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**NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION, INC.**

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June 4, 2003

Margaret H. McFarland  
Deputy Secretary  
U.S. Securities and Exchange Commission  
450 Fifth Street NW  
Washington DC 20549-0609

RE: File No. SR-NASD-2002-168; Proposed Rule 2130 Concerning the  
Expungement of Customer Dispute Information from CRD.

Dear Ms. McFarland:

Please accept NASAA's comments on the NASD's proposed Rule 2130 concerning the expungement of customer dispute information from the CRD. We substantially supported NASD NTM 01-65 because the current policy of allowing an expungement *for any reason with no criteria* as long as it is supported by a court order, was intended to be a temporary solution to the arbitrator ordered expungement problem. The longer this solution is in effect, the longer customer complaints will be expunged based upon a one-sided argument to an arbitration panel and/or a judge. The proposed rule strives for a better and more appropriate solution.

While we support the need for the rule and the criteria it establishes, we question why the criteria established in the NTM are not imposed directly as criteria NASD members must abide by and as criteria that an arbitration panel must find before they award expungement.

As the joint managers of the CRD, NASAA and the states it represents are interested parties to this rule. We acknowledge that NASAA worked closely with the NASD over many months to develop the concepts that form the basis of this rule. We are using this formal comment process to offer clarifications that we believe can improve this rule. As stated numerous times in the NTM 01-65, "expungement is an extraordinary remedy," and the discussion of criteria for its application ought to reflect this extraordinary remedy.

*Background*

As NASAA stated in its letter to NASD NTM 01-65, which is attached for reference, the proposed rule is a product of years of discussion among many entities representing different interests with often divergent goals. The expungement debate illustrates the difficulty of sharing a database among industry, regulators and the investing public. We have worked very hard to try to strike a balance between treating stockbrokers fairly and providing and preserving relevant information about stockbrokers for regulators and investors. The recent proliferation of privacy issues that have been raised because of advances in technology, combined with the

increasing number of retail investors that the states are charged to protect, increases the importance of adopting a fair, common sense expungement policy.

Prior to the 1999 moratorium on expungements set forth in NTM 99-09, customer complaints on the CRD were being expunged based upon the order of the arbitrator. Many records were being expunged by agreement of the parties in *quid pro quo* settlements. Whether an agent was able to have his record expunged was often a matter of having a clever lawyer rather than the merits of the complaint. Regulators and investors were thereafter denied access to important, relevant information about agents. After extensive discussions, the NASD and NASAA, in their capacity as joint managers of CRD, agreed that the NASD would establish an interim moratorium on this policy and only honor court-ordered expungements and certain others based on defamation claims. NASAA and the states believe that allowing arbitrators to order expungement without objective standards is bad for investors, regulators and the financial services industry.

### *Proposed NASD Rule 2130*

#### **NASAA Supports Specific, Limited Criteria Which Must Be Met Before Expungement Is Permitted.**

In our discussions, the NASD proposed that the rule on CRD expungement would establish three criteria under which an NASD member could seek to have customer complaint information expunged from the CRD. If the arbitration panel awarded expungement after a specific finding that the customer dispute information met one of the three criteria, the member could then have the award confirmed in court after naming the NASD as a party to the confirmation process. This step was to serve as a protective measure to assure that the arbitration panel made a *finding* that one of the specific criteria was met. If the member provided information to the NASD prior to the court confirmation process that demonstrated that the arbitration panel made a finding that one of the criteria was met, the NASD could consider whether to oppose the confirmation of the award or not.

While proposed Rule 2130 may ultimately achieve this objective described in the above paragraph, it is peculiarly drafted and may not work as contemplated in the NTM. Proposed Rule 2130(a) states that an expungement award must be ordered by a court of competent jurisdiction, an essential requirement under state record laws. Proposed Rule 2130(b) then states that a member seeking expungement must name the NASD as a necessary member to the court proceeding unless the member gets a waiver from the NASD based on one of the criteria enumerated in the rule: that the customer's complaint was without factual basis, that the complaint failed to state a claim or was frivolous, or that the complaint was defamatory. In the proposed rule, the criteria only comes into play when the *NASD decides* whether they want to oppose the expungement. NASD NTM 01-65 implied that the criteria would apply when a *broker dealer or registered representative* seeks to have their record expunged and that the *arbitration panel* could only award expungement if one of the criteria were met. On its face, the new rule places no obligations on broker dealers, their representatives or arbitration panels.

We believe that these criteria were established, among other reasons, to dissuade the practice of plaintiffs and NASD members from inappropriately bartering away the record of the complaint in a cash settlement. The rule, therefore, should state that a member could only seek expungement if their case meets one of the three criteria.<sup>1</sup> The rule would then require the arbitration panel to find that the customer complaint information met one of the three criteria. The rest of the rule would explain the process and have other safeguards to assure that this extraordinary relief is not abused. We offer the following as a draft of how the rule could be made clearer, including a suggested improvement on the “defamation” criteria.

### **Alternative to Proposed Rule 2130**

#### *Expungement through an arbitration proceeding*

(a) Members or associated persons seeking to expunge information from the CRD system in an arbitration proceeding arising from disputes with public customers may only seek expungement relief if the customer’s

- (1) claim, allegation or information is without factual basis;
- (2) complaint fails to state a claim upon which relief can be granted or is frivolous; or
- (3) complaint was false and made knowingly with intent to harm the agent’s reputation;

(b) The arbitration panel must make a finding that the customer complaint information at issue meets one of the 3 criteria established in (a).

(c) A member or associated person who has been awarded expungement by the arbitration panel must have the award confirmed in a court of competent jurisdiction and name the NASD as party to this proceeding.

#### *Expungement through a court proceeding*

(a) Members or associated persons seeking to expunge information from the CRD system arising from disputes with public customers in a court proceeding must name the NASD as a necessary party to the proceeding.

(b) The court must find that that the customer’s:

- (1) claim, allegation or information is without factual basis;
- (2) complaint fails to state a claim upon which relief can be granted or is frivolous;  
or
- (3) complaint was false and made knowingly with intent to harm the agent’s reputation.

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<sup>1</sup> The NASD has added a fourth criteria that the NASD will not oppose an expungement order even if it does not meet the 3 criteria if the case is so extraordinary that expungement should be granted anyway. We would be concerned if there were more than 1 or 2 expungements a year falling under this category.

*Conclusion*

NASAA engaged in the endeavor to craft an expungement rule in an effort to stop the process of NASD members inappropriately seeking to expunge customer complaint information. The best way to accomplish this goal is to create a rule stating clear criteria for when an arbitration panel can grant expungement relief and create an obligation on NASD members to seek arbitration only if the claim meets one of those criteria. While the proposed rule does create criteria, it does not put an affirmative duty on the NASD members to seek expungement only in certain circumstances and it does not place a duty on arbitrators to award expungements only when this specific criteria is met.

Thank you for the opportunity to respond to this release, should you have any questions, please call me at 360/902-8760.

Sincerely,

A handwritten signature in black ink that reads "Deborah R Bortner". The signature is written in a cursive, flowing style.

Deborah Bortner  
NASAA CRD Steering Committee Co-Chair and  
Washington Director of Securities

Cc: Doug Shulman, NASD  
Derek Linden, NASD

Attachment: Letter from Joseph Borg to Barbara Sweeney of (12/31/2001)