



NASAA

NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION, INC.

750 First Street N.E., Suite 1140

Washington, D.C. 20002

202-737-0900

Fax: 202-783-3571

www.nasaa.org

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Submitted electronically to rule-comments@sec.gov

Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-0609

RE: **File Number SR-FINRA-2020-030: Proposed Rule Change to Amend the Codes of Arbitration Procedure Relating to Requests to Expunge Customer Dispute Information, Including Creating a Special Arbitrator Roster To Decide Certain Expungement Requests**

Dear Ms. Countryman:

On behalf of the North American Securities Administrators Association (“NASAA”),¹ I hereby submit the following comments regarding the above-referenced proposal (“the Proposal”), made by the Financial Industry Regulatory Authority, Inc. (“FINRA”), and published by the Commission on October 1, 2020.

NASAA has a unique expertise in the expungement process because it has been involved in developing – and reforming – the process since its inception. NASAA also has a long-standing interest in ensuring that there is no compromise to the integrity of the information housed on the Central Registration Depository (“CRD”) and its investment adviser equivalent, the Investment Adviser Registration Depository (“IARD”). Each system contains information filed with state securities administrators by applicants for registration as broker-dealers, investment advisers, and their representatives. State securities administrators use this information as part of their licensing and oversight responsibilities, and they are generally obligated under state securities and public records laws to retain all information filed as part of a registration application or an amendment to the application.

As FINRA is aware, state securities administrators are not the only stakeholders who rely on the data in the CRD and IARD systems. These systems also contain critical information that allows the investing public to make informed decisions about selecting financial professionals to

¹ Organized in 1919, NASAA is the oldest international organization devoted to investor protection. NASAA’s membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, Mexico, Puerto Rico, and the U.S. Virgin Islands. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

guide them in building sound financial futures. Industry also uses this data to evaluate and hire the representatives who will in turn be trusted with customers' financial futures. Given the data's many uses and critical importance, the integrity of this data is imperative to all stakeholders.

NASAA's position on expungement is clear: expungement is an extraordinary remedy that should be granted solely in limited circumstances.² The frequency of arbitrator-awarded expungements demonstrates that this is not in fact the case.³ While the Proposal strengthens the procedures surrounding expungements, it unfortunately does not achieve the result of making expungement extraordinary, and therefore the ongoing threat to the integrity of recordkeeping and public information remains.

If adopted, the Proposal would require a broker named as a party in a customer-initiated arbitration to request expungement in the course of the underlying dispute or forfeit the ability to request expungement of the event at issue. Requiring a named broker to bring an expungement request during the underlying customer case is a procedural improvement over the current process. This change would enable an arbitrator to make a better-informed decision because the arbitrator would have presided over the case in chief. Further, the change would aid in ensuring that documentation is available to support such a decision. The current lack of timeliness of expungement requests is a significant concern for NASAA and its members. It is not uncommon for a broker to request expungement of a consumer complaint years after the event and, more importantly, well after documents have been destroyed for record retention purposes. As more

² See NASAA's 2018 Letter from Joseph Borg, NASAA President, to Marcia E. Asquith, EVP, Board and External Relations, *Re, Request for Comments – 17-42 Proposed Amendments to the Codes of Arbitration Procedure Relating to Requests to Expunge Customer Dispute Information* (Feb. 5, 2018) (the "17-42 Letter"), available at <https://www.nasaa.org/wp-content/uploads/2011/07/NASAA-Comments-to-FINRA-Regarding-Reg-Notice-17-42-Expungement.pdf>; Letter from William Beatty, NASAA President, to Barbara Black, FINRA Dispute Resolution Taskforce, *Re, NASAA Comments on Expungement of Matters from the Central Registration Depository* (Aug. 31, 2015), available at <http://nasaa.cdn.s3.amazonaws.com/wp-content/uploads/2011/07/NASAA-Expungement-Letter-enclosure.pdf>; Letter from Joseph Borg, NASAA President, to Barbara Sweeney, Secretary NASD Regulation, Inc., *Re, Request for Comments – 01-65 Proposed Rules and Policies Relating to the Expungement of Information from the Central Registration Depository* (Dec. 31, 2001), available at <http://www.nasaa.org/wp-content/uploads/2011/07/95-Letter.37262-47637.pdf>; Letter from Deborah Bortner, NASAA CRD Steering Committee Co-Chair, to Margaret H. McFarland, Deputy Secretary, U.S. Securities and Exchange Commission, *Re, File No. SR-NASD-2002-168; Proposed Rule 2130 Concerning the Expungement of Customer Dispute Information from CRD* (June 4, 2003), available at <https://www.nasaa.org/wp-content/uploads/2011/07/82-ProposedNASDRule-202130.37775-72237.pdf>; Letter from Karen Tyler, NASAA President, to Nancy M. Morris, Secretary, U.S. Securities and Exchange Commission, *Re, Release No. 34-57572; File No. SR-FINRA-2008-010, Notice of Filing of Proposed Rule Change Relating to Amendments to the Codes of Arbitration Procedure To Establish New Procedures for Arbitrators To Follow When Considering Requests for Expungement Relief* (Apr. 24, 2008), available at <http://www.nasaa.org/wp-content/uploads/2011/07/31-Release-No34-57572SR-FINRA-2008-010NASAA.pdf>; Letter from Andrea Seidt, NASAA President, to Elizabeth M. Murphy, Secretary, U.S. Securities and Exchange Commission, *Re, Release No. 34-71959, File No. SR-FINRA-2014-020 Notice of Filing of a Proposed Rule Change to Adopt FINRA Rule 2081 (Prohibited Conditions Relating to Expungement of Customer Dispute Information)* (May 14, 2014), available at <https://www.nasaa.org/wp-content/uploads/2011/07/NASAA-Comment-Letter-Release-No-34-71959-File-No-SR-FINRA-2014-020.pdf>.

³ See The PIABA Foundation's 2019 Study on FINRA Expungements, available at <https://piabafoundation.org/wp-content/uploads/2019/10/Expungement-Study-101519-FINAL-VERSION.pdf>.

time passes, evaluating the merits of a request for expungement becomes even more challenging and thereby increases the likelihood that relief is granted inappropriately. Requiring a named broker to bring an expungement request during the underlying customer case goes a long way toward closing a significant loophole in the current expungement process. NASAA therefore supports this proposed change.

NASAA also supports the Proposal's requirement that a broker who requests expungement must be present for an in-person hearing on his or her request. NASAA does not believe, however, that the proposed in-person requirement should be satisfied by allowing the broker to appear by telephone or, as a matter of course, video conference.⁴ Requiring a broker to be physically present during an expungement hearing to present his or her case and respond to the panel is not an unreasonable burden given the extraordinary relief the broker is seeking. If a broker has a significant challenge that prevents in-person attendance, NASAA believes an exception may be allowed to permit the broker requesting expungement to appear via videoconference.

NASAA supports the Proposal's requirement that arbitration matters that involve expungement requests which were not decided during an underlying customer case must be heard by a specialized panel of arbitrators with enhanced experience and training. In NASAA's experience, a significant number of expungement requests are made in arbitration matters in which the underlying customer dispute is settled. As NASAA has noted previously, post-settlement expungement hearings often consist of one-sided presentations of the facts, because investors and their counsel—the only other parties to the case—have little incentive to participate after the investor's concerns have been resolved.⁵

NASAA supported FINRA's proposal under Regulatory Notice 17-42 that all expungement recommendations must be made unanimously by a three-person arbitration panel. NASAA is disappointed this was changed in the current Proposal to a majority decision. Given the extraordinary nature of expungement relief, it is inappropriate to recommend expungement without the agreement of the full arbitration panel. A divided panel indicates that there is doubt that the broker has met the higher burden attendant to eligibility for extraordinary relief, and thus should not merit an expungement recommendation.

The Proposal would prohibit a broker from filing a straight-in request against a customer, would codify guidance that directs a broker to provide the customer with a copy of the statement of claim when a straight in request is filed, and would codify guidance that directs arbitrators to allow customer participation in expungement hearings. NASAA supports FINRA's Proposal and agrees that while customers should not be obligated to participate in separate proceedings after their claims have been resolved, brokers should be required to provide actual notice to customers of expungement requests, and customers should be allowed to participate if they wish to be involved in hearings.

⁴ NASAA understands and supports temporary relief from requiring the broker to be physically present during the current pandemic.

⁵ See NASAA 2015 Letter, at 4-5. See also NASAA 2003 Letter, *supra* note 2.

The Proposal would codify FINRA guidance that prohibits brokers from “forum shopping,” and from attempting to request the expungement of an occurrence that has already gone in front of an arbitrator or a court. NASAA agrees with FINRA’s position that re-filing an expungement request that has been denied undermines the integrity of the process and therefore, supports these proposed changes as well.

The Proposal would establish time limitations surrounding when a broker can request expungement of customer dispute information. If adopted, a broker would be barred from requesting expungement (a) if more than two years have elapsed since the close of the customer arbitration or civil litigation that gave rise to the customer dispute information, or (b) if there was no customer arbitration or civil litigation involving the customer dispute information and more than six years had elapsed since the date that the customer complaint was initially reported in the CRD system. While NASAA generally supports this proposed change, we favor the 1-year timeframe that was proposed in Regulatory Notice 17-42.

If adopted, the Proposal would require FINRA to notify NASAA of an expungement request within 30 days after receiving a complete request for expungement. Unfortunately, this proposal falls short of responding to our 2018 feedback to Regulatory Notice 17-42. In that Comment Letter, NASAA laid out a six-principle framework for a more meaningful reform, each part of which reinforced the others. One request was for earlier notice to state regulators of an expungement request in order to better facilitate regulator involvement, where appropriate.⁶

FINRA’s Proposal only addresses one part of the six principles of NASAA’s framework. The Proposal identifies a complete request as: (1) the applicable filing fee under the Codes, (2) the CRD number of the party requesting expungement, (3) each CRD occurrence number that is the subject of the request, (4) an explanation as to whether expungement has been requested for the occurrence, and (5) the case name and docket number that gave rise to the disclosure, if applicable. While it is true that NASAA would receive earlier notice, this notice alone would not address the fact that NASAA members would have no opportunity to intervene during the arbitration hearing. Although states would be notified that a broker is requesting an expungement and the occurrence number, there would be no meaningful disclosure of information on which to assess the expungement request, nor would there be a legal mechanism to facilitate regulator involvement, the critical part of our 2018 framework that is missing from the current Proposal. The bottom line is that the Proposal fails to provide a pathway to contest the expungement relief request during the arbitration should a state determine it is appropriate to do so. Without NASAA’s members having a legal mechanism to intervene at this stage of the arbitration, notice is either meaningless or could force an investigation into every situation in which a broker requests expungement. While NASAA appreciates FINRA’s willingness to give it earlier notice of expungements, NASAA strongly prefers this relief be deferred to a proposal that would allow states to act on it.

While NASAA generally supports the Proposal and recognizes the amount of time, effort and consideration that FINRA has put into it, NASAA regards the reforms offered as procedural

⁶ See 17-42 Letter, *supra* note 2.

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improvements that do not address the core problem with the expungement process. NASAA maintains that further expungement reform is required to improve a failed system. NASAA encourages FINRA to continue to close gaps in the existing process and to initiate steps towards more meaningful expungement reform. NASAA looks forward to continuing its dialogue with FINRA in this regard, and we appreciate the opportunity to offer comments on the Proposal. Should you have any questions regarding the comments in this letter, please do not hesitate to contact either Melanie Senter Lubin (mlubin@oag.state.md.us), Maryland Securities Commissioner, and Chair of NASAA's CRD/IARD Steering Committee, or Vince Martinez (vlm@nasaa.org), NASAA's General Counsel.

Sincerely,

A handwritten signature in black ink, appearing to read "Lisa Hopkins". The signature is fluid and cursive, with a long, sweeping underline that extends to the right.

Lisa Hopkins
NASAA President
General Counsel and Senior Deputy
Commissioner of Securities, West Virginia