



Invested in America

May 6, 2022

Via E-Mail to rule-comments@sec.gov
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090
Attn: Vanessa A. Countryman, Secretary

Re: **File No. SR-FINRA-2020-030**
SIFMA Supplemental Comment on FINRA Expungement Rules and
Request for Immediate Remedial Relief

Dear Ms. Countryman:

The Securities Industry and Financial Markets Association (“*SIFMA*”)¹ appreciates the opportunity to submit this supplemental comment on FINRA’s proposed rule change to amend the Code of Arbitration Procedure regarding requests for expungement (the “*Proposal*”)² and current expungement rules, and to request immediate remedial relief, as follows:

On April 22, 2022, FINRA published a Discussion Paper entitled *Expungement of Customer Dispute Information* (the “*Discussion Paper*”)³ in which FINRA reiterated its intent to pursue the Proposal. In the Discussion Paper, FINRA repeated its erroneous assertion – also made in the Proposal – that the grounds on which FINRA arbitrators may grant expungement under Rules 12805(c) and 13805(c) are strictly limited to the three grounds listed in Rule 2080(b)(1) (i.e., error, mistake, or falsity).⁴ But that is not what the rules say.⁵

¹ SIFMA is the leading trade association for broker-dealers, investment banks and asset managers operating in the U.S. and global capital markets. On behalf of our industry’s nearly 1 million employees, we advocate on legislation, regulation and business policy, affecting retail and institutional investors, equity and fixed income markets and related products and services. We serve as an industry coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. We also provide a forum for industry policy and professional development. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit <http://www.sifma.org>.

² Securities Exchange Act Release No. 90000 (Sep. 25, 2020), 85 FR 62142 (Oct. 1, 2020), <https://www.govinfo.gov/content/pkg/FR-2020-12-28/pdf/2020-28509.pdf>.

³ Discussion Paper – Expungement of Customer Dispute Information (April 2022), https://www.finra.org/sites/default/files/2022-04/Expungement_Discussion_Paper.pdf at p. 17.

⁴ *Id.* at p. 5.

⁵ This is the third time we have brought this issue to FINRA’s attention. See SIFMA comment letter to SEC, File No. SR-FINRA-2020-030 (Oct. 22, 2020), <https://www.sifma.org/wp-content/uploads/2020/10/sifma-comment-re-FINRA-expungement-10.22.2020.pdf>, at pp. 2 – 5; and SIFMA comment letter to SEC, File No. SR-FINRA-2020-030 (Jan. 19,

Rules 12805(c) and 13805(c) state that the arbitration panel must indicate “which of the Rule 2080 grounds for expungement serve(s) as the basis for [the] expungement order.” Rules 12805(c) and 13805(c) do *not* limit expungement to the Rule 2080(b)(1) grounds. Rather, the rules explicitly extend to the full “Rule 2080 grounds” which include *both* Rule 2080(b)(1) and (b)(2) grounds.

FINRA’s position is in direct conflict with the plain language of Rule 2080. Rule 2080(b)(2) states, “If the expungement relief is based on arbitral findings *other than those described* above [i.e., in Rule 2080(b)(1)], FINRA . . . also may waive the obligation to name FINRA as a party if it determines that: [the expungement relief and findings are meritorious and would have no material adverse effect on investor protection, CRD system integrity, or regulatory requirements].” (emphasis added). Thus, FINRA arbitrators (and courts) today remain free to grant expungement on equitable grounds,⁶ including without limitation the grounds listed in Rule 2080(b)(2).

In a May 2021 response to an SEC staff request to clarify the grounds on which FINRA arbitrators may grant expungement, FINRA offered two explanations, neither of which hold water. First, FINRA stated that it was “FINRA’s longstanding view” that the grounds were limited to Rule 2080(b)(1).⁷ Obviously, “longstanding views” do not rewrite existing rules.⁸

Second, FINRA argued that the grounds listed in Rule 2080(b)(2) are not “grounds” for granting expungement, but are simply factors for FINRA to consider whether to waive the obligation to name FINRA as a party in a court petition for expungement relief.⁹ This argument also makes no sense. Rules 2080(b)(1) and 2080(b)(2) operate in exactly the same manner. When Rule 2080 is applied directly, both 2080(b)(1) and 2080(b)(2) serve as factors for FINRA to consider whether to waive being

2021), <https://www.sifma.org/wp-content/uploads/2021/01/sifma-comment-re-SEC-review-of-expungement-proposal-1.19.2020-FINAL.pdf>, at pp. 2 – 4.

⁶ See, e.g., *Lickiss v. FINRA*, A134179 (Cal. App. 1st, 2012) (a court may exercise its equitable jurisprudence to decide whether and under what circumstances expungement relief is appropriate), <https://caselaw.findlaw.com/ca-court-of-appeal/1610198.html#X34IDVBp9HI.mailto>.

⁷ FINRA letter to SEC, File No. SR-FINRA-2020-030 (May 18, 2021) (“*FINRA Letter*”), <https://www.sec.gov/comments/sr-finra-2020-030/srfinra2020030-8811356-238001.pdf> at pp. 5 – 6.

⁸ Regardless, FINRA’s view is not *that* longstanding. In 2003, when the SEC approved then new Rule 2130 (now known as Rule 2080), FINRA apparently held a different view, as evidenced by the following excerpt:

Some commenters suggested that the burden of complying with the three proposed standards should be placed squarely upon [FINRA’s] members. Such a rule would require that NASD members only seek expungement of data from the CRD system if such data fits within one of the three standards. NASD noted that it does not believe such an approach is necessary to achieve the objectives of the proposed rule. Federal and state courts, that are fully informed about the investor protection and regulatory implications of a proposed expungement order, [FINRA] argued, should be trusted to make the proper decision.

Release No. 34-48933; File No. SR-NASD-2002-168 (Dec. 16, 2003), <https://www.sec.gov/rules/sro/34-48933.htm>. FINRA’s FAQs about Rule 2080 also explicitly recognize that “expungement relief [may be] based on judicial or arbitral findings other than those described [in Rule 2080(b)(1)].” See FAQ 5, <https://www.finra.org/registration-exams-ce/classic-crd/faq/finra-rule-2080-frequently-asked-questions>. See also FAQ 6 (acknowledging that courts are not obligated to follow the standards in Rule 2080, but FINRA recommends that they do so).

⁹ FINRA Letter at p. 5.

named as a party. When Rule 12805 is applied (noting that it can only be applied by reference to Rule 2080), both 2080(b)(1) and 2080(b)(2) serve as grounds for granting expungement.

So how did we get into this mess? Following is the relevant background.

Background

1. **FINRA Expungement Rules Proposal.** In 2008, FINRA filed with the SEC its proposal to create then new FINRA Rules 12805 and 13805.¹⁰ Nowhere in the proposal did FINRA state that the grounds for expungement should be limited to those under Rule 2080(b)(1). Because the plain text of the proposed new rules did not limit the expungement ground to those under Rule 2080(b)(1), and because FINRA did not state that was its intention, none of the commenters on the proposal, or the public generally, had notice or opportunity to comment on this crucial point.
2. **SEC Order Approving.** In late 2008, the SEC published its Order Approving new Rules 12805 and 13805.¹¹ Because FINRA never requested that expungement be limited to the Rule 2080(b)(1) grounds, the SEC Order never addressed whether or why it would be appropriate to limit expungement to the Rule 2080(b)(1) grounds. In the *Description of the Proposed Rule Change – Background*, however, the SEC misstated that new Rules 12805 and 13805 require the arbitration award to indicate “which of the grounds for expungement in [Rule 2080](b)(1)(A)-(C) serves as the basis for the expungement...”¹² (emphasis added). This was a misstatement because it did not accurately describe the plain text of the proposed rules, or FINRA’s stated rationale and intent for proposing the rules. This misstatement is not reiterated in the SEC’s *Discussion and Commission Findings*, nor does it appear in the *Conclusion* or the final *Order*. Thus, this simple misstatement in the *Background* section of the Order Approving did not operate as an SEC approval of a rule change that FINRA neither gave notice of, nor requested.
3. **FINRA Reg. Notice 08-79.** In late 2008, FINRA published Reg. Notice 08-79 to announce the SEC’s approval of new FINRA Rules 12805 and 13805.¹³ Remarkably, FINRA ran with the misstatement in the SEC’s Order Approving and repeated it, misstating again that expungement relief is limited to the Rule 2080(b)(1) grounds.¹⁴ Needless to say, a misstatement made in the background section of an SEC order approving, and repeated in a FINRA regulatory notice, does not have the force or effect of rulemaking, and does not change the existing rules.

¹⁰ Securities Exchange Act Release No. 57572 (March 27, 2008), 73 FR 18308 (April 3, 2008), <https://www.finra.org/sites/default/files/RuleFiling/p038245.pdf> (stating that the purpose of the new rules was to ensure expungement occurs only when arbitrators find and document one of the grounds specified in Rule 2080 (formerly known as Rule 2130)).

¹¹ Securities Exchange Act Release No. 58886 (October 30, 2008), 73 FR 66086 (November 6, 2008), <https://www.finra.org/sites/default/files/RuleFiling/p117370.pdf>.

¹² *Id.* at 66087.

¹³ FINRA Reg. Notice 08-79 (December 2008), <https://www.finra.org/sites/default/files/NoticeDocument/p117540.pdf>.

¹⁴ *Id.* at p. 3.

4. Subsequent FINRA Publications. Since the approval of FINRA Rules 12805 and 13805, FINRA has continued to misstate that expungement is limited to the Rule 2080(b)(1) grounds in numerous publications, including without limitation:
- FINRA DRS Arbitrators Guide¹⁵
 - Notice to Arbitrators and Parties on Expanded Expungement Guidance¹⁶
 - FINRA Basic Arbitrator Training¹⁷
 - FINRA Reg. Notice 08-79, the Proposal, and the Discussion Paper (all discussed above)

FINRA apparently wishes that the grant of expungement was limited to the Rule 2080(b)(1) grounds, and did not include the Rule 2080(b)(2) grounds. Yet, FINRA does not seem interested in filing to amend Rules 12805 and 13805(c) and/or Rule 2080 to explain and justify, to respond to public comment on, or to require SEC approval of, its desired rule change. Instead, FINRA's preferred approach is to misstate the rules; continually republish those misstatements (including in various regulatory notices and arbitrator training materials), and then cite to those published misstatements as authority for its preferred rule change.

That is not how our notice and comment rulemaking process works. In fact, it is improper conduct for a regulator like FINRA to take a clerical error in the background section of an SEC order approving its expungement rules, and to exploit it to unilaterally effectuate its desired rule change without following the appropriate process. FINRA has never explained or justified why it is fair or appropriate to limit the grant of expungement to the Rule 2080(b)(1) grounds, nor has FINRA ever provided the public with a meaningful "opportunity to submit written data, views, and argument concerning" this limitation.¹⁸ As discussed above, FINRA has never had the Rule 2080(b)(1) limitation approved by the SEC. Even worse, to this day, FINRA continues to instruct its arbitrators to apply its misinterpreted, unvetted, and unapproved rule interpretation to actual expungement requests.¹⁹

Request for Immediate SEC Remedial Relief

For all the foregoing reasons, we respectfully request that the SEC direct FINRA to immediately cease and desist from misstating the grounds for granting expungement under FINRA Rules, and to promptly publish corrections to each publication, including without limitation all notices to members, arbitrator training materials, and the Discussion Paper, in which FINRA has misstated the ground for granting expungement.

¹⁵ <https://www.finra.org/sites/default/files/arbitrators-ref-guide.pdf> at p. 74.

¹⁶ <https://www.finra.org/arbitration-mediation/notice-arbitrators-and-parties-expanded-expungement-guidance>.

¹⁷ <https://www.finra.org/arbitration-mediation/required-basic-arbitrator-training>.

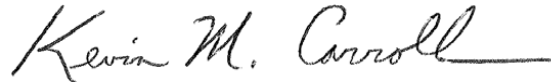
¹⁸ Securities Exchange Act, §§ 19(b)(1) and 19(d)(1).

¹⁹ See footnotes 15 – 17 and accompanying text.

* * *

Thank you for the opportunity to further comment. If you have any questions or would like to further discuss these issues, please contact the undersigned.

Sincerely,

A handwritten signature in black ink that reads "Kevin M. Carroll". The signature is written in a cursive style with a long horizontal line extending to the right.

Kevin M. Carroll
Managing Director and
Associate General Counsel

cc: *via e-mail to:*

Emily Westerberg Russell, Chief Counsel, Division of Trading and Markets
Lourdes Gonzalez, Assistant Chief Counsel, Division of Trading and Markets
Robert W. Cook, CEO, FINRA
Robert L.D. Colby, Chief Legal Officer, FINRA
Richard W. Berry, Executive Vice President and Director FINRA-DRS