

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-88251; File No. SR-FINRA-2020-005)

February 20, 2020

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; 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

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on February 7, 2020, Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FINRA. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

FINRA is proposing 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 requests for expungement of customer dispute information. The proposed rule change would amend Part IX (Fees and Awards) of the Codes to apply minimum filing fees to requests for expungement of customer dispute information, whether the request is made as part of the customer arbitration or the associated person files an expungement request in a separate

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

<sup>2</sup> 17 CFR 240.19b-4.

arbitration (“straight-in request”).<sup>3</sup> The proposed rule change would also apply a minimum process fee and member surcharge to straight-in requests, as well as a minimum hearing session fee to expungement-only hearings.

The text of the proposed rule change is available on FINRA’s website at <http://www.finra.org>, at the principal office of FINRA and at the Commission’s Public Reference Room.

II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, FINRA included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

(a) Background and Discussion

I. Customer Dispute Information in the Central Registration

Depository

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<sup>3</sup> FINRA is separately developing other changes to the current expungement framework, including codifying as rules the Notice to Arbitrators and Parties on Expanded Expungement Guidance (“Guidance”), see <https://www.finra.org/arbitration-mediation/notice-arbitrators-and-parties-expanded-expungement-guidance>, and establishing a roster of arbitrators with additional training and experience from which a panel would be selected to decide straight-in requests and expungement requests in settled customer arbitrations. See Regulatory Notice 17-42 (December 2017).

Information regarding customer disputes involving associated persons is contained in the Central Registration Depository (“CRD<sup>®</sup>”) system, the central licensing and registration system used by the U.S. securities industry and its regulators.<sup>4</sup> FINRA operates the CRD system pursuant to policies developed jointly with NASAA. FINRA works with the SEC, NASAA, and other members of the regulatory community to ensure that information submitted and maintained in the CRD system is accurate and complete.

In general, the information in the CRD system is submitted by registered securities firms, brokers and regulatory authorities in response to questions on the uniform registration forms.<sup>5</sup> Among other things, these forms collect administrative, regulatory, criminal history, and disciplinary information about brokers, including customer complaints, arbitration claims and court filings made by customers (i.e., “customer dispute information”). FINRA, state and other regulators use this information in connection with their licensing and regulatory activities, and member firms use this information to help them make informed employment decisions.

Pursuant to rules approved by the SEC, FINRA makes specified current CRD information publicly available through BrokerCheck<sup>®</sup>.<sup>6</sup> BrokerCheck is part of FINRA’s

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<sup>4</sup> The concept for CRD was developed by FINRA jointly with the North American Securities Administrators Association (“NASAA”), and NASAA and state regulators play a critical role in its ongoing development and implementation.

<sup>5</sup> The uniform registration forms are Form BD (Uniform Application for Broker-Dealer Registration), Form BDW (Uniform Request for Broker-Dealer Withdrawal), Form BR (Uniform Branch Office Registration Form), Form U4 (Uniform Application for Securities Industry Registration or Transfer), Form U5 (Uniform Termination Notice for Securities Industry Registration), and Form U6 (Uniform Disciplinary Action Reporting Form).

<sup>6</sup> There is a limited amount of information in the CRD system that FINRA does not display in BrokerCheck, including personal or confidential information. A

ongoing effort to help investors make informed choices about the brokers and broker-dealer firms with which they may conduct business. BrokerCheck maintains information on the approximately 3,600 registered broker-dealer firms and 628,000 registered brokers. BrokerCheck also provides the public with access to information about formerly registered broker-dealer firms and brokers.<sup>7</sup> In 2019 alone, BrokerCheck helped users conduct more than 40 million searches of firms and brokers.

The regulatory framework governing the CRD system and BrokerCheck has long contemplated the possibility of expunging certain customer dispute information from these systems in limited circumstances, such as where the allegations made about the broker are factually impossible or clearly erroneous. The expungement framework seeks to balance the important benefits of disclosing information about customer disputes to regulators and investors with the goal of protecting brokers from the publication of false allegations against them.

A broker can seek expungement of customer dispute information by going through the FINRA arbitration process or directly to court (without first going through arbitration). Regardless of whether expungement of customer dispute information is sought directly through a court or through arbitration, FINRA Rule 2080 (Obtaining an

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detailed description of the information made available through BrokerCheck is available at <http://www.finra.org/investors/about-brokercheck>.

<sup>7</sup> Formerly registered brokers, although no longer in the securities industry in a registered capacity, may work in other investment-related industries or may seek to attain other positions of trust with potential investors. BrokerCheck provides information on more than 16,800 formerly registered broker-dealer firms and 567,000 formerly registered brokers. Broker records are available in BrokerCheck for 10 years after a broker leaves the industry, and brokers who are the subject of disciplinary actions and certain other events remain on BrokerCheck permanently.

Order of Expungement of Customer Dispute Information from the Central Registration Depository (CRD) System), which was developed in close consultation with representatives of NASAA and state regulators, requires a broker-dealer firm or broker seeking expungement to obtain an order of a court of competent jurisdiction directing such expungement or confirming an award containing expungement relief. FINRA will expunge customer dispute information only after the court orders it to execute the expungement.<sup>8</sup>

## II. Current Fee Structure in FINRA Arbitration

Under the Codes, if a customer files a claim in arbitration against an associated person and a firm, the customer is assessed a filing fee based on the claim amount.<sup>9</sup> The firm is assessed a member surcharge and a process fee based on the claim amount.<sup>10</sup> The

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<sup>8</sup> FINRA Rule 2080 also requires that firms and brokers seeking a court order or confirmation of the arbitration award containing expungement relief name FINRA as a party, and FINRA will challenge the request in court in appropriate circumstances. FINRA may, however, waive the requirement to name it as a party if it determines that the award containing expungement relief is based on affirmative judicial or arbitral findings that: (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. In addition, FINRA has sole discretion “under extraordinary circumstances” to waive the requirement if the request for expungement relief and accompanying award are meritorious and expungement would not have a material adverse effect on investor protection, the integrity of the CRD system, or regulatory requirements. See FINRA Rule 2080.

<sup>9</sup> Customers, associated persons, and other non-members who file a claim, counterclaim, cross claim or third party claim must pay a filing fee. See FINRA Rule 12900(a)(1); see also FINRA Rule 13900(a)(1).

<sup>10</sup> A member surcharge is assessed against a member if, for example, the member files an arbitration claim, is named as a respondent in a claim, or employed, at the time the dispute arose, an associated person who is named as a respondent; the amount of the surcharge is based on the amount of the claim. See FINRA Rules

member is assessed only one surcharge and one process fee per arbitration.<sup>11</sup> When the associated person answers the claim,<sup>12</sup> the associated person is not assessed a fee if he or she does not add a claim to the answer.<sup>13</sup>

If the parties do not settle the arbitration, the panel will hold at least one hearing to decide the customer arbitration and, at the conclusion of the hearing(s), issue an award. In the award, the panel will allocate the fees incurred by the parties during the arbitration, including each party's portion of the hearing session fees,<sup>14</sup> which are also based on the amount of the customer's claim.<sup>15</sup> If the parties settle, the panel will not issue an award.

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12901(a)(1)(B) and 12901(a)(1)(C) and FINRA Rules 13901(a)(2) and 13901(a)(3).

Further, each member that is a party to an arbitration claim in which more than \$25,000 is in dispute, or that is non-monetary or not specified, is required to pay a process fee based on the amount or nature of the claim. If an associated person of a member is a party, the member that employed the associated person at the time the dispute arose is charged the process fee. See FINRA Rules 12903(a) and (b) and FINRA Rules 13903(a) and (b).

<sup>11</sup> Under the Codes, no member is assessed more than a single surcharge or process fee in any arbitration. See FINRA Rules 12901(a)(4) and 12903(b) and FINRA Rules 13901(d) and 13903(b).

<sup>12</sup> The respondent must answer the statement of claim within 45 days and may include other claims and remedies requested. See FINRA Rules 12303(a) and (b) and FINRA Rules 13303(a) and (b).

<sup>13</sup> For example, an associated person is permitted to file a claim against the claimant requesting relief. Such counterclaim would require the associated person to pay a filing fee. See FINRA Rule 12303(d); see also FINRA Rule 13303(d).

<sup>14</sup> Parties are charged hearing session fees for each hearing session, based on the customer's claim amount. In the award, the panel determines the amount of each hearing session fee that each party is required to pay. See FINRA Rules 12902 and 13902.

<sup>15</sup> FINRA makes all arbitration awards publicly available. See <https://www.finra.org/arbitration-mediation/arbitration-awards>.

(i) Current Fee Structure for Expungement Requests Made during a Customer Arbitration

Currently, even if the associated person's answer to a customer's claim includes a request for expungement, the associated person is not assessed a filing fee. The member, having been assessed the surcharge and process fee for the customer arbitration, will not incur additional charges because of the expungement request. If the customer's claim closes by award after a hearing,<sup>16</sup> the panel will decide the customer's claim and the expungement request (assuming the associated person pursues the request during the arbitration), and allocate the hearing session fees among the parties.

If the customer arbitration does not close by award after a hearing (e.g., settles) and the associated person or requesting party, if it is an on-behalf-of request, continues to pursue the expungement request, the panel from the customer arbitration will hold a separate expungement-only hearing to decide the expungement request.<sup>17</sup> The hearing session fee for the expungement-only hearing will be based on the amount of the

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<sup>16</sup> The term "hearing" means the hearing on the merits of an arbitration under Rule 12600. See FINRA Rule 12100(o).

<sup>17</sup> In 2009, the SEC approved amendments to Forms U4 and U5 to require, among other things, the reporting of allegations of sales practice violations made against unnamed persons. See Securities Exchange Act Release No. 59916 (May 13, 2009), 74 FR 23750 (May 20, 2009) (Order Approving SR-FINRA-2009-008). Specifically, Forms U4 and U5 were amended to add questions to elicit whether the applicant or registered person, though not named as a respondent or defendant in a customer-initiated arbitration, was either mentioned in or could be reasonably identified from the body of the arbitration claim as a registered person who was involved in one or more of the alleged sales practice violations. A party (typically, the firm) named in a customer arbitration may request expungement on-behalf-of an associated person who is a subject of, but not named in, the arbitration. Such on-behalf-of requests occur in customer-initiated arbitrations only.

customer's claim. Under the Codes, fees for hearing sessions held solely to decide an expungement request must be charged to the party or parties requesting expungement.<sup>18</sup>

(ii) Current Fee Structure for a Straight-In Request

An associated person may request expungement by filing a straight-in request rather than requesting expungement during a customer arbitration. The straight-in request may be filed against a former or current firm or the customer.<sup>19</sup> A claim that does not request a dollar amount is considered a non-monetary or not specified claim (“non-monetary claim”) under the Codes. An expungement request is a non-monetary claim; thus, under the Codes, the associated person must pay a \$1,575 filing fee, and the member named as a respondent or that employed the associated person at the time the dispute arose must pay a \$3,750 process fee.<sup>20</sup> A member named as a respondent or that employed the associated person at the time the dispute arose would also be assessed a surcharge of \$1,900.<sup>21</sup> These claims are decided by a three-person panel, unless the parties agree in writing to one arbitrator.<sup>22</sup> Further, the per-hearing session fee for a non-monetary claim is \$1,125.

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<sup>18</sup> See FINRA Rules 12805(d) and 13805(d).

<sup>19</sup> FINRA notes, however, that straight-in requests filed against the customer are rare.

<sup>20</sup> See supra note 10. Some associated persons have independent contractor, rather than employment, relationships with their firms. In these circumstances, FINRA assesses applicable member surcharge or process fees against the firm at which the associated person was associated at the time the dispute arose.

<sup>21</sup> See supra note 10; see also supra note 11.

<sup>22</sup> See FINRA Rules 12401(c) and 13401(c).

(iii) Concerns with Avoidance of the Current Fee Structure for Expungement Requests

As discussed above, an expungement request is a non-monetary claim and parties requesting expungement should pay the fees associated with such requests under the Codes. FINRA is concerned about practices to avoid fees applicable to expungement requests, particularly straight-in requests. For example, FINRA is aware that associated persons who file a straight-in request often add a small monetary claim (typically, one dollar) to the expungement request to reduce the fees assessed against the associated person and qualify for an arbitration heard by a single arbitrator.<sup>23</sup> Further, the small damages claim reduces the member fees that the forum assesses firms when an arbitration claim is filed. Thus, adding a claim for one dollar in a straight-in request against a member firm reduces the fees assessed to the associated person requesting expungement and member firm from \$9,475 to \$300.<sup>24</sup> Often, the associated person will subsequently drop the claim for one dollar.

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<sup>23</sup> Whether the claimant specifies damages, and the amount specified, determines the fees assessed in arbitration cases and whether a single arbitrator or a three-person panel will decide the case. See FINRA Rules 12401 and 13401. If the amount of the claim is \$50,000 or less, exclusive of interest and expenses, the panel will consist of one arbitrator and the claim is subject to the simplified arbitration procedures under Rule 12800. If the amount of the claim is more than \$50,000, but less than \$100,000, exclusive of interest and expenses, the panel will consist of one arbitrator unless the parties agree in writing to three arbitrators. If the amount of a claim is more than \$100,000, exclusive of interest and expenses, or is non-monetary, or if the claim does not request money damages, the panel will consist of three arbitrators, unless the parties agree in writing to one arbitrator.

<sup>24</sup> If an associated person files a straight-in request against a member firm, does not add a monetary claim, and assuming one prehearing conference and one hearing session on the merits, the associated person is assessed a filing fee of \$1,575 and a hearing session fee of \$2,250 (\$1,125 for the prehearing conference and \$1,125 for the hearing session on the merits). In addition, the respondent member firm is assessed a member surcharge of \$1,900 and a process fee of \$3,750. If the

Adding a small damages claim also changes the panel composition such that the straight-in request is heard by a single arbitrator rather than a three-person panel.<sup>25</sup> FINRA believes that most expungement requests should be decided by a three-person panel. Expungement requests may be complex to resolve, particularly straight-in requests where customers typically do not participate in the expungement hearing. Thus, having three arbitrators available to ask questions and request evidence would help ensure that a complete factual record is developed to support the arbitrators' decision at such expungement hearings.

To help ensure that parties requesting expungement pay the fees intended for such requests under the Codes, that the fees charged when expungement is requested are more consistent, and that more expungement requests are heard by a three-person panel, FINRA is proposing to amend the Codes to apply a minimum filing fee for all expungement requests, irrespective of whether the request is made as part of the customer arbitration or the associated person files a straight-in request, or the requesting party adds a small damages claim. The proposed rule change would also apply a minimum process fee and member surcharge to straight-in requests, as well as a minimum hearing session

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associated person adds a one dollar claim to the request, assuming one prehearing conference and one hearing session on the merits, the associated person is assessed a filing fee of \$50 and a hearing session fee of \$100 (\$50 for the prehearing conference and \$50 for the hearing session on the merits). The member firm is also assessed a member surcharge of \$150 but no process fee. See also *infra* Item II.B. (discussing the economic impacts of the proposed rule change).

<sup>25</sup> See *supra* note 23.

fee to expungement-only hearings held after a customer arbitration<sup>26</sup> or in connection with a straight-in request.<sup>27</sup>

(b) Proposed Amendments

I. Proposed Filing Fee

Under the proposed rule change, an associated person, or requesting party if it is an on-behalf-of request,<sup>28</sup> would be required to pay the filing fee for a non-monetary claim for an expungement request made during a customer arbitration<sup>29</sup> or filed as a straight-in request.<sup>30</sup> If the associated person or requesting party adds a monetary claim

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<sup>26</sup> For example, under the current expungement process, if the customer arbitration settles, but an associated person seeks to pursue a request for expungement made during the customer arbitration, the panel from the customer arbitration will hold a separate expungement-only hearing to decide the expungement request and issue an award setting forth its decision on the expungement request. Under the proposed rule change, the associated person requesting expungement would be required to pay the minimum hearing session fee for this separate expungement-only hearing.

<sup>27</sup> The proposed rule change would apply to all members, including members that are funding portals or have elected to be treated as capital acquisition brokers (“CABs”), given that the funding portal and CAB rule sets incorporate the impacted FINRA rules by reference.

<sup>28</sup> See supra note 17.

<sup>29</sup> Under the proposed rule change, an associated person who requests expungement of customer dispute information during an industry arbitration would also be required to pay the filing fee for a non-monetary claim. However, these requests are rare.

<sup>30</sup> If the requesting party chooses to seek expungement in the customer arbitration, but later determines not to pursue the request and then files a straight-in request for expungement of the same customer dispute information, the requesting party would be required to pay the filing fee applicable to the straight-in request, notwithstanding previous payment of the filing fee applicable to the expungement request during the customer arbitration.

to the expungement request, the filing fee would be the fee for a non-monetary claim or the applicable filing fee based on the claim amount, whichever is greater.<sup>31</sup>

As discussed above, under the Codes, an expungement request that does not include a claim for damages is a non-monetary claim that is currently assessed a \$1,575 filing fee and triggers a three-person panel. FINRA believes that all parties requesting expungement should pay the same minimum filing fee, and that parties should not be able to avoid the fee (or a three-person panel) simply by adding a small claim amount.

Accordingly, FINRA is proposing that the filing fee for non-monetary claims would be the minimum filing fee for all expungement requests, and that the minimum filing fee would apply to expungement requests in customer arbitrations as well as to straight-in requests.<sup>32</sup> A request for expungement is a claim that a party is requesting the arbitrators to decide. Under the Codes, if a party files a claim or adds a claim in an answer to a statement of claim, the respondent must pay all required filing fees.<sup>33</sup> As an expungement request is also a claim, the party requesting this relief should also pay a filing fee.

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<sup>31</sup> See proposed Rules 12900(a)(3) and 13900(a)(3). An associated person could add a monetary or non-monetary claim to the expungement request. FINRA notes, however, that it is rare that significant dollar claims accompany expungement requests.

<sup>32</sup> Under the Codes, the Director may defer payment of all or part of an associated person's filing fee on a showing of financial hardship. See FINRA Rules 12900(a)(1) and 13900(a)(1). The proposed rule change would make clear this provision applies to expungement requests. Information on how to request an arbitration fee waiver is available at <https://www.finra.org/arbitration-mediation/arbitration-fee-waivers>. In addition, in the award, the panel may order a party to reimburse another party for all or part of any filing fee paid. See FINRA Rules 12900(d) and 13900(d).

<sup>33</sup> See FINRA Rules 12303(d) and 13303(d).

The proposed minimum filing fee is also commensurate with the additional steps that arbitrators should take when deciding an expungement request during a customer arbitration or in connection with a straight-in request. Regardless of whether expungement is decided during a customer arbitration or separately, FINRA Rules 12805 and 13805 require the panel to hold one or more recorded hearing sessions regarding the appropriateness of expungement, to review settlement documents and consider the amount of payments made to any party and any other terms and conditions of the settlement, and to make a determination as to whether any of the Rule 2080 grounds for expungement have been established. In addition, as described in the Guidance, arbitrators have a unique, distinct role when deciding whether to recommend a request to expunge customer dispute information from CRD. Accordingly, the Guidance directs arbitrators to ensure that they have all of the information necessary to make an informed and appropriate recommendation on expungement. The Guidance also directs arbitrators to request any documentary or other evidence they believe is relevant to the expungement request.

## II. Proposed Member Surcharge for Straight-in Requests

The proposed rule change would apply a minimum member surcharge when an associated person files a straight-in request against either a customer or a member firm.<sup>34</sup> Under the proposed rule change, if an associated person files a straight-in request against a member firm, that firm would be assessed the member surcharge for a non-monetary claim under the Industry Code (currently \$1,900).<sup>35</sup> The proposed member surcharge is

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<sup>34</sup> See supra note 10 (discussing the member surcharge under the Codes today).

<sup>35</sup> See proposed Rule 13901(c). If the associated person files the straight-in request against another associated person, each firm that employed the respondent

consistent with what a member firm should pay today for a straight-in request without an additional small monetary claim filed against a member firm.<sup>36</sup>

The proposed rule change would also provide that, for straight-in requests filed against a customer, each member that employed the associated person at the time the customer dispute arose would be assessed the member surcharge for a non-monetary claim under the Customer Code (currently \$1,900).<sup>37</sup>

If the associated person adds a separate claim for damages to the straight-in request against the customer or member firm, the member surcharge would be the non-monetary member surcharge or the applicable surcharge under the Codes, whichever is greater. Under the proposal, the surcharge would be due when the Director serves the Claim Notification Letter or the initial statement of claim under the Codes.<sup>38</sup>

### III. Proposed Hearing Session Fees

The proposed rule change would apply the hearing session fee for a non-monetary claim heard by three arbitrators to each hearing session in which the sole topic is the determination of a request for expungement relief.<sup>39</sup> Thus, the proposed hearing session

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associated person at the time the dispute arose would be assessed the member surcharge for a non-monetary claim under the Industry Code. See FINRA Rule 13901(a)(3) and proposed Rule 13901(c).

<sup>36</sup> Consistent with how the member surcharge is assessed today, under the proposal, FINRA would not assess a member more than a single surcharge in any arbitration. See also supra note 11.

<sup>37</sup> See proposed Rule 12901(a)(3).

<sup>38</sup> See proposed Rules 12901(a)(5) and 13901(e).

<sup>39</sup> FINRA notes that the proposed \$1,125 hearing session fee for expungement hearings would apply if a party requests expungement as part of a Simplified Arbitration and no hearings are held to decide the underlying customer claim,

fee would apply when a customer arbitration does not close by award after a hearing (e.g., settles) and there is a separate hearing session held after the customer arbitration to decide an expungement request that was made during the customer arbitration, and to straight-in requests.<sup>40</sup> If the requesting party adds a monetary claim to the expungement request, the hearing session fee would be the greater of the fee for a non-monetary claim with three arbitrators or the applicable hearing session fee under the Codes based on the claim amount.<sup>41</sup> In addition, consistent with the Codes today, the hearing session fee would be assessed against the party requesting expungement.<sup>42</sup>

#### IV. Proposed Process Fees for Straight-in Requests

The proposed rule change would apply a minimum process fee when an associated person files a straight-in request against either a customer or member firm. Under the proposed rule change, if an associated person files a straight-in request against a member firm, that firm would be assessed the process fee for a non-monetary claim under the Industry Code (currently \$3,750).<sup>43</sup>

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regardless of whether a single arbitrator or a panel hears the Simplified Arbitration.

<sup>40</sup> See proposed Rules 12900(a)(3) and 13900(a)(3); see also supra note 26. If an associated person requests expungement during a customer arbitration, the customer arbitration closes by award after a hearing, and the arbitrator or panel decides the expungement request during the customer arbitration, the hearing session fee would be based on the amount of the customer's claim.

<sup>41</sup> See proposed Rules 12902(a)(5) and 13902(a)(4).

<sup>42</sup> See proposed Rules 12902(a)(5) and 13902(a)(4).

<sup>43</sup> See proposed Rule 13903(c). If the associated person files the straight-in request against another associated person, the firm that employed the respondent associated person at the time the dispute arose would be assessed the process fee

The proposed rule change would also clarify that, for straight-in requests filed against a customer, the member that employed the associated person at the time the customer dispute arose would be assessed the process fee for a non-monetary claim under the Customer Code (currently \$3,750).<sup>44</sup>

If the associated person adds a separate claim for damages to the straight-in request against the customer or member firm, the process fee would be the non-monetary process fee or the applicable process fee under the Codes, whichever is greater.<sup>45</sup> The proposed process fee is consistent with what member firms should pay today for straight-in requests without an additional small monetary claim filed against a customer or member firm.

FINRA will announce the effective date of the proposed rule change in a Regulatory Notice to be published no later than 60 days following Commission approval. The effective date will be no later than 60 days following publication of the Regulatory Notice announcing Commission approval of the proposed rule change.

## 2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>46</sup> which requires, among other things, that FINRA rules

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for a non-monetary claim under the Industry Code. See proposed Rules 13903(b) and 13903(c).

<sup>44</sup> See proposed Rule 12903(c).

<sup>45</sup> Consistent with how the process fee is assessed today, under the proposal, FINRA would not assess a member more than one process fee in any arbitration. See also supra note 11.

<sup>46</sup> 15 U.S.C. 78q-3(b)(6).

must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest, and Section 15A(b)(5) of the Act,<sup>47</sup> which requires, among other things, that FINRA rules provide for the equitable allocation of reasonable dues, fees and other charges among members and issuers and other persons using any facility or system that FINRA operates or controls.

The proposed rule change represents an equitable allocation of reasonable dues and fees against those who would either file or be a party to an expungement request, as is currently intended. As an expungement request is a separate relief request that an arbitrator or panel must consider and decide, the filing fees and related member and forum fees should reflect the general complexity of these requests, as well as the time and effort needed to administer, consider and decide them. In addition, the fees should apply consistently to all parties requesting expungement.

The proposed rule change will close gaps in the fee structure that have emerged in the existing expungement process, such as where parties add small dollar claims to their expungement requests to significantly lower the fees associated with expungement requests and to have expungement requests considered and decided by a single arbitrator rather than a three-person panel. The proposed rule change will help ensure that parties requesting expungement pay the fees intended for such requests under the Codes and that the fees charged when expungement is requested are more consistent, irrespective of whether the request is made as a straight-in request or during an arbitration, or whether damages are included in the request. The proposed rule change should also result in more

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<sup>47</sup> 15 U.S.C. 78q-3(b)(5).

expungement requests being heard by a three-person panel. A three-person panel will help ensure a complete factual record to support the arbitrators' decision, particularly in straight-in requests that often do not include customer participation and can be complex to resolve.

B. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

Economic Impact Assessment

FINRA has undertaken an economic impact assessment, as set forth below, to analyze the regulatory need for the proposed rule change, 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.

(a) Regulatory Need

FINRA is aware that parties requesting expungement are not always paying the fees intended for such requests under the Codes, particularly for straight-in requests. In addition, the current fee schedules under the Codes do not ensure that costs to the forum for administering expungement requests are being allocated to the party or parties requesting expungement and, as applicable, the member firms that employ them. The proposed rule change would help ensure that the fees for expungement requests are assessed, and that the costs borne by the forum to administer expungement requests are allocated, as intended, to those requesting expungement under the Codes.

(b) Economic Baseline

The economic baseline for the proposed rule change includes the provisions under the Codes that address the fees associated with expungement requests in FINRA arbitration. In general, the proposed rule change is expected to affect parties to an expungement request including associated persons and member firms. The proposed rule change may also affect other stakeholders of the forum, and users of customer dispute information contained in the CRD system and displayed through BrokerCheck.<sup>48</sup>

The customer dispute information contained in the CRD system is submitted by registered securities firms and regulatory authorities in response to questions on the uniform registration forms.<sup>49</sup> The information can be valuable to current and prospective customers to learn about the conduct of associated persons.<sup>50</sup> Current and prospective customers may not select or remain with an associated person or a member firm that employs an associated person with a record of customer disputes. Similarly, member

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<sup>48</sup> Other stakeholders of the forum include FINRA, other member firms, and other forum participants. Users of customer dispute information include investors; member firms and other companies in the financial services industry; individuals registered as brokers or seeking employment in the brokerage industry; and FINRA, states, and other regulators.

<sup>49</sup> See supra note 5 and accompanying text (discussing the uniform registration forms and the information contained in the CRD system). The information includes matters, which may or may not have been previously adjudicated in FINRA arbitration or a court of competent jurisdiction.

<sup>50</sup> Recent academic studies provide evidence that the past disciplinary and other regulatory events associated with a firm or individual can be predictive of similar future events. See Hammad Qureshi and Jonathan Sokobin, Do Investors Have Valuable Information About Brokers? FINRA Office of the Chief Economist Working Paper, (August 2015); see also Mark Egan, Gregor Matvos, and Amit Seru, The Market for Financial Adviser Misconduct, *Journal of Political Economy* 127, no. 1 (February 2019): 233-295.

firms and other companies in the financial services industry may use the information when making employment decisions.<sup>51</sup> In this manner, the customer dispute information contained in the CRD system (and displayed through BrokerCheck) may negatively affect the business and professional opportunities of associated persons but also provide for customer protections.

Any such negative impact on the business and professional opportunities of associated persons may be appropriate and consistent with investor protection, such as when the customer dispute information has merit. Any such negative impact may be inappropriate, however, such as when the customer dispute information is factually impossible, clearly erroneous, or false. Regardless of the merit, associated persons have incentive to remove customer dispute information from the CRD system and its public display through BrokerCheck.

An associated person or party on behalf of an associated person typically begins the process to remove customer dispute information from the CRD system by filing an expungement request in FINRA arbitration. FINRA is able to identify 5,732 expungement requests of customer dispute information filed from January 2016 through June 2019. More than one expungement request can be filed in a single arbitration, and multiple expungement requests may relate to the same customer complaint if the complaint relates to more than one associated person.

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<sup>51</sup> Customer dispute information submitted to the CRD system may have other uses. For example, associated persons may use information from the CRD system when deciding with whom to do business. FINRA, states, and other regulators also use the information to regulate brokers.

Under the Codes, a claim for expungement is considered a non-monetary claim, generally requiring fees in the middle of the range of potential fees that are assessed based on claim amount, and triggering a three-person panel. As described in more detail above and depending on the method that a party uses to request expungement, however, associated persons and member firms can be assessed fees less than what is intended for non-monetary claims.

Among the 5,732 expungement requests, 2,618 requests (46 percent) were filed during a customer or industry arbitration and 3,114 requests (54 percent) were filed as a straight-in request. The 2,618 expungement requests during a customer or industry arbitration include 2,604 requests during a customer arbitration and 14 requests during an industry arbitration; and the 3,114 straight-in requests include 3,048 requests filed solely against a member firm or against a member firm and a customer, and 66 requests filed solely against a customer. An associated person added a small monetary claim (of less than \$1,000) in 2,356 of the 3,114 straight-in requests (76 percent). In general, associated persons did not add a monetary claim for the remaining straight-in requests.

In general, parties filed an increasing number of expungement requests over the sample period. For example, parties filed 1,400 requests in 2016, 1,708 requests in 2017, 1,936 requests in 2018, and 688 requests in the first half of 2019. Similarly, the proportion of straight-in requests also increased over the sample period. For example, associated persons filed 328 straight-in requests in 2016 (23 percent of 1,400), 846 requests in 2017 (50 percent of 1,708), and 1,371 requests in 2018 (71 percent of 1,936). In the first half of 2019, associated persons filed 569 straight-in requests (83 percent of 688).

The proportion of the straight-in requests where the associated person added a small monetary claim (of less than \$1,000) has also increased over the sample period. For example, associated persons added a small monetary claim to 179 straight-in requests in 2016 (55 percent of 328), 569 requests in 2017 (67 percent of 846), 1,143 requests in 2018 (83 percent of 1,371), and 465 requests in the first half of 2019 (82 percent of 569). FINRA expects that absent this proposed rule change, associated persons who file straight-in requests will continue to add a small monetary claim to avoid the fees typically assessed for non-monetary claims.

(c) Economic Impact

The proposed rule change would apply the fees associated with non-monetary claims as minimum fees to expungement requests in FINRA arbitration. The fees associated with non-monetary claims are not new and would not change under the proposal. The fees would apply when parties file an expungement request during a customer arbitration, when parties file a rare expungement request during an industry arbitration, and when associated persons file a straight-in request.

Under the proposed rule change, a party that requests expungement during a customer or industry arbitration would be assessed a minimum filing fee of \$1,575. Currently, parties requesting expungement during a customer or industry arbitration are not assessed a filing fee in connection with the expungement request.

In addition, under the proposed rule change, if the arbitrator or panel holds a separate expungement-only hearing to decide the expungement request after the customer's arbitration, then the party that requested expungement would be assessed a

minimum hearing session fee of \$1,125.<sup>52</sup> The proposed minimum hearing session fee may be less than, equal to, or greater than the fees currently assessed for expungement-only hearings held after an arbitration. These current fees depend on the claim amount in the customer arbitration.<sup>53</sup>

If an associated person files a straight-in request against a member firm, assuming one prehearing conference and one hearing session on the merits, then under the proposed rule change, the associated person and a member firm would be assessed minimum fees totaling \$9,475. The associated person would be assessed a minimum filing fee of \$1,575 and a minimum hearing session fee of \$2,250 (\$1,125 for the prehearing conference and \$1,125 for the hearing session on the merits). In addition, the member firm would be assessed a minimum surcharge of \$1,900 and a minimum process fee of \$3,750.<sup>54</sup>

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<sup>52</sup> See supra note 26.

<sup>53</sup> From January 2016 through June 2019, 314 expungement-only hearings were held after an arbitration. In these instances, the assessed hearing session fee under the proposed rule change for an expungement-only hearing would have been less than (86 cases or 28 percent), equal to (155 cases or 49 percent), or greater than (73 cases or 23 percent) the fee assessed currently for an expungement-only hearing held after an arbitration, depending on the size of the initial claim. Assuming one expungement-only hearing session to consider and decide the expungement request, on average and under the proposed rule change, the party filing an expungement request would be assessed an additional hearing session fee of \$54 per arbitration. One expungement-only hearing session is consistent with the median number of hearing sessions (one) associated with the straight-in requests that were filed and closed during the sample period.

<sup>54</sup> The assumption of one prehearing conference and one hearing session on the merits is consistent with the median number of prehearing conferences (one) and hearing sessions on the merits (one) associated with straight-in requests that were filed and closed during the sample period. Also, the assumption that one member firm would be assessed a minimum surcharge and process fee is consistent with

In general, these fees are the same as those that are assessed today if the associated person does not add a small monetary claim to the straight-in request against a member firm. Associated persons and member firms, however, may incur significantly lower fees than what is intended for a straight-in request if the associated person adds a small monetary claim (of less than \$1,000) to the request. Assuming one prehearing conference and one hearing session on the merits, an associated person and the member firm would currently be assessed fees totaling \$300.<sup>55</sup>

The fees associated with a small claim procedure are intended to ensure that the forum is economically feasible for claimants with small claims,<sup>56</sup> and, in general, do not cover the specific costs to administer an expungement request, which requires a hearing session and typically involves a prehearing conference. For example, the costs to administer a straight-in request can include chairperson honoraria, travel expenses, conference room rental, and other costs to administer the forum. For the typical straight-

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the median number of member firms (one) that were assessed these fees in a straight-in request that was filed and closed during the sample period.

<sup>55</sup> For these requests, the associated person is assessed a filing fee of \$50 and a hearing session fee of \$100 (\$50 for the prehearing conference and \$50 for the hearing session on the merits). The member firm is also assessed a member surcharge fee of \$150 but no process fee. If instead the associated person files an expungement request solely against the customer, then the parties to the request are assessed fees totaling \$150. The associated person is still assessed a filing fee of \$50 and a hearing session fee of \$100, but the member firm is not assessed a member surcharge or a process fee.

<sup>56</sup> Under the Codes, arbitrations involving \$50,000 or less, exclusive of interest and expenses, will consist of one arbitrator and the claim is subject to the simplified arbitration procedures. Under these procedures, no hearing is held unless the customer or claimant requests a hearing, and the arbitrator renders an award based on the pleadings and other materials submitted by the parties. See FINRA Rules 12800 and 13800.

in request with one prehearing conference and one hearing session on the merits to consider and decide the request, the chairperson honoraria alone totals \$725;<sup>57</sup> yet as discussed above, if the associated person adds a small monetary claim (of less than \$1,000) to a straight-in request filed against a member firm, then the parties to the request are assessed fees totaling \$300.

The minimum fees that would be assessed under the proposed rule change reflect the application of the fee schedule as intended for a non-monetary claim. The proposed rule change would help ensure that costs to the forum for administering expungement requests are allocated as intended to the party or parties requesting expungement and, as applicable, the member firms that employ them. The costs to the forum include the specific costs to administer the claim as well as the overall attendant costs to administer expungement requests in the forum. Associated persons and member firms that are not assessed the fees for a non-monetary claim experience a benefit in the form of an economic transfer; the costs that were intended to be allocated but not assessed to the party or parties requesting expungement are instead borne by FINRA, other member firms, and other forum participants including other member firms, associated persons, and customers.

In the aggregate, if parties requesting expungement had been assessed the fees applicable to non-monetary claims during the sample period, then a reasonable estimate for the additional fees that would have been assessed is \$9.7 million. The \$9.7 million includes \$2.4 million for the expungement requests during a customer or industry

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<sup>57</sup> The chairperson honoraria includes \$300 for the prehearing conference and \$425 for the hearing session on the merits.

arbitration,<sup>58</sup> and \$7.3 million for the straight-in requests where an associated person added a small monetary claim (of less than \$1,000).<sup>59</sup> This amount reflects the potential economic transfer over the sample period. The extent of the transfer increased over the sample period with the proportion of straight-in requests where the associated person added a small claim amount.

The proposed rule change may affect some parties more so than others. Some parties, including associated persons and parties who request expungement relief on behalf of an unnamed person, may be more sensitive to the assessed fees under the proposed rule change or have monetary constraints that may inhibit them from filing an expungement request. They may determine that the cost of seeking expungement is

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<sup>58</sup> From January 2016 through June 2019, there were 1,508 arbitrations that closed during which an expungement request was filed (that was not a straight-in request). If the parties requesting expungement had been assessed the fees applicable to non-monetary claims, the parties requesting expungement would have been assessed additional filing fees totaling \$2.4 million (minimum filing fee of \$1,575 for each of the 1,508 cases). Although the parties to these expungement requests may also be assessed additional hearing session fees, the additional fees associated with hearing sessions are estimated to be marginal (see supra note 53).

<sup>59</sup> From January 2016 through June 2019, there were 1,064 arbitrations that closed in which a straight-in expungement request was filed. Associated persons added a small monetary claim (of less than \$1,000) in 797 of the 1,064 cases. Among the 797 arbitrations, 783 were filed against a member firm or a member firm and a customer, and 14 were filed solely against a customer. If parties requesting expungement had been assessed the fees applicable to non-monetary claims, and assuming one prehearing conference and one hearing session on the merits, then the parties to the straight-in requests filed against a member firm (or filed against that member firm and a customer) would have been assessed additional fees totaling \$7.2 million (\$9,475 less \$300 for each of the 783 cases), and the parties to the straight-in requests filed against a customer would have been assessed additional fees totaling \$0.1 million (\$9,475 less \$150 for each of the 14 cases). See supra notes 54 and 55 and accompanying text (discussing the fees that would be assessed under the proposed rule change and that are currently assessed).

higher than the anticipated benefit and, therefore, not seek expungement relief.<sup>60</sup>

Associated persons and parties who request expungement relief on behalf of an unnamed person may also be more sensitive to the fees assessed under the proposed rule change if, given the facts and circumstances of the customer dispute, an arbitrator or panel is less likely to recommend expungement.<sup>61</sup>

Associated persons who would have otherwise expunged customer dispute information that may have or not have merit may experience a loss of business and professional opportunities as a result of the information remaining on the CRD system and its display through BrokerCheck. The loss of business and professional opportunities by one associated person, however, may be the gain of another. Associated persons who may benefit in this regard include those who are less price sensitive and continue to seek expungement of customer dispute information, and associated persons who do not have similar disclosures.

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<sup>60</sup> Under the Codes, the Director may defer payment of all or part of an associated person's filing fee on a showing of financial hardship. See supra note 3232.

<sup>61</sup> A firm or associated person can also initiate an expungement proceeding directly in a court of competent jurisdiction without first going through any arbitration proceeding. FINRA will challenge these requests in court in appropriate circumstances. From January 2016 through June 2019, the expungement of 123 customer dispute disclosures were sought directly in court. The assessed fees may incent firms or associated persons to initiate an expungement proceeding directly in a court of competent jurisdiction without first going through any arbitration proceeding. The number of firms or associated persons who would instead initiate an expungement proceeding directly in a court of competent jurisdiction is dependent not only on the fees assessed under the proposed rule change, but also the legal fees and other costs a firm or associated person would expect to incur in the different forums to initiate an expungement proceeding. This information is generally not available, and accordingly the potential effect of the proposed rule change on direct-to-court expungement requests is uncertain.

The proposed rule change may also affect some member firms more so than others. In particular, the fees assessed under the proposed rule change may be more material for small firms or firms with fewer financial resources than for large firms or firms with additional financial resources.<sup>62</sup> Although the fees may be more material to some firms, the fees are the same as those required for a non-monetary claim and do not depend on the size or financial resources of the firm.

Although the proposed rule change may affect some associated persons and member firms more so than others, the proposed rule change will not result in any burden on competition that is not necessary or appropriate. As discussed above, associated persons and member firms that are assessed significantly lower fees for an expungement request than what is intended under the Codes by adding a small damages claim to the expungement request experience a benefit in the form of an economic transfer. Any burden on competition as a result of this proposed rule change, therefore, relates to the removal of this unintended benefit.

Finally, the proposed rule change may have other, marginal, economic effects. For example, the proposed minimum filing fee would trigger a three-person panel for all

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<sup>62</sup> The definition of firm size is based on Article 1 of the FINRA By-Laws. A firm is defined as “small” if it has at least one and no more than 150 registered persons, “mid-size” if it has at least 151 and no more than 499 registered persons, and “large” if it has 500 or more registered persons. In the cases associated with an expungement request filed and closed from January 2016 through June 2019, including expungement requests during a customer or industry arbitration and straight-in requests, 78 percent of the surcharge and process fees were incurred by large firms, 11 percent were incurred by mid-size firms, and 11 percent were incurred by small firms. The large firms incurring member surcharge or process fees had a median excess net capital of \$21.7 million in the year prior to the filing of a straight-in request, the mid-size firms had a median excess net capital of \$1.6 million, and the small firms had a median excess net capital of more than \$334,000.

straight-in requests. Associated persons would lose the ability to unilaterally decide the number of arbitrators who would consider and decide the request and, therefore, may increase the number of three-person panels. The impact of this change may be small because parties may still jointly agree to a single arbitrator.

The proposed rule change may also affect the customer dispute disclosures on the CRD system and their public display through BrokerCheck. The disclosures that would have otherwise been expunged would remain, and, depending on the merit of these disclosures, may affect the value of the information describing the conduct of associated persons. The merit of these disclosures is dependent on many factors which are difficult to predict. These factors include the incentive of parties to file an expungement request under the proposed rule change and the merit of the customer disputes that would have otherwise been sought expunged. The effect on the value of the customer dispute information is therefore uncertain.

(d) Alternatives Considered

An alternative to the proposed rule change includes the minimum filing fee of \$1,425 for all expungement requests that was proposed in Regulatory Notice 17-42 (December 2017) (discussed in more detail below). Although parties filing an expungement request would pay an additional \$100 to file an expungement request under the proposed rule change, the \$1,575 filing fee is the filing fee applicable to non-monetary claims. As discussed above, an expungement request is a non-monetary claim under the Codes.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

FINRA published Regulatory Notice 17-42 (December 2017) (“Notice”) to seek comment on proposed rule changes related to expungement, including the minimum fees discussed in this filing.<sup>63</sup> FINRA received 28 comment letters in response to the Notice that addressed the filing fee, member surcharge, or process fee. A copy of the Notice is attached as Exhibit 2a. A list of the comment letters received in response to the Notice that are applicable to this filing are attached as Exhibit 2b.<sup>64</sup> Copies of the comment letters received in response to the Notice that are applicable to this filing are attached as Exhibit 2c.

In the Notice, FINRA proposed a minimum filing fee of \$1,425 for all expungement requests. In addition, FINRA proposed, consistent with the existing provisions under the Codes, to assess a member surcharge and process fee against each member that is named a party or respondent, or that employed the associated person at the time of the events giving rise to the dispute, as applicable. Some commenters supported the proposal and others raised concerns with the proposed fees or with the costs of expungement in general. A summary of the comments and FINRA’s responses are discussed below.

#### Filing Fee

NASAA and Public Citizen supported the \$1,425 minimum filing fee proposed in the Notice. NASAA stated that “the increased fees would at least in part” offset the

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<sup>63</sup> This filing addresses the comments to the Notice that: (i) relate to the proposed fees and (ii) do not address the other proposed changes in the Notice to the expungement framework that are not part of this filing, but are being developed separately from this filing. See supra note 3.

<sup>64</sup> All references to commenters are to the comment letters as listed in Exhibit 2b.

significant costs that FINRA and the states incur related to expungement requests, which include both the costs to review and to process expungement requests. Public Citizen stated that the minimum filing fee would be a “limit[] to potential overuse of expungement proceedings.” White expressed some support for the proposed minimum filing fee, stating that it may “benefit staff and limit” the “occasional” request for expungement “made years after the underlying event.”

Other commenters, including associated persons, member firms, and their industry and legal representatives, opposed the proposed minimum filing fee. Some commenters viewed the proposed minimum filing fee as an additional fee that would be burdensome and discourage associated persons from pursuing meritorious expungement claims.<sup>65</sup> For example, SIFMA stated that the filing fee would be an additional fee that the individual would have to pay in addition to the fees in the underlying arbitration. SIFMA also stated that the filing fee could (along with the other fees proposed in the Notice)<sup>66</sup> “have an unfortunate impact of creating a tiered system where only registered representatives and firms that can absorb these additional costs will be able to pursue expungement, regardless of merit.” JonesBell and Behr contended that since “presentation of an expungement request by a registered person who is a party to the underlying customer case does not require any additional administrative time or effort, either by FINRA, or by the arbitrators,” a purpose of the fee was to “financially punish

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<sup>65</sup> See Behr, JonesBell, and SIFMA; see also infra note 67.

<sup>66</sup> Some commenters misconstrued the proposed fees discussed in the Notice as allowing the same member firm to be charged two separate member surcharge and process fees in the same arbitration. See infra note 80 and accompanying text.

the associated person for making an expungement request, and to generate additional (but unwarranted) revenue for FINRA.” Liebrader stated that the approximately \$1,500 filing fee “just to file their claim” was “too high” for both associated persons seeking expungement and claimants in general in comparison to court filing fees, which “are in the \$200-\$300 range.” Several other commenters objected to the proposed minimum filing fee as an increase in the amount of the filing fee<sup>67</sup> or objected to the costs of requesting expungement in general.<sup>68</sup> Some commenters objected to the current costs associated with requesting expungement, which they viewed as too high.<sup>69</sup>

In response to these comments, FINRA declines to reduce or eliminate the proposed minimum filing fee. The \$1,425 filing fee proposed in the Notice corresponds to the minimum claim amount tier for a three-person panel to decide an arbitration.<sup>70</sup> As noted above, FINRA believes that most expungement requests should be decided by a

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<sup>67</sup> See Baritz, Higgenbotham, James, Janney, Keesal, Saretsky, Speicher, Walter, and Weinerf. One commenter, SEC Investor Advocate, stated that potentially increasing the fees that brokers or firms must pay when requesting expungement, along with other enhancements to the expungement process proposed in the Notice but not addressed in this filing, may cause brokers to seek to avoid the Rule 2080 process entirely, and instead request expungement of their records directly from a court. FINRA notes that a broker can seek expungement by going through the FINRA arbitration process or directly to court (without first going through arbitration). See FINRA Rule 2080; see also supra note 8 (describing the requirement to name FINRA as a party when brokers seek expungement in court).

<sup>68</sup> See Deal, Harris, Isola, Rieger, and Smart.

<sup>69</sup> See AdvisorLaw, Commonwealth, Di Silvio, Mahoney, and Scrydloff. AdvisorLaw also provided a hyperlink to an online petition that requested signatures to “support a balanced, cost and time effective, expungement process” and that collected associated comments.

<sup>70</sup> The minimum claim amount tier for a three-person panel and a filing fee of \$1,425 is \$100,000.01 to \$500,000.

three-person panel.<sup>71</sup> In addition, an expungement request without a damages claim is a non-monetary claim under the Codes, which requires a three-person panel and currently requires a filing fee of \$1,575. Thus, under the proposed rule change, an associated person, or a requesting party if it is an on-behalf-of request, would be required to pay a \$1,575 filing fee for an expungement request made during a customer arbitration or straight-in request.

Associated persons should not be able to reduce the filing fee from the \$1,575 owed for a non-monetary claim to \$50—and reduce the hearing session fee to \$50, the member surcharge to \$150 and the process fee to \$0—merely by adding a small monetary claim, that the associated person often subsequently drops. Today, persons who do not add a small monetary claim to a straight-in request pay the \$1,575 filing fee associated with non-monetary claims. The proposal would ensure that all associated persons who request expungement are subject to the same minimum filing fee.

In addition, as with other non-monetary claims, FINRA incurs costs to process expungement requests. Accordingly, expungement requests should be subject to the same minimum filing fee as other non-monetary claims.

FINRA also declines to revise its proposal to charge the minimum filing fee when expungement is requested, irrespective of whether the request is made in a straight-in request or in an underlying customer arbitration. FINRA notes that other claims for relief filed by associated persons during a customer arbitration (i.e., counterclaims, cross claims, and third party claims) all result in a separate filing fee, just as they would if the

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<sup>71</sup> See supra Item II.A.1.(a)II.(iii), “Concerns with Avoidance of the Current Fee Structure for Expungement Requests.”

associated person filed the claim in a separate arbitration. FINRA acknowledges that the costs to process straight-in requests and requests made in an underlying customer arbitration may not be identical.<sup>72</sup> However, FINRA believes that the proposed minimum filing fee is commensurate with the additional work that arbitrators should undertake when expungement is requested.<sup>73</sup>

With respect to the concern that the minimum filing fee may prevent associated persons from making meritorious expungement requests, FINRA notes that the Director may defer payment of all or part of an associated person's filing fee on a showing of financial hardship.<sup>74</sup>

#### A. Cost Shifting

Some commenters proposed shifting the costs of requesting expungement away from associated persons. Braschi suggested that FINRA provide a mechanism to shift the cost of expungement to customers and their attorneys, and Wellington suggested that FINRA should impose little or no cost if the associated person receives an expungement recommendation. Liebrader stated that FINRA should have its members "shoulder more of the cost in this mandatory arbitration forum" and should "provide more relief for Claimants who for financial reasons have trouble coming up with the filing fees."

FINRA believes that the costs associated with expungement requests should generally be shared by the associated persons who are the subject of the customer

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<sup>72</sup> See supra note 11 (describing how a second member surcharge and process fee will not be assessed in an arbitration, even if expungement is requested).

<sup>73</sup> See supra Item II.A.1.(b)I.

<sup>74</sup> See supra note 32.

complaints and arbitrations, and the firms that employ them.<sup>75</sup> In addition, consistent with the current fee structure under the Codes, under the proposed rule change member firms will continue to bear the larger share of the costs of expungement. As with other types of arbitration claims, member firms that are respondents or employed the associated person seeking expungement, not the associated person or customer, pay the majority of the expense of the forum through the member surcharge and process fee. In addition, as noted above, the Director may defer payment of the filing fee for claimants that demonstrate financial hardship.<sup>76</sup>

#### Member Surcharge and Process Fee

In the Notice, FINRA proposed that when expungement is requested, there would be an assessment of a member surcharge and process fee, consistent with the existing provisions of the Codes,<sup>77</sup> against each member that is named as a party or respondent, or that employed the associated person named as a respondent or party at the time of the events giving rise to the dispute, as applicable. Several commenters expressed concerns with this proposal.

A. Assessment Against Firm that Employed Associated Person “At the Time of the Events Giving Rise to the Dispute”

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<sup>75</sup> Under the Codes, a panel may order in the award that a party reimburse another party for all or part of any filing fee paid. See supra note 32. In addition, in a customer arbitration, the Director will refund the member surcharge if the panel denies all of the customer’s claims against the member or associated person and allocates all hearing session fees against the customer. See FINRA Rule 12901(b)(1).

<sup>76</sup> See supra note 32.

<sup>77</sup> See supra notes 10 and 11 and accompanying text.

Keesal stated that the proposed assessment of a member surcharge and process fee against the member firm that employed the associated person at the time of the “events giving rise to the dispute” required “further clarification.” Keesal stated that parties may contend that multiple events gave rise to a customer claim, during which the associated person may have been employed with multiple member firms.

After considering the comment, FINRA has modified the proposal to assess, consistent with the existing provisions of the Codes, member surcharge and process fees against the member firm that is a party or is named as a respondent, or “that employed the associated person at the time the customer dispute arose.”<sup>78</sup> This is the standard that currently triggers an obligation to pay the process fee and member surcharge in FINRA arbitrations.<sup>79</sup>

#### B. When Expungement is Requested in a Customer Arbitration

SIFMA expressed concern that, when expungement is requested in a customer arbitration, the proposal would result in the assessment of a second member surcharge and process fee against a member firm “in addition to the fees charged in the underlying arbitration.” Keesal similarly stated that imposing these fees during the customer arbitration was not justified because the expense of “empaneling and compensating arbitrators and administering the case” should be handled as part of the customer arbitration.

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<sup>78</sup> See supra notes 35 and 43 and accompanying text.

<sup>79</sup> See, e.g., FINRA Rules 12901(a)(1)(C) and 13903(b).

FINRA notes that the proposal retains the existing requirement that firms may be assessed only one member surcharge and one process fee in a customer arbitration,<sup>80</sup> and that the proposal does not impact how the member surcharge and process fee are assessed today in a customer arbitration.<sup>81</sup> Accordingly, member firms will not be assessed these fees twice in the same customer arbitration, even if expungement is requested during the arbitration. In addition, in the proposal, FINRA has clarified that the minimum member surcharge and process fee apply only when the associated person files a straight-in request against a member firm or customer.<sup>82</sup>

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve or disapprove such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

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<sup>80</sup> See supra notes 36 and 45; see also proposed Rules 12901(a)(6), 12903(e), 13901(f), and 13903(e).

<sup>81</sup> See supra note 10.

<sup>82</sup> See proposed Rules 12901(a)(3), 12903(c), 13901(c), and 13903(c).

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2020-005 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2020-005. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of such filing also will be available for inspection and copying at the

principal office of FINRA. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FINRA-2020-005 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>83</sup>

Jill M. Peterson  
Assistant Secretary

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<sup>83</sup> 17 CFR 200.30-3(a)(12).