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## I. Introduction and Overview

To support their investor protection missions, FINRA and state securities regulators jointly collect and publicly disclose extensive registration information about financial professionals associated with broker-dealer firms (referred to herein as FINRA-registered financial professionals or RFPs). This registration information, which includes information about customer complaints, is used by regulators to license and oversee RFPs. The information publicly disclosed about RFPs is far more comprehensive than what is published for most other types of professionals.<sup>1</sup>

At times, RFPs seek to remove, or “expunge,” customer dispute information from their registration records. The expungement of customer dispute information raises important issues for multiple parties—RFPs, broker-dealer firms, regulators and the investing public. This Paper discusses these issues and asks questions about alternative processes for expungement determinations.

FINRA is mandated by federal statute to collect and maintain registration information about RFPs.<sup>2</sup> To satisfy this statutory responsibility, FINRA operates the Central Registration Depository (CRD®), which is used by FINRA, the Securities and Exchange Commission (SEC), other self-regulatory organizations (SROs), state securities regulators and securities firms.<sup>3</sup> The North American Securities Administrators Association (NASAA) and state securities regulators play a critical role in the ongoing development and implementation of the CRD system. FINRA also makes information reported to the CRD system publicly available through BrokerCheck®.<sup>4</sup>

The collection of registration information in the CRD system and the disclosure of the information through BrokerCheck serves three important purposes: (1) allowing investors to obtain information about an RFP or securities firm with whom they may do business; (2) providing securities regulators with a critical regulatory tool in overseeing the activities of RFPs and in detecting regulatory problems; and (3) providing securities firms with information for use in making informed employment decisions.

The value of the information is dependent on its completeness and accuracy. The absence of accurate information, as well as the presence of clearly inaccurate information, decreases the reliability and hence the value of the disclosure regime.

The requirements for reporting disputes between customers and RFPs are extensive. Reportable disputes include customer complaints, arbitration claims and court filings made by customers against RFPs and their broker-dealer firms, and the arbitration awards or court judgments that may result from those claims or filings. Information about these disputes must be reported regardless of whether the firm or the RFP believes the allegations are untrue, inaccurate or malicious, and FINRA is required by law and FINRA rules to disclose this information.

As discussed in more detail in this Paper, to expunge customer dispute information from the CRD system, a broker-dealer firm or RFP must obtain an order from a court of competent jurisdiction: (1) directing such expungement or (2) confirming an arbitration award containing expungement relief. Over the course of many years, FINRA has adopted a number of rules<sup>5</sup> governing the use of the arbitration forum administered by FINRA Dispute Resolution Services (DRS) to seek expungement of customer dispute information.<sup>6</sup> These rules seek to balance the interests of securities regulators in having accurate and relevant information to fulfill their regulatory responsibilities; the interests of investors in having access to accurate and meaningful information about RFPs with whom they may entrust their money; the interests of securities firms in having accurate information for use in making informed employment decisions; and the interests of the brokerage community in having a fair process to address inaccurate customer dispute information.

FINRA rules specify a narrow set of circumstances in which expungement of customer dispute information from the CRD system is appropriate. An arbitrator considering an expungement request must make a finding that the information to be expunged is factually impossible, clearly erroneous or false, or that the RFP was not involved in the alleged misconduct. When these standards were approved by the SEC, it was contemplated that expungement would be an extraordinary remedy that would be allowed only in these limited circumstances.

In addition to customer dispute information, FINRA maintains other registration information in the CRD system, including information about criminal proceedings, regulatory actions, civil judicial judgments and financial events. FINRA rules do not contemplate expungement of these other disclosure event types.<sup>7</sup> This Paper focuses exclusively on expungement of customer dispute information from the CRD system.

To put this discussion in context, we note that from January 2016 to December 2021 (sample period), approximately 8 percent of RFPs who were registered with FINRA at any point during the sample period had a customer dispute disclosure on their record; and of these RFPs, one in 10 had customer dispute information expunged from their CRD record. The number of RFPs who had customer dispute information expunged from their CRD record is 0.8 percent of all RFPs who were registered with FINRA at any point during the sample period.

FINRA has engaged in longstanding efforts with NASAA and state securities regulators to explore a redesign of the current expungement process. NASAA and state securities regulators have a shared interest with FINRA in protecting the integrity of the information contained in the CRD system, as it is a crucial tool in their registration and oversight responsibilities. According to NASAA, “[s]tate securities regulators are often legally obligated to maintain the information in the CRD system as a state record. Much of the information in the CRD system is filed with state securities regulators as part of the registration and qualification process, or filed by state securities regulators themselves. The Uniform Securities Acts, which form the basis of most state securities statutes, generally provide that securities regulators must retain all information filed as part of a registration application or as an amendment to the information filed as part of the application.”<sup>8</sup> Thus, NASAA has indicated that expungement of customer dispute information potentially implicates the public records obligations of state governments.<sup>9</sup>

This Paper examines the current process to obtain expungement of customer dispute information from the CRD system. The Paper then discusses several concerns associated with the current process for resolving expungement requests through arbitration and FINRA's efforts to address a number of those concerns through its recent Special Roster Proposal (described more fully below). The Paper then discusses other potential changes to the expungement process, including whether to change the standards in FINRA rules that arbitrators must apply when considering expungement requests, and whether to replace the use of arbitration to resolve expungement requests with a new administrative (non-arbitration) process in which FINRA and state securities regulators would determine whether the standards for expungement have been met. The establishment of a new administrative process presents policy issues that will need to be considered more fully, may require action by the SEC and state securities regulators, and may also require federal or state legislation.

This Paper is intended to inform and encourage a continued dialogue regarding potential changes to the process used to resolve requests to expunge customer dispute information. Related policy questions may also be relevant to that dialogue, including: (1) what customer dispute information should be reported and publicly disclosed, and under what circumstances such information should be eligible for expungement; and (2) whether expungement should have a consistent set of standards and processes for RFPs and investment adviser representatives.<sup>10</sup> To further this dialogue regarding expungement, FINRA plans to organize discussions with other securities regulators and interested parties on the topics raised in this Paper, identify additional data or analysis that may help inform effective decision-making in this area, and consider further potential changes to the expungement regime beyond those that FINRA has already initiated.

## II. Background and Discussion

### A. FINRA's Role in Maintaining Information About Customer Disputes Involving RFPs

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As noted previously, customer dispute information reported about RFPs is maintained in the CRD system, the central licensing and registration system used by the U.S. securities industry and its regulators.<sup>11</sup> FINRA operates the CRD system pursuant to policies developed by FINRA and NASAA. FINRA, state securities regulators and the SEC use the CRD system as an important source of regulatory information to help inform registrations, examinations, investigations and disciplinary actions to protect investors and safeguard the markets. In addition, broker-dealer firms use information in the CRD system to help them make informed employment decisions. As of December 31, 2021, over 60 million registrations for RFPs have been processed through the CRD system over a period spanning more than 20 years.

Pursuant to rules approved by the SEC and pursuant to its statutory mandate, FINRA makes information from the CRD system publicly available through BrokerCheck.<sup>12</sup> BrokerCheck is a free tool available on FINRA's website to help investors make informed choices about the RFPs and broker-dealer firms with whom they may conduct business.<sup>13</sup> As part of its statutory obligation, FINRA publishes on BrokerCheck extensive disclosure information, including customer dispute information for RFPs who are currently or were formerly registered with FINRA.<sup>14</sup>

In general, the information in the CRD system is reported by registered broker-dealer firms, RFPs and regulatory authorities in response to questions on the uniform registration forms.<sup>15</sup> Customer dispute information maintained in the CRD system is reported through Forms U4 and U5.<sup>16</sup> Investment-related customer disputes that allege sales practice violations involving an RFP in a written complaint, arbitration, or civil litigation must be reported on these forms if the customer claims compensatory damages of at least \$5,000.<sup>17</sup> That information may relate to disputes that are pending, contested, unresolved or unproven.<sup>18</sup> If a customer dispute meets the reporting requirements, a broker-dealer firm must report information about the dispute, including the customer's allegations, even if the firm or the RFP believe the allegations are untrue, inaccurate or malicious.

FINRA requires that broker-dealer firms update an RFP's Form U4 or U5 not later than 30 days after learning of the facts or circumstances of a customer dispute.<sup>19</sup> The information a broker-dealer firm must provide when reporting a customer dispute includes where the RFP was working when the activities that led to the dispute occurred, the customer's allegations, the type of investment product at issue (if any), the alleged amount of damages and how the dispute was resolved. A broker-dealer firm also is obligated to amend Forms U4 or U5 when there are any changes to the status of a previously reported customer dispute not later than 30 days after learning of the changes, including providing details as to how the matter was resolved.<sup>20</sup>

During the sample period referenced previously (January 2016 through December 2021), there were approximately 920,000 RFPs.<sup>21</sup> Of the 920,000 RFPs, approximately 75,000 RFPs (8 percent) had at least one customer dispute disclosure on their CRD record. The disclosure may have been reported prior to or during the sample period.

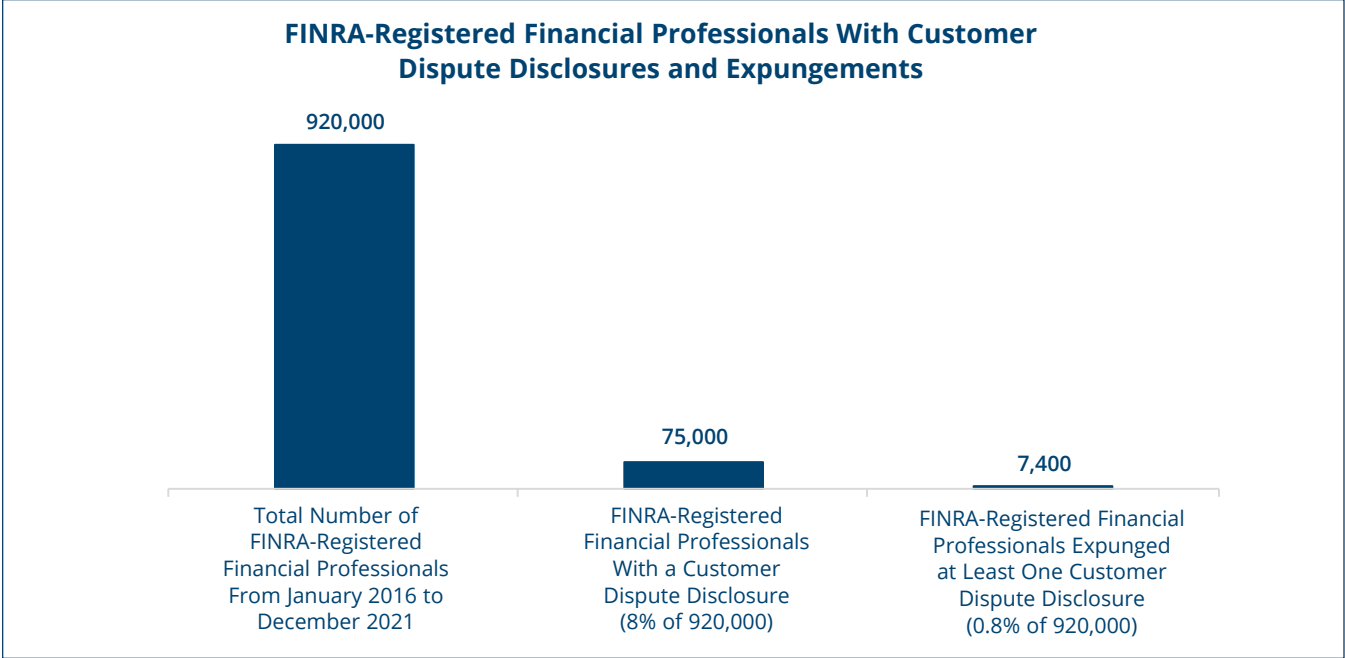
Forms U4 and U5 have been changed over the years to significantly expand the amount of information required to be reported. In 2009, for example, the SEC approved amendments to the forms to require a broker-dealer firm to report allegations of sales practice violations made against an RFP in an arbitration or a civil litigation even when the RFP is not a named party in the proceeding (e.g., a complaint is filed against the firm, without formally naming the individual RFP, but alleging that the RFP was involved in the alleged violation). The information reported about such disputes is now maintained in the CRD system as part of the RFP's record and is disclosed through BrokerCheck.<sup>22</sup> Prior to this change in the reporting requirements, customer-initiated arbitrations and civil litigations were not required to be reported on Form U4 unless the RFP was formally named as a defendant or respondent.<sup>23</sup> RFPs who were not named in the customer-initiated arbitration, but who as a result of these rules have that dispute included on their record in the CRD system, are referred to herein as "unnamed RFPs."

This change and others led to a significant increase in the number of customer disputes reported to the CRD system. Relatedly, the number of RFPs seeking expungement of customer dispute information from the CRD system has also increased because, for example, an RFP believes that the customer dispute information is false. During the sample period, approximately one-third of the 31,900 customer disputes reported on Forms U4 and U5 involved an unnamed RFP in an arbitration or civil litigation.<sup>24</sup>

## B. The Framework for Expungement of Customer Dispute Information

FINRA will expunge customer dispute information from the CRD system only pursuant to a court order. FINRA Rule 2080, which was developed in close consultation with representatives of NASAA and state securities regulators, provides that RFPs seeking expungement of customer dispute information from the CRD system must obtain an order from a court of competent jurisdiction directing expungement relief or confirming an arbitration award that contains expungement relief.<sup>25</sup> If a court directs expungement or confirms an arbitration award containing expungement, the customer dispute information is removed from the CRD system and is no longer made public through BrokerCheck.

Among the 75,000 RFPs during the sample period that had at least one customer dispute disclosure on their CRD record, approximately 7,400 of the RFPs had expunged at least one customer dispute disclosure from the CRD system. The removal of the customer dispute disclosures from the CRD system may have occurred either prior to or during the sample period. The 7,400 RFPs represent 0.8 percent of the 920,000 RFPs during the sample period, and almost 10 percent of the 75,000 RFPs that had at least one customer dispute disclosure on their CRD record.



### a. Seeking Expungement Through DRS’s Arbitration Forum

The process of seeking expungement through DRS’s arbitration forum originally developed when RFPs who were not found liable in a customer-initiated arbitration asked the panel<sup>26</sup> in that same case to expunge the underlying customer dispute from the CRD system. Use of DRS’s arbitration forum for expungement subsequently expanded when RFPs began requesting expungement of customer dispute information by initiating a new arbitration claim that was separate from the customer-initiated arbitration and did not involve the panel from the customer-initiated arbitration (this category of expungement requests are referred to as “straight-in requests”). Typically, these straight-in requests for expungement are filed after the customer-initiated arbitration settles or where a customer complaint has not evolved into a customer-initiated arbitration.

As discussed in further detail below, straight-in requests present inherent difficulties. Panels deciding straight-in requests issue awards containing expungement relief more often than panels deciding expungement requests made in customer-initiated arbitrations.

For either type of expungement request initiated in DRS’s arbitration forum, an independent arbitrator or a panel of independent arbitrators decides whether the party requesting expungement has established one of the Rule 2080(b)(1) grounds for expungement.<sup>27</sup> Pursuant to FINRA rules, in order to issue an award containing expungement relief, the panel must first hold a recorded hearing session regarding the appropriateness of expungement of the customer dispute information, and in cases involving settlements, review settlement documents and consider the amount of payments made to any party and any other terms and conditions of the settlement.<sup>28</sup> FINRA rules also require the panel to specify in the award which of the Rule 2080(b)(1) grounds serves as a basis for the expungement order and provide a brief written explanation of the reasons for its finding that one or more of the Rule 2080(b)(1) grounds applies to the facts of the case.<sup>29</sup> Thus, to include expungement relief in an award, the panel must find that: (A) the claim, allegation or information is factually impossible or clearly erroneous; (B) the RFP was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation or conversion of funds; or (C) the claim, allegation or information is false.<sup>30</sup> Arbitration awards are final and binding unless vacated based on one of the limited grounds set forth in applicable state or federal statutes<sup>31</sup>

These FINRA DRS rules are supplemented with extensive guidance and training provided to DRS's independent arbitrators. DRS has enhanced its expungement training for arbitrators to emphasize the importance of the information in the CRD system and BrokerCheck, and to underscore the arbitrator's important role in maintaining the relevancy and integrity of the information in those systems. DRS requires arbitrators to take mandatory online training on expungement to be eligible to serve as an arbitrator. The training includes materials that arbitrators should review when considering expungement requests, with a particular focus on the Notice to Arbitrators and Parties on Expanded Expungement Guidance (Guidance), first published in 2013 and expanded further periodically thereafter.<sup>32</sup> The Guidance explains the requirements of FINRA Rules 12805 and 13805, and provides arbitrators with best practices and recommendations to follow when deciding expungement requests.

**The Guidance reminds arbitrators:**

- ▶ to request any documentary or other evidence they believe is relevant to the expungement request, particularly in cases that settle before an evidentiary hearing or in cases where only the requesting party participates in the expungement hearing;
- ▶ to ask the RFP requesting expungement to provide a current copy of their BrokerCheck report;
- ▶ to inquire, in settled matters, whether the firm or RFP requesting expungement conditioned settlement of the arbitration upon agreement by the investor not to oppose the request for expungement;<sup>33</sup>
- ▶ to allow participation by customers and their counsel in expungement hearings;
- ▶ to consider whether a prior arbitration panel or court has issued an award or decision denying the same expungement request;
- ▶ that RFPs cannot file a separate request for expungement of customer dispute information arising from a customer-initiated arbitration until the customer-initiated arbitration has concluded; and
- ▶ to identify in the award the specific documentary or other evidence that they relied upon when deciding an expungement request.<sup>34</sup>

As a neutral administrator of the arbitration forum, DRS does not participate in the expungement decision-making process by arbitrators. That decision is made by the independent arbitrators selected by the parties.

## **b. Extent of Expungement in DRS's Arbitration Forum**

During the sample period, more than 4,700 RFPs (or broker-dealer firms on their behalf) requested the expungement of 10,156 customer dispute disclosures in 6,192 arbitrations that closed.<sup>35</sup> In 6,997 of the 10,156 expungement requests, a panel decided the customer case, issued an award on the expungement request, or both. The 6,997 expungement requests include requests made as part of customer-initiated arbitrations and straight-in requests.

In the remaining 3,159 requests, a panel did not decide the customer case or issue an award on an expungement request. This includes instances where the RFP withdrew or did not pursue the expungement request. This most often occurs when the RFP makes the expungement request as part of a customer-initiated arbitration that settles prior to a hearing on the merits.

Overall, RFPs were awarded expungement relief from a panel for 5,443 expungement requests filed during the sample period (as shown in the next chart). This represents 54 percent of the 10,156 expungement requests in arbitrations that closed during the sample period, and 78 percent of the 6,997 expungement requests in arbitrations during the sample period in which a panel issued an award on the merits of a customer dispute or on a straight-in request.

The rate at which expungement relief is awarded varies depending on whether the panel hears the merits of a customer’s case at a hearing and whether the request is made during a customer arbitration or filed as a straight-in request. For example, in customer-initiated arbitrations in which the customer dispute was resolved *after* a hearing on the merits, RFPs obtained awards containing expungement relief for 42 percent of the expungement requests. In comparison, in customer-initiated arbitrations in which the customer dispute was resolved *without* a hearing on the merits (*e.g.*, the customer dispute was settled), RFPs obtained awards containing expungement relief for 68 percent of the expungement requests. Finally, in straight-in requests, RFPs obtained awards containing expungement relief for 84 percent of the expungement requests.

Expungement Outcomes in Cases That Closed – January 2016 to December 2021					
	Number of Requests in Closed Cases	Number of Requests Where Award Issued	Number of Requests Where Award Issued With Relief	Percent of Requests Where Award Issued With Relief	Percent of Requests in Closed Cases With Relief
Requests as Part of Customer Arbitration	4,346	1,632	943	58%	22%
Customer Dispute Resolved After Hearing on the Merits	632	632	267	42%	42%
Customer Dispute Resolved Without Hearing on the Merits ( <i>e.g.</i> , Settled)	3,714	1,000	676	68%	18%
Straight-In Requests	5,810	5,365	4,500	84%	77%
Total	10,156	6,997	5,443	78%	54%

### c. The Court Confirmation Process

FINRA will not expunge customer dispute information from the CRD system based on an arbitration award unless that award is confirmed by a court of competent jurisdiction.<sup>36</sup> As described above, during the sample period, a panel in DRS’s arbitration forum issued an award containing expungement relief for 5,443 expungement requests. As of the end of the sample period, RFPs had sent to FINRA court orders confirming arbitration awards containing expungement relief for 4,717 customer dispute disclosures.<sup>37</sup>

FINRA will oppose confirmation of an arbitration award containing expungement relief in particular circumstances. For example, FINRA has opposed confirmation of arbitration awards when: (1) a panel included expungement of a customer dispute disclosure related to a prior arbitration in which the RFP was found liable; (2) a panel issued an award containing expungement relief but failed to follow the procedures required by FINRA rules and guidance when considering an expungement request; (3) a panel included expungement of information not eligible for expungement pursuant to FINRA Rule 2080; and (4) a panel included expungement of a customer dispute that was previously denied in another proceeding. These challenges by FINRA are intended to help ensure the integrity and accuracy of the information in the CRD system.

## C. Expungement Directed by Court Order

Relatively few RFPs seek a court order directing expungement of customer dispute information without first seeking expungement through arbitration (direct-to-court expungement cases). The decision to seek expungement in a direct-to-court expungement case instead of as a straight-in request in DRS's arbitration forum may be informed by a number of factors, including the costs to seek expungement, the participation and potential opposition by other parties including FINRA and state securities regulators in direct-to-court expungement cases, and whether the choice of forum might affect the likelihood of success of the request.

During the sample period, broker-dealer firms or RFPs sought expungement of customer dispute information in 104 direct-to-court expungement cases, an average of 17 direct-to-court expungement cases per year:

	2016	2017	2018	2019	2020	2021	Total	Avg. Per Year
Number of Direct-to-Court Expungement Cases	13	19	19	10	19	24	104	17

In a direct-to-court expungement case, a current or former RFP asks a court to consider the facts of the customer dispute information disclosure and to issue an order directing expungement of such disclosure from the CRD system. FINRA rules require that an RFP who files a direct-to-court expungement case name FINRA as an additional party.<sup>38</sup> FINRA's information regarding the underlying customer dispute, however, may be limited to the information reported in the CRD system. In addition, unlike in a straight-in request, when an RFP seeks expungement of customer dispute information directly from the court, customers are not likely to receive notice of the expungement request.

Unlike arbitrators considering expungement requests, courts are not bound by FINRA rules related to expungement of customer dispute information. While arbitrators considering expungement requests have received training regarding the importance of expungement, judges may or may not have knowledge about the missions of FINRA or the state securities regulators, the securities markets and the important purposes of the CRD system.

When FINRA is served with a direct-to-court expungement case, FINRA evaluates the facts and circumstances alleged in each case. FINRA will oppose a direct-to-court expungement case if, for example, the case seeks to expunge customer dispute information where: (1) the RFP was previously found liable to the customer; (2) the only basis for seeking expungement is the age of the customer complaint; (3) a prior fact-finder previously denied expungement; (4) the basis for seeking expungement is that the firm denied the customer's complaint, and the customer did not pursue litigation of the dispute; (5) the case seeks expungement of a customer complaint that was the subject of an arbitration award denying expungement, which was vacated without FINRA being notified or provided an opportunity to respond; (6) the facts presented by the RFP in the case clearly do not establish that the customer complaint meets one of the FINRA Rule 2080 standards; (7) the case seeks expungement of a customer dispute disclosure that was also the subject of regulatory action; or (8) the RFP invokes a court's equitable authority to seek expungement.<sup>39</sup>

FINRA also notifies NASAA of each direct-to-court expungement case in which FINRA is named and served.<sup>40</sup> NASAA and the appropriate state securities regulators conduct their own analysis of each direct-to-court expungement case to determine the state's position on the expungement request and assess whether a state will intervene to oppose expungement. FINRA's experience has been that, in cases where FINRA has opposed an expungement request and the state securities regulator intervenes to represent the interest of the state's investors, courts are more likely to deny expungement relief.



Of the 104 direct-to-court expungement cases during the sample period, RFPs sought expungement of 194 customer dispute information disclosures. As of December 2021, court proceedings had concluded for 173 of those disclosures and proceedings remained ongoing for 21 disclosures. Among the 173 disclosures for which the court proceeding had concluded, 107 disclosures were ordered expunged by a court (62 percent) and 66 disclosures were not ordered to be expunged (38 percent).

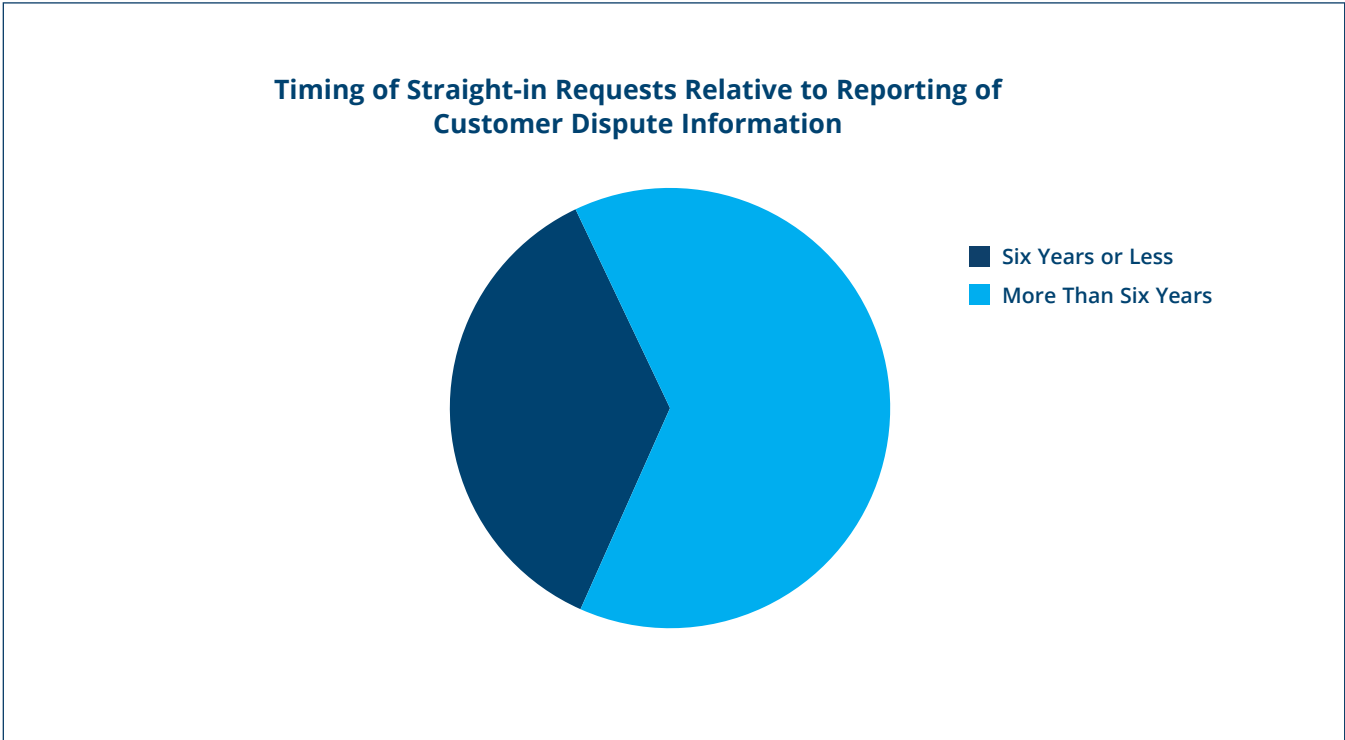
### D. Concerns With Existing Expungement Process

As discussed above, an RFP may request expungement of customer dispute information from the CRD system through the DRS arbitration process in two ways: (1) by requesting expungement during the customer-initiated arbitration; or (2) by initiating a new arbitration claim, separate from a customer-initiated arbitration, as a straight-in request.<sup>41</sup>

While commenters have raised concerns generally about RFPs' use of DRS's arbitration forum to seek expungement, their concerns, as well as FINRA's, have been particularly focused on straight-in requests.<sup>42</sup>

First, straight-in requests often involve aged customer dispute information reported on the RFP's CRD record a number of years prior to the expungement request. As a result, documents or information relating to the dispute may no longer be available.

For example, 6,476 straight-in requests were filed during the sample period in arbitrations that either remained open or were closed as of the end of the sample period. Approximately one-third of the straight-in requests were filed within six years of when the customer dispute information was initially reported to the CRD system. The remaining two-thirds of straight-in requests were filed more than six years after the customer dispute information was initially reported to the CRD system.<sup>43</sup>



Second, although DRS guidance provides that an arbitrator must ensure the customer has notice and an opportunity to participate in the expungement arbitration, customers and their representatives typically do not participate in hearings in straight-in requests and, therefore, the panel may receive information only from the RFP requesting expungement.

Third, the firm named in the straight-in request by the RFP may not have any relevant documents pertaining to the customer dispute because the event occurred while the RFP was employed at a different firm, or the respondent firm may support the expungement request because it has an interest in removing negative information from the RFP's CRD record.<sup>44</sup>

Fourth, RFPs are also making repeated attempts to seek expungement of the same customer dispute information. For example, some RFPs make requests for expungement (by filing straight-in requests) after withdrawing or deciding not to pursue an expungement request made in the customer-initiated arbitration, presumably believing that another panel that has not heard the merits of the customer's claim may be more likely to decide expungement in their favor. FINRA is concerned about this practice of "arbitrator shopping," particularly when RFPs withdraw an original expungement request after the panel has been made aware of evidence that could result in the denial of the expungement request. FINRA has also observed that unnamed RFPs may attempt to seek expungement (using straight-in requests) after expungement was denied in the customer-initiated arbitration to which they were not a party, claiming they were not aware of the expungement request in the customer-initiated arbitration.<sup>45</sup>

Among the requests to expunge customer dispute information in arbitration during the sample period, FINRA identified 193 disclosures that were the subject of a previously withdrawn or denied request to expunge.<sup>46</sup> FINRA is concerned that "arbitrator shopping" and repeated attempts to seek expungement of the same customer dispute information are inconsistent with the arbitration process and threaten the integrity of the information in the CRD system.<sup>47</sup>

## E. FINRA's Efforts to Improve the Process of Seeking Expungement in DRS's Arbitration Forum

Concerns with the expungement process were previously considered by the FINRA Dispute Resolution Task Force (Task Force), whose members included representatives from the industry and the public with a broad range of interests in securities dispute resolution.<sup>48</sup> The Task Force unanimously recommended in its final report the creation of a special arbitration panel consisting of experienced arbitrators from the chairperson roster, who have received enhanced training on expungement, to decide expungement requests in settled customer-initiated arbitrations and for straight-in requests.<sup>49</sup> In making this recommendation, the Task Force noted some of the concerns identified in Section II.D. above. In particular, the Task Force noted that the majority of issues that arise in the expungement process are those involving settled cases that do not go to final resolution because in such cases: (1) the panel selected by the parties may not have heard the full merits of the customer dispute and, therefore, may not bring to bear any special insights in determining whether to grant an expungement request; and (2) claimants or their counsel have little incentive to participate in an expungement hearing once their dispute has been settled. The Task Force stated that creation of a special arbitration panel would make up for these deficiencies. The Task Force stated that this corps of specially trained arbitrators would follow the procedures set forth in FINRA rules and guidance and make a decision about whether FINRA Rule 2080 grounds exist to award expungement, keeping in mind the importance of maintaining the integrity of information in the CRD system. The Task Force also stated that a special arbitration panel should handle expungement requests when claimants did not name the RFP as a respondent in the customer-initiated arbitration; and that in these cases, the arbitration panel should ensure that the customer has notice of the RFP's expungement request and an opportunity to participate in the proceeding.<sup>50</sup>

In response to these Task Force recommendations, and to address concerns that FINRA and other interested parties have identified with the current expungement process, FINRA published proposed changes to further enhance the current expungement process, particularly with respect to straight-in requests, in *Regulatory Notice 17-42*.<sup>51</sup> The *Notice* requested comment on, among other things:

- ▶ establishing a roster of public chairpersons with additional training and experience from which a panel would be selected to decide straight-in requests;
- ▶ imposing time limits on when an RFP can request expungement in a straight-in request;
- ▶ codifying a party's ability to request expungement on behalf of an unnamed RFP and establishing procedures for such requests; and
- ▶ applying a minimum fee to expungement requests.

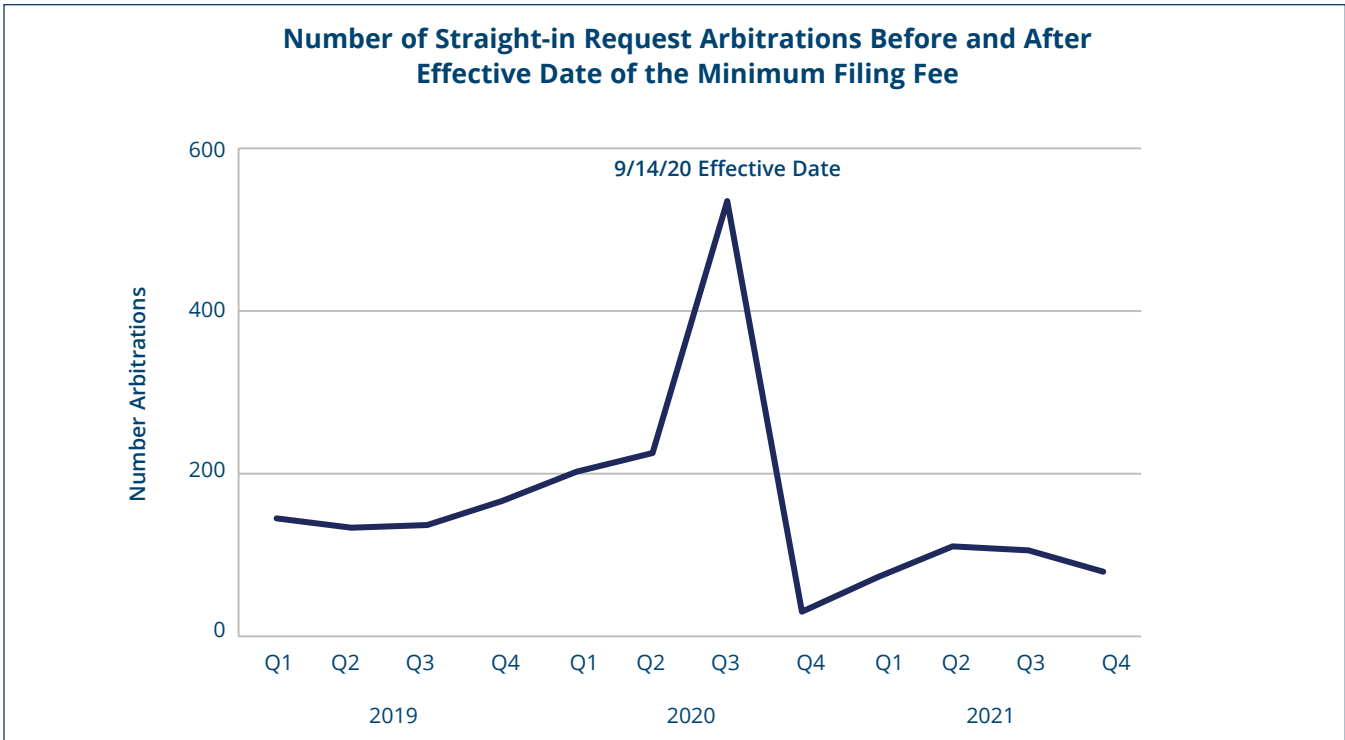
Since publication of the *Notice* and consideration of the comments, FINRA has filed with the SEC two significant rulemakings to amend the Codes to address concerns with the current expungement process, and straight-in requests in particular.

### **a. Amendments to Apply Minimum Fees to Expungement Requests**

Effective September 14, 2020, FINRA amended the Codes to apply minimum fees to requests for expungement of customer dispute information, whether the request is made as part of the customer-initiated arbitration or the RFP files a straight-in request. These minimum fees are the fees applicable to a non-monetary or unspecified claim.<sup>52</sup>

FINRA adopted these amendments to the Codes to address concerns about practices to avoid fees that were intended to be applicable to expungement requests, particularly where RFPs filing straight-in requests added a small monetary claim (typically, one dollar) to the expungement request to reduce the fees assessed against the RFP and to qualify for an arbitration to be heard by a single arbitrator. As a result of the amendment, parties requesting expungement can no longer avoid the fees intended for such requests under the Codes or automatically qualify for a single arbitrator to review their requests. The amendments 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.

Just prior to the effective date of this amendment, there was a material increase in the number of arbitrations filed in DRS's forum pertaining to straight-in requests. Following the effective date, the number of these arbitrations decreased significantly. The number of arbitrations pertaining to straight-in requests has since rebounded, but to levels below those prior to the effective date of the amendment. For example, the number of straight-in request arbitrations in 2021 is 63 percent of the number of straight-in request arbitrations in 2019.



### b. Special Roster Proposal

In September 2020, FINRA filed with the SEC a rule filing to make several significant enhancements to the current expungement process by establishing special arbitration procedures for expungement requests (referred to as the Special Roster Proposal).<sup>53</sup> The proposed changes adopted the recommendations of the Task Force and provided additional safeguards for ensuring that information maintained in the CRD system and disclosed through BrokerCheck is accurate and complete. Key proposed changes include:

- ▶ Imposing time limits within which RFPs may request expungement, which would prevent RFPs from requesting expungement many years—sometimes as many as 15 or 20 years—after customer disputes were reported to the CRD system. Specifically, DRS would deny the forum if the request for expungement is more than two years after the close of the customer-initiated arbitration or civil litigation that gave rise to the customer dispute information, and more than six years after the date the customer complaint was initially reported in the CRD system (if the customer complaint does not evolve into a customer-initiated arbitration or civil litigation).
- ▶ Providing state securities regulators with notification of all properly filed expungement requests at the time of filing of the expungement request in DRS’s arbitration forum.
- ▶ Requiring that all straight-in requests be decided by a three-person arbitration panel, randomly selected from a roster of experienced public arbitrators, with no significant ties to the industry (Special Arbitrator Roster).
- ▶ Prohibiting the parties to a straight-in request from agreeing to fewer than three arbitrators to review their expungement requests, striking any of the selected arbitrators, stipulating to an arbitrator’s removal or stipulating to the use of pre-selected arbitrators.<sup>54</sup>
- ▶ Requiring arbitrators to receive enhanced expungement training in order to be included on the Special Arbitrator Roster.
- ▶ Requiring an RFP named in a customer-initiated arbitration to request expungement during that customer-initiated arbitration, thereby ensuring that the panel that hears the full merits of a customer-initiated arbitration also reviews the related expungement request.

- ▶ Preventing an RFP from getting “two bites at the apple” by: (1) conditioning and limiting the ability of a party to a customer-initiated arbitration to request expungement during the customer-initiated arbitration on behalf of an unnamed RFP, so that the RFP cannot later claim they were not aware of the prior expungement request made on their behalf; and (2) precluding an RFP from requesting expungement of customer dispute information if a panel or a court previously denied a request to expunge the same customer dispute information.
- ▶ Prohibiting an RFP who withdraws an expungement request from refileing the same request at a later date, thereby preventing “arbitrator shopping.”
- ▶ Facilitating customer participation in straight-in requests by notifying customers of the time, date and place of any prehearing conferences and the expungement hearing, and making clear that customers are entitled to appear with representation at prehearing conferences and the expungement hearing (including providing testimony).
- ▶ Providing customers who seek to participate in straight-in requests with access to all relevant documents filed in the arbitration.
- ▶ Specifically authorizing the panel to request any documentary, testimonial or other evidence that it deems relevant from the broker-dealer firm or RFP seeking expungement.
- ▶ Requiring that the RFP requesting expungement appear personally at the expungement hearing.
- ▶ Requiring that the panel deciding the expungement request provide enough detail in the award to explain its rationale for including expungement relief in the award.<sup>55</sup>

The Special Roster Proposal was intended to reduce the concerns with straight-in requests identified above and to help ensure that the current expungement process works as intended—with specially trained and experienced arbitrators issuing awards containing expungement relief only in specified circumstances in accordance with the narrow standards in FINRA rules. Under the Special Roster Proposal, approximately 90 percent of the expungement requests filed in DRS’s arbitration forum and closed during the sample period, including requests made in customer-initiated arbitrations and straight-in requests, would have been considered by a three-person panel, randomly selected from the Special Arbitrator Roster. The remaining expungement requests would have been considered by a panel from the customer-initiated arbitration that heard the full merits of a customer’s arbitration claim.

On May 28, 2021, following discussions with SEC staff, FINRA withdrew the Special Roster Proposal rule filing from the SEC in order to consider whether modifications to the Proposal were appropriate in response to concerns raised by SEC staff and commenters.<sup>56</sup> At that time, FINRA indicated its intent to (1) continue pursuing the Special Roster Proposal, while also (2) continuing discussions with NASAA and other interested parties regarding a more fundamental redesign of the current expungement process, separate from and in addition to the changes included in the Special Roster Proposal.<sup>57</sup> FINRA’s Board of Governors continues to consider further changes to enhance the Special Roster Proposal.

FINRA continues to believe it is important to pursue a two-track approach to improving the expungement process. First, the integrity of the CRD system should be protected in the near-term by adopting the substantial improvements to the current expungement process that can be readily achieved with the Special Roster Proposal. For the reasons described above, this Proposal—which has already been through and benefited from several rounds of public comment, and many elements of which enjoy broad support—would immediately and materially mitigate a number of concerns with the existing process identified by the Task Force and other commenters and further highlighted by the data provided in this Paper. Moreover, developing alternative enhancements to the existing process, or redesigning that process altogether, will take substantially more time than approving the Special Roster Proposal—particularly since any such alternative changes need to be developed and analyzed, published for public comment, potentially revised in light of that comment, and (depending on their nature) may require legislative action. Failure to adopt the Special Roster Proposal in the meantime may result in expungements continuing to occur in the manner and frequency described above.

FINRA also believes, moreover, that moving forward with the Special Roster Proposal in the near term need not delay work that can be undertaken concurrently on developing additional enhancements to the current expungement process, or more fundamental alternatives to that process, with a view to better achieving in the long run the relevant policy goals in this space. As part of FINRA's commitment to encouraging continued discussions along these lines, the balance of this Paper puts forth several potential enhancements or modifications to the expungement process, together with related questions for consideration.

## F. Potential Further Improvements to the Expungement Process

Separate from and in parallel with the Special Roster Proposal, FINRA is considering potential additional improvements to the expungement process. Any such improvements must continue to seek to balance the interests of securities regulators in having accurate and relevant information to fulfill their regulatory responsibilities, the interests of investors in having access to accurate and meaningful information about RFPs with whom they may engage in business, the interests of securities firms in having accurate information for use in making informed employment decisions, and the interests of the brokerage community in having a fair process to address inaccurate information.

In order to promote further dialogue about potential improvements to the expungement process beyond adoption of the Special Roster Proposal, FINRA has set forth below questions to consider regarding: (1) further enhancements to the current expungement process through changes to FINRA Rule 2080; and (2) the development of an alternative to the existing expungement process that would be based on determinations made by regulators, rather than independent arbitrators. These or any other potential improvements to the expungement process require further analysis in order to inform decision-making by the relevant regulatory authorities, would likely require SEC approval of changes to FINRA's rules, and may require federal or state legislation.

### a. Potential Additional Enhancements to the Current Expungement Process

While FINRA believes the proposed changes in the Special Roster Proposal would address many concerns with the current expungement process, FINRA believes it is important to explore whether additional changes to its rules could further enhance the current process.

For example, FINRA could consider changes to the narrow standards in FINRA Rule 2080(b)(1) on which a panel must base its determination on an expungement request by an RFP. As discussed above, to include expungement relief in an award under current rules, the panel must find that:

- (A) the claim, allegation or information is factually impossible or clearly erroneous;
- (B) the registered person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation or conversion of funds; or
- (C) the claim, allegation or information is false.

Any changes to the standards expressed in FINRA Rule 2080 would raise a number of policy issues and must accomplish multiple goals. These goals include the need to maintain the integrity of the information in the CRD system, and to balance the interests of securities regulators, investors, securities firms and the brokerage community in the information contained in the CRD system.<sup>58</sup>

Consideration of changes to the standards in FINRA Rule 2080 would raise a number of other questions, including:

- ▶ Are there alternative standards to those set forth in FINRA Rule 2080(b)(1) that should apply to an RFP's expungement request?
- ▶ Should the same standards apply to an expungement request in arbitration and to FINRA's determination about whether to grant a request to waive the requirement that FINRA be named as an additional party in any court proceeding related to the expungement of customer dispute information?
- ▶ Should the standards for determining whether to include expungement relief in an award differ depending on whether expungement is sought in a customer-initiated arbitration or in a straight-in request?

In addition, consideration of changes to the standards and processes applicable to the expungement of customer dispute information from the CRD system might also include a review of the types of customer dispute information broker-dealer firms and RFPs are currently required to report to the CRD system; the relative benefits of these different types of information to investors, regulators and firms; whether any changes to what must be reported would be warranted; whether the ability of RFPs to comment on the information reported should be expanded or narrowed; and whether there are types of customer dispute information that should not be eligible for expungement or as to which different standards for expungement should apply.<sup>59</sup>

Given the critical role NASAA and state securities regulators play in the ongoing development and implementation of the CRD system, any changes to the standards related to the collection and potential expungement of information from the CRD system would require close consultation with NASAA and state securities regulators. In addition, any changes to FINRA rules would require SEC approval.

## **b. Questions Regarding a Potential Alternative Approach to the Current Expungement Process**

A potential alternative approach to expungement would be to develop an administrative process pursuant to which RFPs would seek expungement. This process could rely on FINRA and state securities regulators as decision-makers on expungement requests, in place of independent arbitrators in DRS's arbitration forum. Similar to the discussion above regarding any potential changes to the standards expressed in FINRA Rule 2080, development of an administrative process would need to balance the interests of securities regulators, investors, securities firms and the brokerage community in the information in the CRD system. In addition, development of an administrative process for expungement requests would raise the question of who is in the better position to determine such requests—FINRA, state securities regulators, independent arbitrators in DRS's arbitration forum, the courts, or a combination of the foregoing.

Development of an administrative process for expungement would raise a number of other policy issues as well as procedural questions, including:

### **Design of an Administrative Process**

- ▶ What would an administrative process look like such that both FINRA and state securities regulators would be involved in the expungement of records of importance to both groups?
- ▶ How would state securities regulators ensure they are satisfying their state records requirements?
- ▶ Would there be a way to design an administrative process that would not overly burden the limited resources of the relevant regulatory authorities? For example, should arbitral findings regarding the underlying customer dispute be considered in an administrative process that follows a customer-initiated arbitration? Would such an approach help reduce the potential resource burden of an administrative process?

- ▶ Even with an administrative process, should an RFP still be able to make an expungement request and obtain an expungement award in a customer-initiated arbitration? Should an administrative process be limited to expungement requests made in a customer-initiated arbitration where there is no hearing on the merits (*e.g.*, where the case settles), or where a customer complaint does not evolve into a customer-initiated arbitration?
- ▶ As part of an administrative process, would it be necessary for FINRA and the state securities regulators to agree on an expungement request? What would happen if FINRA and state securities regulators disagree as to the merits of the expungement request?

### Application for SEC Review

- ▶ A person aggrieved by final action of FINRA may apply for review by the SEC pursuant to Section 19(d)(2) of the Exchange Act. What rights of SEC review, if any, would an RFP have as part of the administrative process if their request for expungement is denied by FINRA?
- ▶ Should an RFP be required to exhaust administrative remedies, including SEC review of a denial of an expungement request, before seeking relief in court?

### Court Confirmation of an Administrative Decision to Expunge Customer Dispute Information

- ▶ Under the current expungement process, FINRA will expunge customer dispute information from the CRD system only pursuant to a court order.<sup>60</sup> With an administrative process, would a court order still be required before FINRA could expunge the customer dispute information from the CRD system, and if so, who would be necessary parties to that proceeding?

### Procedural Requirements

- ▶ As is the case with the current expungement process, development of an administrative process would necessitate consideration of applicable procedural requirements, including:
  - ▶ How should responsibility for determining whether expungement relief is appropriate, and advocating for FINRA and state securities regulators' positions on expungement requests, be structured?
  - ▶ To what extent, and by whom, would expungement requests be investigated and relevant evidence be obtained and presented?
  - ▶ What would be the appropriate standard of review and criteria for deciding expungement requests?
  - ▶ What time limitations should apply to expungement requests?<sup>61</sup>
  - ▶ What documentary evidence would be required in support of an expungement request?
  - ▶ What burden of proof should the RFP requesting expungement be required to meet?
  - ▶ Should expungement be available if documentary evidence is unavailable or not provided?
  - ▶ Should the administrative process require, or include the right to, a hearing on expungement?<sup>62</sup>

### Customer Participation

- ▶ The current expungement process stresses the importance of allowing customers and their representatives to participate in expungement hearings in DRS's arbitration forum. The Special Roster Proposal would amend the current expungement process to further encourage and facilitate participation by customers and their representatives in expungement hearings. With an administrative process, should customers and their representatives be notified of the expungement request and be permitted to participate in the administrative process? If so, to what extent?
- ▶ What would be the mechanism for participation by customers and their representatives?
- ▶ If customers and their representatives cannot or do not participate, how would the fact finders ensure they have the necessary relevant facts and information?



## Fees

- ▶ Under the current expungement process, forum fees are assessed by the panel against the parties requesting expungement where the sole topic of the hearing session is the determination of the appropriateness of expungement.<sup>63</sup> This requirement is retained in the Special Roster Proposal. What level of fees should be associated with an administrative process and how should the fees be assessed?

As both FINRA and state securities regulators have an interest in the outcome of any proposed administrative process, FINRA will continue to consult with state securities regulators and NASAA in developing any such process. In addition, the SEC and potentially Congress would need to consider what rights of appeal, if any, would be available to an RFP and whether an RFP would be required to exhaust administrative remedies prior to seeking relief in court. Finally, the SEC would have to approve FINRA-proposed rule changes to implement an administrative process.

## III. Conclusion

Protecting the integrity of the information in the CRD system and BrokerCheck is essential to FINRA's mission of investor protection. FINRA is committed to shaping the expungement process so that it operates as intended—as a remedy that is appropriate only in limited circumstances in accordance with the narrow standards in FINRA rules. Over the past several years, FINRA has taken numerous, meaningful steps to enhance the current expungement process, and FINRA intends to continue working on further improvements to this process. For example, FINRA believes that the Special Roster Proposal would address a number of significant issues in connection with the current expungement process, and FINRA intends to continue pursuing that Proposal.

FINRA also believes it is important to engage in a broader discussion with other securities regulators, broker-dealer firms and other interested parties on the issue of expungement. This Paper sets forth for discussion potential further enhancements to the current expungement process beyond the changes in the Special Roster Proposal, as well as questions regarding the use of an administrative process as a potential alternative approach to the current expungement framework. These potential changes require further analysis and may require action not only by FINRA, but also by the SEC and state securities regulators, who as discussed in this Paper play an important role in addressing expungement issues. Certain aspects of the potential changes may also require federal or state legislation.

In addition, to ensure consistent reporting about investment professionals, FINRA believes discussion regarding an alternative approach to the current expungement process for RFPs should include discussion of whether similar standards and procedures should also apply to customer dispute information reported about investment adviser representatives.<sup>64</sup>

By publishing this Paper, FINRA seeks to advance the dialogue on how to enhance or modify the expungement process available to RFPs. FINRA plans to organize further discussions with other securities regulators, broker-dealer firms and other interested parties to consider the questions raised in this Paper; identify additional data or analysis that may help inform effective decision-making in this area; and consider further improvements to the expungement process.

# Appendix

## Expungement Initiatives Chronology

FINRA first adopted a rule governing expungement in 2003. FINRA Rule 2080 sets forth the criteria applicable to the expungement of customer dispute information from the CRD system. Rule 2080 codified FINRA's practice of only expunging customer dispute information from the CRD system if a court of competent jurisdiction ordered expungement or confirmed an arbitration award containing expungement relief. Since the adoption of Rule 2080, FINRA has continued to work on several initiatives to improve the expungement process as described below.

- ▶ **November 2008** – FINRA adopted new Rules 12805 and 13805 governing arbitrators' consideration of expungement requests. Specifically, the rules require a panel to hold a recorded hearing session, and, if applicable, review settlement documents and the amount of payments made to any party before including expungement relief in an award, and to provide transparency in the award by indicating on which of the grounds in FINRA Rule 2080(b)(1) the panel based the expungement relief along with a brief explanation of the reasons for the finding.
- ▶ **April 2012** – FINRA published *Regulatory Notice 12-18* requesting comment on a proposal that would permit unnamed RFPs to seek expungement relief by initiating *In re* expungement proceedings at the conclusion of the customer-initiated arbitration. This was the first in a series of initiatives FINRA began to consider to address concerns with the number of expungement requests determined after the customer-initiated arbitration case settles.
- ▶ **October 2013** – DRS published the Guidance to address concerns that arbitrators may not be considering all relevant factors in determining whether to include expungement relief in an award after the customer-initiated arbitration case settles.
  - ▶ In **December 2014**, the Guidance was amended to remind arbitrators of the importance of customer and counsel participation in expungement hearings.
  - ▶ In **September 2015**, the Guidance was further amended to make clear that when an arbitration panel has issued an award denying an RFP's expungement request, the RFP *may not* request expungement in another arbitration case.
  - ▶ In **September 2017**, the Guidance was further amended to state that an RFP *may not* file a request for expungement of customer dispute information arising from a customer-initiated arbitration until the customer-initiated arbitration has concluded.
- ▶ **June 2014** – FINRA established the Task Force to consider possible enhancements to DRS's arbitration and mediation forum. The Task Force, which was composed of individuals from the public and industry sectors who represent a broad range of interests in securities dispute resolution, was charged with working together to suggest strategies to enhance the transparency, impartiality and efficiency of DRS's securities dispute resolution forum for all participants. The Task Force addressed a number of issues in its final report, including expungement.
- ▶ **July 2014** – FINRA adopted new Rule 2081 prohibiting conditioned settlements. The rule prohibits firms and RFPs from conditioning or seeking to condition settlements of customer disputes on, or otherwise compensating customers for, an agreement to consent to, or not to oppose, a request to expunge customer dispute information from the CRD system.
- ▶ **December 2015** – The Task Force issued its Final Report and Recommendations, in which it recommended that FINRA create a special arbitrator roster composed of chair-qualified arbitrators, who have completed enhanced expungement training, to handle expungement requests in settled cases and in straight-in requests.

- ▶ **December 2017** – FINRA published *Regulatory Notice 17-42* seeking comment on a proposal that, among other things, would establish a roster of arbitrators with additional training and specific backgrounds or experience from which a panel would be randomly selected to decide an RFP’s request for expungement of customer dispute information. The arbitrators from this roster would decide expungement requests where the customer-initiated arbitration is not resolved on the merits or the RFP files a separate claim requesting expungement of customer dispute information. In addition, the *Notice* requested comment on additional enhancements to the current expungement process that would apply to all expungement requests.
- ▶ **November 2019** – FINRA published an FAQ on Prohibited Conditions Relating to Expungement of Customer Dispute Information stating that FINRA Rule 2081 does not apply only to settlements; a violation of the rule does not depend on whether money or other consideration is provided to the customer; and an agreement reached at any time to release the customer from claims in exchange for the customer’s agreement to consent to, or not to oppose, an expungement request violates the rule.
- ▶ **July 2020** – FINRA amended the Codes to apply minimum fees to requests for expungement of customer dispute information, whether the request is made as part of the customer-initiated arbitration or the RFP files a straight-in request. The amendments 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.
- ▶ **September 2020** – FINRA filed the Special Roster Proposal with the SEC. Following discussions with SEC staff, on May 28, 2021, FINRA temporarily withdrew from SEC consideration the proposed amendments.

## Endnotes

1. For example, FINRA makes available to the public more comprehensive information on RFPs than is available for insurance agents, bankers, doctors, lawyers and accountants.
2. FINRA does not regulate investment adviser firms or the persons associated with those firms, including investment adviser representatives. They are instead regulated by the SEC or state securities regulators.
3. Registration information about investment adviser firms and investment adviser representatives is not maintained in the CRD system. Instead, registration information about investment adviser firms and their associated personnel is maintained in a different registration and disclosure system that is authorized by the SEC—the Investment Adviser Registration Depository (IARD) and the Investment Adviser Public Disclosure database (IAPD). See *What is IARD?*, Investment Adviser Registration Depository, <https://www.iard.com/whatisiard> and <https://adviserinfo.sec.gov>.
4. BrokerCheck fulfills FINRA's statutory obligation under Section 15A(i) of the Securities Exchange Act of 1934 (Exchange Act) to establish and maintain a readily accessible electronic or other process, to receive and promptly respond to inquiries regarding registration information on, among others, broker-dealer firms and RFPs. BrokerCheck displays information from the CRD system. A detailed description of the information made available through BrokerCheck is available at <http://www.finra.org/investors/about-brokercheck>.
5. A chronology of the steps FINRA has taken to develop and strengthen the expungement process in the arbitration forum throughout the years is provided in the Appendix.
6. DRS's arbitration forum is operated in accordance with rules approved by the SEC and is subject to ongoing oversight by the SEC. Decisions in DRS's arbitration forum are made by independent arbitrators selected by the parties, not by DRS staff. In almost every arbitration proceeding seeking expungement of customer dispute information, all or a majority of the arbitrators reviewing requests for expungement are public arbitrators (who, among other requirements, have never been employed in the securities industry). See also *infra* note 27. DRS's role in the arbitration process is to administer cases brought to the forum in a neutral, efficient and fair manner. In its role as the neutral forum administrator, DRS does not have any input into the outcome of specific arbitrations.
7. FINRA also maintains information about employment terminations in the CRD system. An RFP may seek expungement of this information through DRS's arbitration forum. See, e.g., *Notices to Members 99-09* (February 1999) and *99-54* (July 1999).
8. North American Securities Administrators Association, Inc., Brief of Amicus Curiae in Support of the Division of Securities and Retail Franchising, at 6-7, <https://www.nasaa.org/wp-content/uploads/2021/06/Brief-of-Amicus-Curiae-NASAA-in-Support-of-the-Div-of-Securities-and-Retail-Franchising-06.23.21.pdf>.
9. See *id.*
10. While this Paper focuses on the expungement of customer dispute information maintained in the CRD system for RFPs, FINRA believes that any consideration of the reporting and potential expungement of customer dispute information should also consider customer dispute information reported about investment adviser representatives. The SEC has long recognized the investor confusion about the different regulatory regimes for broker-dealers and investment advisers, and it has previously considered potential harmonization of regulatory requirements. See, e.g., Securities Exchange Act Release No. 69013 (March 1, 2013), 78 FR 14848, 14861-64 (March 7, 2013) (Duties of Brokers, Dealers, and Investment Advisers, File No. 4-606); Securities Exchange Act Release No. 83063 (April 18, 2018), 83 FR 21416, 21417 (May 9, 2018) (Form CRS Relationship Summary; Amendments to Form ADV; Required Disclosures in Retail Communications and Restrictions on the Use of Certain Names or Titles, File No. S7-08-18); Investment Advisers Act Release No. 4889 (April 18, 2018), 83 FR 21203, 21211-14 (May 9, 2018) (Proposed Interpretation and Request for Comment on Enhancing Investment Adviser Regulation, File No. S7-09-18).

11. The concept for the CRD system was developed by FINRA and NASAA. The CRD system fulfills FINRA's statutory obligation to establish and maintain a system to collect and retain registration information set forth in Section 15A(i) of the Exchange Act.
12. BrokerCheck includes information regarding an RFP's employment history, investment-related licensing information, as well as certain criminal, regulatory, civil judicial, financial and customer complaint events. A detailed description of the information made available through BrokerCheck is *available at* <http://www.finra.org/investors/about-brokercheck>.
13. In 2021 alone, almost 38.3 million searches of firms and financial professionals were conducted on BrokerCheck.
14. BrokerCheck discloses information about approximately 3,400 broker-dealer firms and approximately 612,000 current RFPs. BrokerCheck also discloses information about more than 17,000 broker-dealer firms and 548,000 RFPs formerly registered with FINRA. Former RFPs, 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. Pursuant to FINRA rules, approved by the SEC, records for former RFPs are available in BrokerCheck for 10 years after an RFP leaves the brokerage industry, and RFPs who are the subject of disciplinary actions and certain other disclosure events remain on BrokerCheck permanently.
15. 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).
16. FINRA, NASAA and state securities regulators developed Forms U4 and U5. Any amendments to these uniform registration forms require collaboration with, and agreement between FINRA, NASAA and state securities regulators before being filed with the SEC for approval.
17. This monetary threshold, however, does not apply if the customer alleges that the RFP was involved in forgery, theft, misappropriation or conversion of funds or securities.
18. The RFP can provide a brief summary on Form U4 of the circumstances leading to the customer complaint, arbitration or civil litigation as well as the current status or final disposition. Form U5 includes this ability to provide a summary, but the RFP may not be in a position to submit the Form U5 if they are no longer registered with the firm making the filing. An individual who is no longer registered, but for whom a BrokerCheck report is available, may submit a request to add a Broker Comment that provides an update or adds context to information disclosed through BrokerCheck. *See* <https://www.finra.org/registration-exams-ce/individuals/guidelines-broker-comments-brokercheck>.
19. *See* FINRA By-Laws, Article V, Sections 2(c) and 3(b). RFPs share the responsibility to keep current information on Form U4.
20. *See id.*
21. The RFPs included in this number were registered with FINRA at some point during the sample period. Some of the RFPs were not customer-facing and, therefore, unlikely to be named as part of a customer dispute.
22. *See* Securities Exchange Act Release No. 59916 (May 13, 2009), 74 FR 23750 (May 20, 2009) (Order Approving File No. 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 or civil litigation, was either mentioned in or could be reasonably identified from the body of the claim as a registered person who was involved in one or more of the alleged sales practice violations. Pursuant to FINRA Rule 8312, FINRA is required to disclose information about these customer disputes on BrokerCheck.

23. In addition, the SEC's Form BD does not require the reporting of customer disputes involving a firm or its associated persons on the firm's record.
24. During the sample period, there were also 143,000 disclosures of other types, including information about civil judgments and liens, bankruptcies, terminations, regulatory actions and criminal proceedings.
25. FINRA Rule 2080 also requires that FINRA be named as an additional party in any court proceeding related to the expungement of customer dispute information, unless FINRA waives being named. FINRA may waive the obligation that it be named if FINRA determines that a court or arbitration panel provided expungement relief based on one of the narrow standards identified in FINRA Rule 2080(b)(1).
26. The term "panel" means the arbitration panel, whether it consists of one or more arbitrators.
27. In almost every straight-in request, all or a majority of the arbitrators considering an expungement request are public arbitrators. Among other requirements, public arbitrators are not employed in the securities industry and do not devote 20 percent or more of their professional work to the securities industry or to parties in disputes concerning investment accounts or transactions or employment relationships within the financial industry. *See* FINRA Rule 12100(aa).
28. *See* FINRA Rules 12805 and 13805.
29. *See id.*; *see also* Securities Exchange Act Release No. 58886 (October 30, 2008), 73 FR 66086 (November 6, 2008) (Order Approving File No. SR-FINRA-2008-010) (stating that new Rules 12805 and 13805 require the arbitration panel to indicate "which of the grounds for expungement in Rule [2080](b)(1)(A)-(C) serves as the basis for the expungement"). *See also* *Regulatory Notice 08-79* (December 2008) (stating that "[t]he arbitration panel must indicate which of the grounds for expungement under Rule [2080](b)(1)(A)-(C) serve as the basis for their expungement order, and provide a brief written explanation of the reasons for ordering expungement"); FINRA Dispute Resolution Services Arbitrators Guide, p. 74, <https://www.finra.org/sites/default/files/arbitrators-ref-guide.pdf> (explaining that "FINRA Rule 2080 establishes procedures to ensure that expungement occurs only when the arbitrators find and document one of [the three grounds that are listed in FINRA Rule 2080(b)]"); Notice to Arbitrators and Parties on Expanded Expungement Guidance, <https://www.finra.org/arbitration-mediation/notice-arbitrators-and-parties-expanded-expungement-guidance>. DRS's Basic Arbitrator Training also explains that expungement may occur only after the arbitrators find and document one of these three grounds.
30. *See* FINRA Rules 2080(b)(1), 12805 and 13805.
31. Arbitration awards are subject to very limited judicial review under the Federal Arbitration Act and state arbitration statutes. A court of competent jurisdiction will typically confirm an award unless it is vacated or modified. Generally, an award that contains expungement of customer dispute information will not be vacated unless there is evidence that the panel exceeded its authority, was biased, or engaged in misconduct.
32. *See* Guidance, available at <https://www.finra.org/arbitration-mediation/notice-arbitrators-and-parties-expanded-expungement-guidance>. *See also* the Appendix.
33. In July 2014, FINRA adopted Rule 2081 to expressly prohibit firms and RFPs from conditioning settlement agreements for the purpose of obtaining expungement relief.
34. DRS also periodically provides additional materials to arbitrators to keep them informed about any changes to the expungement rules or forum practices. DRS offers an updated online "Neutral Workshop" on expungement, which further emphasizes the best practices described in the Guidance. A Neutral Workshop is an online discussion between or among experienced arbitrators on a specific arbitration topic, with a DRS staff member as a moderator. The discussions are posted on FINRA's website as a free, educational tool. Additional information about expungement rules and forum practices have been provided to arbitrators via a number of articles in a DRS staff quarterly newsletter, *The Neutral Corner*, which provides arbitrators and mediators with updates on important rules and procedures within DRS's arbitration forum and is distributed to neutrals and published on FINRA's website. *See, e.g., The Neutral Corner* Volume 1-2016 (Changes to Expungement Requests), available at [https://www.finra.org/sites/default/files/The\\_Neutral\\_Corner](https://www.finra.org/sites/default/files/The_Neutral_Corner)

[Volume 1 2016 0.pdf](https://www.finra.org/sites/default/files/The_Neutral%20Corner_Volume_4_2015.pdf); *The Neutral Corner* Volume 4-2015 (Questions and Answers: Parties Making Second Expungement Requests After Previous Denial), available at [https://www.finra.org/sites/default/files/The\\_Neutral%20Corner\\_Volume\\_4\\_2015.pdf](https://www.finra.org/sites/default/files/The_Neutral%20Corner_Volume_4_2015.pdf); *The Neutral Corner* Volume 1-2015 (Updated Expungement Guidance), available at [https://www.finra.org/sites/default/files/Neutral\\_Corner\\_Volume.1\\_2015.pdf](https://www.finra.org/sites/default/files/Neutral_Corner_Volume.1_2015.pdf); and *The Neutral Corner* Volume 3-2014 (Prohibited Conditions Relating to Expungement of Customer Dispute Information; Expanded Expungement Guidance; Questions and Answers: Expungement; Expungement Training: Updated to Include Rule 2081), available at [https://www.finra.org/sites/default/files/Neutral%20Corner\\_Volume%203\\_0.pdf](https://www.finra.org/sites/default/files/Neutral%20Corner_Volume%203_0.pdf).

35. During the sample period, more than one quarter of customer-initiated arbitrations and approximately 40 percent of intra-industry arbitrations involved an expungement request of customer dispute disclosures. The expungement requests related to customer dispute disclosures reported to the CRD system both before and during the sample period.
36. As discussed above, FINRA rules require that a party seeking to confirm an arbitration award containing expungement of customer dispute information name FINRA as an additional party, unless FINRA waives being named. *See supra* note 25. Regardless of FINRA's position on a waiver request, the applicable state securities regulators may seek to intervene in a court proceeding to challenge confirmation of the award containing expungement relief.
37. RFPs may have not yet sought or obtained a court order confirming an arbitration award for the remaining disclosures.
38. *See* FINRA Rule 2080. While FINRA Rule 2080 requires that FINRA be named as an *additional* party to any court proceeding regarding the expungement of customer dispute information, in 87 of the 104 direct-to-court expungement cases filed during the sample period, FINRA was the *only* named defendant.
39. It is FINRA's position that courts lack equitable authority to grant expungement relief absent a legal cause of action. In addition, FINRA rules, which do not purport to and cannot confer jurisdiction on state or federal courts, cannot form the basis of equitable relief in a court proceeding. FINRA opposed requests for expungement in 42 percent of the 104 direct-to-court expungement cases filed during the sample period.
40. *See* FINRA Rule 2080(b).
41. An RFP cannot file a separate request for expungement of customer dispute information arising from a customer-initiated arbitration until the customer-initiated arbitration has concluded.
42. A challenge in assessing the overall effectiveness of the current expungement process is that it is not practical to determine how many customer dispute disclosures are in fact eligible for expungement based on the narrow standards articulated in FINRA rules. To do so would require that the circumstances of each customer dispute be reviewed in detail, and that a determination be made regarding whether the disclosures are eligible for expungement. Absent an analysis of this type, however, as discussed further in this Paper it is appropriate to consider ways in which the expungement process can be strengthened to provide greater confidence that the information collected and maintained in the CRD system is accurate, while preserving appropriate flexibility to identify and expunge inaccurate information.
43. The Codes of Arbitration Procedure for Customer and Industry Disputes (Codes) provide that no claim shall be eligible for submission to arbitration under the Codes where six years have elapsed from the occurrence or event giving rise to the claim. This six-year eligibility rule applies to all arbitration claims, including those requesting expungement of customer dispute information. The issue of eligibility may be raised in a motion by the parties or *sua sponte* by the arbitrators. *See Horst v. FINRA*, No. A-18-777960-C (Dist. Ct. Nevada Oct. 25, 2018) (Order Denying Motion to Vacate Arbitration Award). In addition, FINRA Rules 12409 and 13413 provide that the arbitrators have the authority to interpret and determine the applicability of all provisions under the Codes. Thus, the decision of whether to dismiss a claim pursuant to this six-year eligibility rule is within the sole discretion of the panel. *See Howsam v. Dean Witter Reynolds*, 537 U.S. 79, 85-86 (2002) (finding that an arbitrator properly decides issues of eligibility). Such interpretations and decisions are final and binding upon the parties.

44. The Codes do not currently specify who RFPs must name when filing a straight-in request. Typically, RFPs file their straight-in requests against the broker-dealer firm at which the RFP is currently employed.
45. An unnamed RFP may seek to expunge customer dispute information by: (1) asking a party to the customer-initiated arbitration, usually the firm, to request expungement on their behalf; (2) seeking to intervene in the customer-initiated arbitration; (3) initiating a new arbitration in which the unnamed RFP requests expungement and names the customer or firm as the respondent; or (4) seeking expungement in a court of competent jurisdiction.
46. Additional subsequent requests to expunge customer dispute disclosures may have been filed in arbitration during the sample period but are not in this calculation because the initial expungement request was made prior to the sample period (*i.e.*, before January 2016). The 193 disclosures for which expungement of the same customer dispute information was sought in a subsequent arbitration can, therefore, be considered a lower bound for the number of these requests during the sample period.
47. In addition, FINRA has observed RFPs are moving to vacate arbitration awards that deny expungement relief and then seeking expungement in a new proceeding. If an award denying expungement is vacated and the RFP files a direct-to-court expungement case, FINRA may oppose expungement if FINRA was not provided notice or an opportunity to be heard in the proceeding to vacate the award.
48. See FINRA Dispute Resolution Task Force, <https://www.finra.org/arbitration-mediation/finra-dispute-resolution-task-force>. FINRA formed the Task Force to consider possible enhancements to DRS's arbitration and mediation forum.
49. See Final Report and Recommendations of the FINRA Dispute Resolution Task Force, <http://www.finra.org/sites/default/files/Final-DR-task-force-report.pdf>. The Task Force issued its final report with 51 recommendations. DRS has taken action on all of the 51 recommendations. See FINRA Dispute Resolution Task Force Recommendations, Final Status Report, [https://www.finra.org/sites/default/files/DR\\_task\\_report\\_status\\_011519.pdf](https://www.finra.org/sites/default/files/DR_task_report_status_011519.pdf).
50. With regard to arbitration cases that go to hearing on the merits of the customer dispute, the Task Force stated that a stronger argument can be made that the panel who resolves the customer dispute on the merits is the proper panel to make an expungement determination. Thus, the Task Force recommended allowing the panel that heard the merits of the customer dispute to conduct the expungement hearing provided the chairperson has completed the enhanced expungement training. See *id.*
51. *Regulatory Notice 17-42* (December 2017). Seventy comments were submitted on the proposal.
52. An expungement request is a non-monetary or not specified claim (non-monetary claim). The fees applicable to non-monetary claims are higher than those applicable to small monetary claims. See FINRA Rule 13900(a)(1). If an RFP files a straight-in request and does not add a monetary claim to the request, the RFP will be assessed the filing fee associated with a non-monetary claim. Non-monetary claims are decided by a three-person panel unless the parties agree in writing to one arbitrator. See FINRA Rules 12401(c) and 13401(c).
53. A description of the timeline relating to the filing of the Special Roster Proposal with the SEC is available at <https://www.finra.org/rules-guidance/key-topics/expungement#timeline>.
54. Under the Codes, the DRS arbitrator selection process uses the Neutral List Selection System (NLSS), a computer algorithm, to generate lists of arbitrators on a random basis from DRS's rosters of arbitrators for the selected hearing location. After the parties receive the arbitrator lists, the parties select their panel through a process of striking and ranking the arbitrators on the lists. Under the Special Roster Proposal, NLSS would randomly select three arbitrators from the Special Arbitrator Roster to consider the straight-in request. The parties, whose interests may be aligned, would not have the ability to select the arbitrators.
55. As discussed above, FINRA rules require that the panel provide a *brief* written explanation of the reasons for its finding that one or more of the FINRA Rule 2080 grounds for expungement applies to the facts of the case. See FINRA Rules 12805(c) and 13805(c). The Special Roster Proposal would remove the word "brief" from this requirement.



56. See FINRA Statement on Temporary Withdrawal of Specialized Arbitrator Roster Rule Filing, <https://www.finra.org/media-center/newsreleases/2021/finra-statement-temporary-withdrawal-specialized-arbitrator-roster>.
57. See *id.*
58. In its final report, the Task Force noted that when FINRA Rule 2080 was adopted “[w]hile there was general agreement about the need for a rule establishing procedures and criteria for expungement, there was considerable debate over both the procedures and the criteria. NASAA took the position that only ‘factually impossible’ claims should be expunged, while representatives of the brokerage community urged that it was unfair to require associated persons to institute a cumbersome procedure to remove from their record unfounded allegations by disgruntled customers. The final product was necessarily a product of compromise.” See *supra* note 49.
59. As part of its commitment to supporting efforts by broker-dealer industry participants to foster diversity, inclusion and equal opportunity, FINRA sought comment on any aspects of FINRA rules, operations and administrative processes that may create unintended barriers to greater diversity and inclusion in the broker-dealer industry or that might have unintended disparate impacts on those within the industry. In response, FINRA received a number of comment letters that the requirement to disclose some criminal and financial distress events, including events made publicly available through BrokerCheck, can have a significant negative impact on employment opportunities for underrepresented groups. See *Regulatory Notice 21-17* (April 2021).
60. See *supra* Section II.B. (discussing the framework for expungement of customer dispute information).
61. As discussed above, the Special Roster Proposal would impose time limitations beyond which an RFP would no longer be permitted to seek expungement in DRS’s arbitration forum.
62. The current expungement process requires that the panel hold a recorded hearing session by telephone or in person regarding the appropriateness of expungement. See FINRA Rules 12805(a) and 13805(a). As discussed above, under the Special Roster Proposal, in seeking expungement an RFP would be required to appear personally at an expungement hearing in DRS’s arbitration forum.
63. See FINRA Rule 12805(d).
64. It is also important to consider both regulatory regimes due to the growth in investment adviser representatives and decline in the number of RFPs. For example, during the sample period the number of individuals who were solely registered as an investment adviser representative increased by more than 8 percent annually while the number of individuals who were dually registered as an RFP and an investment adviser representative increased by almost 2 percent annually. In comparison, the number of individuals solely registered as an RFP decreased by 3 percent annually.

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