an Unnamed Person";
  - imposing time limits to file straight-in requests within: (a) two years of the close of the customer arbitration or civil litigation that gave rise to the customer dispute information and (b) three years of the date the customer complaint was initially reported in the CRD system and there was no customer arbitration or civil litigation associated with the customer dispute information, Response Letter, supra note 5, Section IX., "Limitations on Expungement Requests"; and
  - requiring an associated person named as a respondent to request expungement during the customer's arbitration and requiring an expungement request to be decided if the customer arbitration is decided by award, Response Letter, supra note 5, Section XII., "Requests For Expungement Under the Customer Code."

<sup>15</sup> Proposal, supra note 1, 87 FR 50170, 50173.

<sup>16</sup> Proposal, supra note 1, 87 FR 50170, 50178.

requirement that the associated person must file the straight-in request against the member firm at which the person was associated at the time the customer dispute arose would help ensure that there is a connection between the respondent firm and the subject matter of the expungement request.<sup>17</sup> For example, the firm at which the person requesting expungement was associated at the time the dispute arose should have knowledge of the dispute and access to documents or other evidence relating to the dispute.<sup>18</sup> In addition, the proposed requirement would help ensure that the panel from the Special Arbitrator Roster would be able to request evidence from the member firm that is relevant to the expungement request.<sup>19</sup> If the requisite connection is not present, the Director would be authorized to deny the use of the DRS arbitration forum for the request.<sup>20</sup>

In response to Del Toro's opposition to requiring the party seeking expungement to include the customer's current address with their request, FINRA believes that the associated person seeking expungement should provide the customer's current address, so that the Director will have the most recent contact information to timely notify the customer of the expungement request, prehearing conferences and expungement hearings.<sup>21</sup>

With respect to Del Toro's comment that the panel should have discretion to decide the appropriateness of the manner and form of the requesting associated person's participation in the expungement hearing, FINRA notes that the Proposal provides the panel with that discretion.<sup>22</sup> The Proposal would require the associated person whose information in the CRD system is the subject of the expungement request, and the party requesting expungement on behalf of an unnamed person or the party's representative, to appear in person or by video conference at the expungement hearing.<sup>23</sup> The method of appearance must be in person or by video conference because FINRA believes the panel may be better able to assess the associated person's credibility through these methods of appearance. For the same reasons, FINRA believes that a party requesting expungement on behalf of an unnamed person or the party's representative must appear in person or by video conference, as such persons would be acting on behalf of the associated person whose information in the CRD system is the subject of the expungement request.

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<sup>17</sup> Proposal, supra note 1, 87 FR 50170, 50179.

<sup>18</sup> See supra note 17.

<sup>19</sup> See supra note 17.

<sup>20</sup> See proposed Rule 13203(b).

<sup>21</sup> Proposal, supra note 1, 87 FR 50170, 50185.

<sup>22</sup> Proposal, supra note 1, 87 FR 50170, 50182.

<sup>23</sup> See proposed Rule 13805(c)(2).

With respect to Del Toro’s comment that “it seems counter-intuitive to deny an affected [unnamed associated person] the chance to have their expungement request heard before the panel with the presence of the customers and their counsel,” FINRA notes that the Proposal would codify the ability of a party to a customer arbitration to file an on-behalf-of request during a customer arbitration.<sup>24</sup> Such a filing would be permissive, not mandatory; however, prior to filing such a request, the unnamed person<sup>25</sup> and the party must execute a form, evidencing the unnamed person’s consent to and the party’s agreement to pursue the request.<sup>26</sup> However, if the associated person is neither a party to the arbitration nor the subject of an on-behalf-of request by another party to the arbitration, FINRA continues to believe that the associated person should not be able to intervene in the customer’s arbitration to request expungement.<sup>27</sup> In these circumstances, the associated person’s conduct is unlikely to be fully addressed by the parties during the customer arbitration, and FINRA does not believe that the customer should have the presentation of their case interrupted or delayed by an associated person’s intervention to request expungement, causing additional cost to the customer.<sup>28</sup>

FINRA believes that these key changes would substantially improve the current expungement process and provide additional safeguards for ensuring that the information in the CRD system and disclosed through BrokerCheck® is accurate and complete. Thus, FINRA declines to amend the Proposal as suggested by the commenters.

## **II. Time Limitations Applicable to Straight-in Requests**

The Proposal would establish separate time limits for requests to expunge customer dispute information arising from customer arbitrations and civil litigations that close, and for customer complaints that were initially reported to the CRD system, after the effective date versus on or prior to the effective date of the Proposal.

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<sup>24</sup> Proposal, supra note 1, 87 FR 50170, 50176–77.

<sup>25</sup> See proposed Rule 12100(ff) (defining an unnamed person as “an associated person, including a formerly associated person, who is identified in a Form U4, Form U5, or Form U6 as having been the subject of an investment-related, customer-initiated arbitration that alleged that the associated person or formerly associated person was involved in one or more sales practice violations, but who is not named as a respondent in the arbitration.”). See also Proposal, supra note 1, 87 FR 50170, 50176 n.63.

<sup>26</sup> See supra note 24.

<sup>27</sup> Proposal, supra note 1, 87 FR 50170, 50178.

<sup>28</sup> See supra note 27.



A. Time Limits Applicable to Customer Arbitrations and Civil Litigations that Close, and Customer Complaints Initially Reported to the CRD System, After the Effective Date of the Proposed Rule Change

1. Two-Year Time Limit Applicable to Customer Arbitrations and Civil Litigations

The Proposal would require associated persons to file straight-in requests under the Industry Code within two years of the close of the customer arbitration or civil litigation associated with the customer dispute information.<sup>29</sup> Del Toro expressed concern that there could be circumstances where an associated person “may not be made aware that the main arbitration has closed and, thus, the two-year time limit has begun to run” on the associated person’s opportunity to request expungement.<sup>30</sup> Del Toro suggested that “[i]f FINRA is to move forward with the two-year time limit, it should adopt a procedure through which all [associated persons] who are affected by a given arbitration claim are given proper notice of the case[’]s closure and the two-year time limit to seek expungement along with any applicable tolling procedure.”

FINRA acknowledges that there could be instances when associated persons may not be aware that a customer arbitration has closed, and that the two-year time limit for requesting expungement of customer dispute information has begun to run. Accordingly, if the SEC approves the Proposal, FINRA will update the cover letter that is provided by DRS to respondents once a statement of claim has been filed (“cover letter”) to explain that (a) an associated person is prohibited from filing a straight-in request while a customer arbitration or civil litigation associated with the customer dispute information that is the subject of the straight-in request is pending; (b) an associated person is permitted to file a straight-in request within two years of the close of a customer arbitration or a civil litigation associated with the customer dispute information, unless such request is barred under the Industry Code; and (c) associated persons may remain apprised of the status of the customer arbitration, including case closure, by contacting the parties to the arbitration or DRS.<sup>31</sup> The cover letter will encourage member firms to provide updates about the status of the customer arbitration to associated persons who are not

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<sup>29</sup> See proposed Rule 13805(a)(2)(A)(vi).

<sup>30</sup> As explained in the Proposal, an associated person would be prevented from filing a straight-in request while a customer arbitration or civil litigation or customer complaint associated with the customer dispute information that is the subject of the straight-in request is pending. See proposed Rule 13805(a)(2)(A)(iii).

<sup>31</sup> Consistent with current practice, member firms and associated persons who are named parties would receive the cover letter through the DR Portal. Following an associated person’s dismissal or withdrawal from a customer arbitration, the associated person would continue to have access through the DR Portal to the cover letter, along with other documents filed in the customer arbitration prior to their dismissal or withdrawal.

named parties to the customer arbitration, including case closure.<sup>32</sup> In addition, FINRA will publish guidance on its website about the changes to the Codes that will include information about how associated persons can remain apprised of the status of a customer arbitration, including through contacting DRS.

## 2. Three-Year Time Limit Applicable to Customer Complaints

The Proposal would require associated persons to file straight-in requests under the Industry Code within three years of the date the customer complaint was initially reported to the CRD system and when no customer arbitration or civil litigation is associated with the customer dispute information.<sup>33</sup> FINRA believes that the proposed three-year time limitation, rather than the current six-year time limitation under Rule 13206 of the Industry Code, is appropriate to help address concerns with straight-in requests.<sup>34</sup>

The three-year time limitation would help address the concern that straight-in requests often lack appreciable opposition since member firms typically do not oppose expungement requests and customers typically do not attend or participate in expungement hearings. The lack of appreciable opposition underscores the importance of the panel's development of a more complete factual record. The three-year time limitation would help ensure that the expungement hearing is held close in time to the events that led to the customer dispute information disclosure, which may increase the likelihood for the customer to participate if they choose to do so. An increase in customer attendance and participation may help a panel develop a more complete factual record on which to decide an expungement request. In addition, the proposed three-year time limitation should help ensure that straight-in requests are filed before relevant evidence and testimony becomes stale or unavailable.

FINRA recognizes that as a result of the three-year time limitation, an associated person may be prevented from filing a request for expungement of customer dispute information because the member firm's investigation of the customer complaint has not concluded and, therefore, the customer complaint associated with the customer dispute information has not

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<sup>32</sup> FINRA's existing rules help ensure that associated persons are aware of arbitration disclosures on their Forms U4 and U5. See, e.g., Rule 1010(c)(2)(A) & (B) and FINRA By-Laws, Article V, Sections 3(a) and 3(b). FINRA also provides several methods for associated persons and former associated persons to check their records, including online through BrokerCheck.

<sup>33</sup> See proposed Rule 13805(a)(2)(A)(vii).

<sup>34</sup> Rule 13206 provides that no claim shall be eligible for submission to arbitration where six years have elapsed from the occurrence or event giving rise to the claim. The panel has discretion to determine if the claim is eligible for arbitration. See also Rule 12206; See also Proposal, supra note 1, 87 FR 50170, 50174 n.38 (discussing the applicability of Rules 12206(a) and 13206(a)).

closed.<sup>35</sup> However, FINRA believes that such instances would occur rarely. As FINRA stated in the Proposal, FINRA believes that the three-year time limitation would generally provide sufficient time for firms to complete their investigation of the complaint, and for associated persons to develop a sense of whether the complaint may evolve into an arbitration or civil litigation and to gather the necessary resources and determine whether to request expungement.<sup>36</sup> Furthermore, in the event that an associated person is prevented from filing a request for expungement of customer dispute information in the DRS arbitration forum because of the three-year time limitation, the associated person could seek a court order directing expungement of the customer dispute information.<sup>37</sup>

B. Time Limits Applicable to Customer Arbitrations and Civil Litigations that Close, and Customer Complaints Initially Reported to the CRD System, on or Prior to the Effective Date of the Proposed Rule Change

The Proposal provides that if an expungement request is otherwise eligible under the six-year limitation period of Rule 13206(a), an associated person would be permitted to file a straight-in request under the Industry Code if: (a) the request for expungement is made within two years of the effective date of the Proposal, and the disclosure to be expunged is associated with a customer arbitration or civil litigation that closed on or prior to the effective date; or (b) the request for expungement is made within three years of the effective date of the Proposal, and the disclosure to be expunged is associated with a customer complaint initially reported to the CRD system on or prior to the effective date.<sup>38</sup> Grebenik suggested that “FINRA should grandfather in [associated persons] who already have disclosures” as an alternative to “[i]mpos[ing] time limits on the filing of straight-in requests.” Conversely, Grebenik suggested that “FINRA should send a notice to all financial advisors giving them a time period in which they must pursue an expungement claim or their opportunity will expire.”

FINRA disagrees with the commenter and continues to believe that the proposed time limitations should apply to associated persons who have customer dispute information on their securities industry records as of the effective date of the Proposal. As discussed above and in the Proposal, the time limits in the Proposal are intended to help address the concern that requests seeking to expunge customer dispute information are made many years after the customer arbitration closes or the customer complaint is reported to the CRD system, when the customer is even less likely to participate and documents or information relating to the dispute may no longer

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<sup>35</sup> See supra note 30.

<sup>36</sup> Proposal, supra note 1, 87 FR 50170, 50181.

<sup>37</sup> Rule 2080; see also Proposal, supra note 1, 87 FR 50170, 50172 (explaining that “FINRA rules require that an associated person must obtain an order from a court of competent jurisdiction (1) directing such expungement or (2) confirming an arbitration award containing expungement relief”).

<sup>38</sup> See proposed Rule 13805(a)(2)(B)(i) and (ii).

be available.<sup>39</sup> If the SEC approves the Proposal, FINRA will issue a Regulatory Notice announcing the effective date of the Proposal. This Regulatory Notice will provide advance notice to associated persons of when the time will commence for seeking expungement of customer dispute information already on their securities industry records.

### **III. Customer Attendance and Participation in Straight-in Requests**

Grebenik expressed concerns that the Proposal would permit all customers whose customer arbitrations, civil litigations or customer complaints are a subject of the expungement request to attend and participate in all aspects of the prehearing conferences and the expungement hearing.<sup>40</sup> In addition, Grebenik stated that the customer should not be able to “request discovery” and notice should be provided to the customer only once for the Initial Prehearing Conference and “not also again for the [expungement] hearing.”

Customer attendance and participation in expungement hearings help the panel fully develop a record on which to decide the expungement request. Accordingly, the Proposal would require the Director to notify all customers whose customer arbitrations, civil litigations or customer complaints are a subject of a straight-in request, of the time, date and place of any prehearing conferences and the expungement hearing.<sup>41</sup> Due to the importance of encouraging and facilitating customer attendance and participation in straight-in requests, FINRA declines to amend the Proposal as suggested by the commenter to limit how often the Director may notify customers of expungement hearings.

In addition, the Director would provide the notified customers with access to all documents that are relevant to the expungement request that are filed in (a) the arbitration requesting expungement relief and (b) any prior customer arbitration brought by the customer that is a subject of the expungement request.<sup>42</sup> This would provide the customer with access to the key documents surrounding the request for expungement prior to their attendance and participation in the expungement hearing. If a customer participates in the expungement hearing, the customer could introduce evidence, testify, call witnesses, state objections to evidence, cross-examine witnesses, and make opening and closing arguments if the panel allows any party to

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<sup>39</sup> Proposal, supra note 1, 87 FR 50170, 50181 (providing that “[t]he proposed time limits should help encourage customer attendance and participation in expungement proceedings and help ensure that straight-in requests are brought before relevant evidence and testimony becomes stale or unavailable.”).

<sup>40</sup> See proposed Rules 12805(c)(3)(A) and 13805(c)(3)(A).

<sup>41</sup> See proposed Rule 13805(b)(1)(B)(i). For a more detailed discussion on notifications to customers, see Proposal, supra note 1, 87 FR 50170, 50185.

<sup>42</sup> See proposed Rule 13805(b)(1)(B)(ii).

present such arguments.<sup>43</sup> However, as a non-party to the straight-in request, the customer would not be entitled to seek discovery from the parties through the DRS arbitration forum.<sup>44</sup>

#### **IV. Finding of Liability in Customer Arbitration**

As stated above, FINRA amended the Initial Filing to, among other things, provide that an associated person shall not file a claim requesting expungement of customer dispute information from the CRD system if the customer dispute information is associated with a customer arbitration or civil litigation in which a panel or court of competent jurisdiction previously found the associated person liable.<sup>45</sup> In the amendment, FINRA explained, in relevant part, that “[a]rbitration awards are final and binding unless vacated based on the limited grounds set forth in applicable state or federal statutes. Thus, if an associated person is found liable in a customer arbitration, FINRA considers the associated person legally bound by the award and the Director will decline the use of the [DRS] arbitration forum if the associated person then requests expungement of customer dispute information that is associated with the customer arbitration in which the associated person was found liable.”<sup>46</sup> As FINRA explained in the Response Letter, FINRA considers such expungement requests a collateral attack on the binding arbitration award, and a collateral attack is not contemplated under FINRA rules and is contrary to the Codes.<sup>47</sup> Furthermore, FINRA believes that prohibiting an associated person from filing such expungement requests would promote greater efficiency in the DRS arbitration forum because it would preclude requests that otherwise would be unsuccessful.

NASAA commented that it “believes that customer dispute information that forms the basis for a finding of liability in any setting should not be subject to expungement.”<sup>48</sup> NASAA suggested, therefore, that “[a]ssociated persons should [] be prevented from seeking expungement of customer dispute information that forms the basis for a finding of liability in all of the contexts in which such information forms part of a regulatory record, such as state regulatory proceedings, proceedings brought by the SEC, or self-regulatory proceedings.”

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<sup>43</sup> Proposal, supra note 1, 87 FR 50170, 50182–83.

<sup>44</sup> See also Proposal, supra note 1, 87 FR 50170, 50186 n.182 (providing that as a non-party to a straight-in request, an authorized representative of a state securities regulator would not be permitted to request discovery).

<sup>45</sup> See Response Letter, supra note 5, Section XII.B., “Finding of Liability in Customer Arbitration”; see also proposed Rule 13805(a)(2)(A)(iv).

<sup>46</sup> See Response Letter, supra note 5, Section XII.B., “Finding of Liability in Customer Arbitration.”

<sup>47</sup> See Response Letter, supra note 5, Section XII.B., “Finding of Liability in Customer Arbitration.”

<sup>48</sup> Emphasis added.

FINRA recognizes NASAA's concern. To address the concern, FINRA is proposing to further amend the Initial Filing to provide that an associated person shall not file a claim requesting expungement of customer dispute information from the CRD system against a member firm at which the person was associated at the time the customer dispute arose if the customer dispute information involves the same conduct that is the basis of a final regulatory action<sup>49</sup> taken by a securities regulator or self-regulatory organization.<sup>50</sup> If an associated person requests expungement of such customer dispute information, the Director will deny the DRS arbitration forum to the expungement request.<sup>51</sup> However, if an associated person is successful at appealing a final regulatory action, the associated person may file a claim requesting expungement of the customer dispute information involving the same conduct that is the basis of the final regulatory action, provided that the request is not otherwise ineligible for arbitration, including time barred.<sup>52</sup>

In addition, FINRA notes that it will continue to emphasize in its expungement training, including the enhanced expungement training under the Proposal, that an essential part of the arbitrator's role when determining whether expungement is appropriate is to consider the expungement request in the context of the associated person's entire securities industry record.<sup>53</sup>

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<sup>49</sup> A "final regulatory action" includes any final action, including any action that is on appeal, by a securities regulator or self-regulatory organization. See Rule 8312(c); see also Regulatory Notice 09-66 (November 2009) (noting that "actions that are delineated in current Form U4 Questions 14C, 14D or 14E will be considered 'final regulatory actions.' Similarly, actions that are detailed in current Form U5 Question 7D, and have a status of 'final' or 'on appeal,' will be considered 'final regulatory actions' as such actions are also addressed in Form U4."). For example, a Letter of Acceptance, Waiver, and Consent and an accepted Offer of Settlement are two examples, among others, of final regulatory actions taken by FINRA. See Rules 9216(a)(4) and 9270(g). A "final regulatory action" may also include a final action reported by a regulator on Form U6. See Regulatory Notice 09-66 (November 2009).

<sup>50</sup> See proposed Rule 13805(a)(2)(A)(v).

<sup>51</sup> See proposed Rule 13203(b).

<sup>52</sup> For purposes of this proposed rule, a "final regulatory action" would not include a final action by a securities regulator or self-regulatory organization that is dismissed, vacated or withdrawn. If, after dismissal, vacatur, or withdrawal of the final regulatory action, the associated person's expungement request in the DRS arbitration forum would be ineligible pursuant to Rule 13805(a)(2), including time barred, the associated person could seek a court order directing expungement of the customer dispute information.

<sup>53</sup> See Guidance, supra note 4 (suggesting that "[a]rbitrators should carefully review the [BrokerCheck] report when considering whether expungement is appropriate" and

An associated person's securities industry record may include disclosure events related to regulatory actions, investigations, criminal matters, and any other registration information that might be relevant to the expungement request.

**V. Required Finding to Issue an Award Containing Expungement Relief**

The Proposal would make changes to Rules 12805 and 13805 to provide that “in order to issue an award containing expungement relief,” a panel must unanimously find “that one or more of the grounds for expungement enumerated in the [Proposal] has been established: (1) the claim, allegation or information is factually impossible or clearly erroneous; (2) the associated person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation or conversion of funds; or (3) the claim, allegation or information is false.”<sup>54</sup> In addition, the Proposal would direct that “the panel shall not issue, and the Director shall not serve, an award containing expungement relief based on any other grounds.”<sup>55</sup>

SIFMA's most recent comment letter restated its position “that the current grounds for granting expungement under FINRA rules are [not] strictly limited to the three grounds listed in Rule 2080(b)(1) (i.e., error, mistake or falsity), and [should] also include the grounds listed in Rule 2080(b)(2). . . .”<sup>56</sup> SIFMA suggested that “Rule 2080(b)(2) provides a catch-all, equitable ground for granting expungement, where the relief sought is meritorious, and where granting expungement would have no material adverse effect on investor protection, CRD integrity, or regulatory requirements.” SIFMA also stated that “FINRA offers no cost-benefit analysis or other principled reason why the grounds for expungement should be strictly limited to the Rule 2080(b)(1) grounds . . . .” SIFMA added that, with the Proposal, “FINRA seeks to circumvent the proper rulemaking process” without “provid[ing] notice, or even acknowledg[ing], that it is proposing a significant rule change to limit the expungement grounds to Rule 2080(b)(1) . . . .”

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“should pay particular attention to the ‘Disclosure Events’ section of the [BrokerCheck] report.”).

<sup>54</sup> Proposal, supra note 1, 87 FR 50170, 50184.

<sup>55</sup> See supra note 54. At any stage of an arbitration proceeding, the Director has the authority to decline the use of the DRS arbitration forum under Rules 12203 and 13203.

<sup>56</sup> See also Del Toro (arguing that “[e]xpungement awards based solely on Rule 2080(b)(2) are rare, but they are nevertheless allowed under the current rules . . . .”).

SIFMA concluded that the Proposal is inconsistent with Sections 19(b)(1)<sup>57</sup> and 15A(b)(6)<sup>58</sup> of the SEA.<sup>59</sup>

FINRA considered and responded to similar comments previously raised by SIFMA on the Initial Filing and, therefore, incorporates those responses herein.<sup>60</sup> FINRA continues to disagree with SIFMA that “Rule 2080(b)(2) provides a catch-all, equitable ground for granting expungement, where the relief sought is meritorious, and where granting expungement would have no material adverse effect on investor protection, CRD integrity, or regulatory requirements.”

Notwithstanding FINRA’s disagreement with SIFMA regarding the current application of Rule 2080(b)(2), in the Proposal, FINRA has determined to amend Rules 12805 and 13805 to codify in those Rules the grounds identified in Rule 2080(b)(1) as the exclusive grounds upon which an arbitration panel may issue an award containing expungement of customer dispute information from the CRD system. If the SEC approves the Proposal, this codification would resolve any potential confusion regarding the applicability of Rule 2080(b)(2) as an appropriate ground upon which arbitrators may issue awards containing expungement relief. Specifically, the Proposal would provide that “[i]n order to issue an award containing expungement relief, the panel must find unanimously that one or more of the following grounds for expungement has been established: 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.” In addition, the Proposal would direct that “[t]he panel shall not issue, and the Director shall not serve, an award containing expungement relief based on grounds other than those specified in [this Rule].” Thus, if the SEC approves the Proposal, arbitrators would no longer look to Rule 2080 to identify the grounds that provide a basis for issuing an award containing expungement relief. Instead, arbitrators would be required to issue an award containing expungement relief only on the grounds specified in proposed Rules 12805(c)(8)(A)(i) or 13805(c)(9)(A)(i).

FINRA believes that amending Rules 12805 and 13805 to codify the three narrow grounds in Rule 2080(b)(1) as the only grounds on which arbitrators may determine to award expungement relief best aligns with FINRA’s position that its expungement framework should allow for the removal of customer dispute information from the CRD system only in extraordinary circumstances in accordance with FINRA’s rules. These three narrow grounds

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<sup>57</sup> 15 U.S.C. 78s(b)(1).

<sup>58</sup> 15 U.S.C. 78o(b)(6).

<sup>59</sup> See also Del Toro (suggesting that “some of the Proposal[’]s changes result in the indirect abrogation of FINRA Rule 2080(b)(2) through a procedural rule change”).

<sup>60</sup> See Response Letter, supra note 5, Section VI., “Required Finding to Issue an Award Containing Expungement Relief.”



fairly address the circumstances in which an associated person would appropriately seek expungement of customer dispute information in the DRS arbitration forum.<sup>61</sup> In addition, allowing expungement only in these narrow circumstances would continue to balance the competing interests of providing regulators with broad access to information about customer disputes to fulfill their regulatory obligations, providing a fair process that recognizes an associated person's interest in protecting their reputation, and ensuring investors have access to accurate information about associated persons with whom they may decide to do business. This Proposal would help further protect the integrity and accuracy of the information in the CRD system, which is essential to FINRA's mission of investor protection.

Moreover, contrary to SIFMA's assertion, FINRA has undertaken an economic impact assessment to analyze the regulatory need for the Proposal, its potential economic impacts, including anticipated costs, benefits and distributional and competitive effects, relative to the current baseline, and the alternatives FINRA considered in assessing how best to meet FINRA's regulatory objectives.<sup>62</sup>

Furthermore, with the Proposal, FINRA has provided notice and the opportunity for public comment of its intent to amend Rules 12805 and 13805 to codify the exclusive grounds upon which an arbitration panel may issue an award containing expungement of customer dispute information from the CRD system. This notice and comment rulemaking is evidenced by publication of the Proposal explaining the reasons for the Proposal,<sup>63</sup> SIFMA's comment letters in response to the Proposal,<sup>64</sup> and FINRA's consideration of and responses to SIFMA's comments.<sup>65</sup> FINRA appreciates this opportunity to engage with SIFMA and other interested parties through this notice and comment rulemaking, but declines to modify the Proposal as suggested by the commenters. As discussed in detail in the Proposal, the Response Letter and herein, FINRA believes these proposed amendments to Rules 12805 and 13805 are necessary to address concerns identified with the current expungement process, and are designed, in general, to protect investors and the public interest.

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<sup>61</sup> See Regulatory Notice 08-79 (December 2008).

<sup>62</sup> See Proposal, supra note 1, 87 FR 50170, 50189–98.

<sup>63</sup> Proposal, supra note 1, 87 FR 50170, 50184 (explaining that the Proposal is intended to “further protect the integrity of the information in the CRD system”); see also 15 U.S.C. 78s(b)(1) and 17 CFR 240.19b-4.

<sup>64</sup> See SIFMA, supra note 7; see also letter from Kevin M. Carroll, Managing Director and Associate General Counsel, SIFMA, to Vanessa A. Countryman, Secretary, SEC, dated September 2, 2022; and Del Toro, supra note 59.

<sup>65</sup> See Response Letter, supra note 5, Section VI., “Required Finding to Issue an Award Containing Expungement Relief.”

## **VI. Additional Comments**

### **A. Disclosures Reported on the Uniform Registration Forms**

Grebenik restated concerns about the threshold for reporting customer dispute information to the CRD system. In addition, Del Toro suggested that the “allegation-based” reporting system “correlates with a) the large number of erroneously reported claims . . . and b) the high incidence of meritless claims.”

As FINRA explained in its Response Letter, the Proposal is focused on the expungement of customer dispute information from the CRD system – not on the information that must be reported on the Uniform Registration Forms.<sup>66</sup> Thus, FINRA declines to amend the Proposal as suggested.

### **B. Arbitrator Review of Customer Dispute Information**

Wagner suggests that the Proposal should include a provision requiring arbitrators to review customer dispute information in the CRD system to “adjudge and determine its adequacy to succinctly convey the substantive” claim, allegation or information contained in a statement of claim, as it may be amended at two milestones in the case: (1) when an arbitrator is assigned to a case; and (2) when arbitrators are deciding expungement of customer dispute information related to the Statement of Claim.

FINRA believes this comment is outside the scope of the Proposal. However, FINRA notes that arbitrators do not have the authority to amend a statement of claim at any point during an arbitration, and FINRA has no plans to revise its rules to grant arbitrators such authority.

## **Conclusion**

FINRA is committed to further strengthening the current expungement process so that it works as intended—as a remedy that is appropriate only in extraordinary circumstances and in accordance with the narrow standards in FINRA rules. FINRA believes the Proposal will help achieve this goal. Further, FINRA believes the Proposal will help maintain and protect the integrity and accuracy of the information in the CRD system, which are essential to FINRA’s mission of investor protection.

If the SEC approves the Proposal, and as FINRA gains experience with the expungement process as revised by the Proposal, FINRA will continue to evaluate whether there are other ways to further strengthen the current expungement process, including whether

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<sup>66</sup> See Response Letter, supra note 5, Section XVI.C., “Data Reported on Uniform Registration Forms.” In addition, FINRA notes that Forms U4 and U5 were developed by FINRA, NASAA and state securities regulators. Any amendments to these forms would require collaboration with, and agreement among FINRA, NASAA and state securities regulators before being filed with the SEC for approval. Id.

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a panel from the Special Arbitrator Roster should be required to decide an expungement request in simplified arbitrations, whether to allow state securities regulators to attend and participate in separate expungement-only hearings in simplified arbitrations, and whether to require that a panel find that the evidence presented in support of an expungement request meets a clear and convincing standard of proof in order to issue an award containing expungement relief.<sup>67</sup> In addition, FINRA intends to provide information on its website regarding expungement requests. FINRA also welcomes continued engagement with interested parties on expungement, including on potential alternative frameworks to the current expungement process.

FINRA believes that the foregoing responds to the material issues raised by the commenters on the Proposal and that the Proposal should be approved.

\* \* \* \*

If you have any questions, please contact me on [REDACTED], email:

[REDACTED].

Very truly yours,

/s/ Mignon McLemore

Mignon McLemore  
Associate General Counsel  
Office of General Counsel

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<sup>67</sup> As discussed in the Response Letter, FINRA believes that the Proposal makes adopting a clear and convincing standard of proof unnecessary at this time. See Response Letter, supra note 5, Section VII., “Other Standards to Decide Expungement.”