



September 6, 2022

**Via email: rule-comments@sec.gov**

Deputy Secretary J. Matthew DeLesDernier  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549-1090

**Re: Release No. 34-95455; File Number SR-FINRA-2022-024  
Notice of Filing of a Proposed Rule Change to Amend the Codes of  
Arbitration Procedure to Modify the Current Process Relating to the  
Expungement of Customer Dispute Information**

Dear Mr. DeLesDernier:

The University of Miami Investor Rights Clinic (“Clinic”) appreciates the opportunity to comment on FINRA’s proposed new rules regarding expungement of customer dispute information.<sup>1</sup> The Clinic is a University of Miami School of Law clinical program that represents investors of modest means who, due to the size of their claims, cannot find legal representation. The Clinic believes its clients and the investing public will greatly benefit from the proposed changes to the expungement process and that the changes will strengthen the integrity of the SEC, FINRA, and the Central Registration Depository (“CRD”). For those reasons, the Clinic supports FINRA’s proposed new rules regarding the expungement process, with additional recommendations and commentary below.

Expungement should be an extraordinary remedy, since it was “intended [] as a remedy that is appropriate only in limited circumstances in accordance with the narrow standards in FINRA rules.”<sup>2</sup> However, as FINRA observed,<sup>3</sup> member firms and their associated persons have increasingly abused this remedy in recent years. While some commentators focus on the fact that only 4 percent of customer dispute information disclosures in the CRD system entered between 2015 and 2020 have been expunged pursuant to a court order,<sup>4</sup> the Clinic believes it is more

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<sup>1</sup> Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing a Proposed Rule Change to Amend the Codes of Arbitration Procedure to Modify the Current Process Relating to the Expungement of Customer Dispute Information, 87 Fed. Reg. 50170 (Aug. 15, 2022) [hereinafter Notice of Filing a Proposed Rule].

<sup>2</sup> *Id.* at 50170; *see also id.* at 50173 (listing the narrow circumstances justifying expungement).

<sup>3</sup> *Id.* at 50170 (“FINRA is concerned, however, that the current expungement process is not working as intended . . .”).

<sup>4</sup> *Expungement of Customer Dispute Information*, FINRA (Aug. 31, 2022, 5:42 PM), <https://www.finra.org/rules-guidance/key->

relevant and informative to examine statistics that focus on the process of expungement. Despite FINRA’s intent that expungement be an extraordinary remedy, a majority of expungement requests—58 percent—were granted during customer arbitration.<sup>5</sup> Moreover, an overwhelming majority of straight-in requests for expungement—84 percent—were granted.<sup>6</sup> These numbers show that expungement is not an extraordinary remedy as intended; it has become quite commonplace when requested by an associated person.

This routine cleansing of broker records has a harmful effect on the investing public. Because the Clinic and retail investors rely on the critical nature of the information available on tools like BrokerCheck and the firm’s Form CRS, the Clinic supports all efforts to increase the accuracy and reliability of brokers’ disciplinary histories available to investors. Investors, including many of the Clinic’s clients, may inaccurately rely on the publicly available records of a broker with expunged customer claims that no longer appear on BrokerCheck or Form CRS.<sup>7</sup> In addition to expressing support for the new proposed rules preserving the integrity of the expungement process, the Clinic also advocates for the continued strengthening of that process in customer-related, simplified arbitrations. This rule directly affects the Clinic’s clients who are investors with small claims that are often decided through a simplified arbitration.

## **I. Bifurcated Expungement Hearings in Arbitration Cases**

### **a. Named Associated Persons’ Requests for Expungement During Simplified Arbitration**

The Clinic supports FINRA’s new proposed rule requiring the arbitrator to bifurcate the arbitration hearing from the expungement-only hearing in “on the papers” and special proceedings when the associated person requests expungement, or when members firms request expungement on behalf of an associated person. Deciding the customer dispute before the expungement minimizes delays in customer recovery and still allows the arbitrator to make a more fully developed record before deciding the expungement request.

However, the current proposed rule for simplified customer-related arbitrations permits named associated persons to file a straight-in request for expungement, rather than requiring

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topics/expungement#:~:text=A%20firm%20or%20a%20broker%20may%20initiate%20a,award.%20FINRA%20has%20no%20part%20in%20the%20decision.

<sup>5</sup> Notice of Filing a Proposed Rule, *supra* note 1, at 50191.

<sup>6</sup> *Id.*

<sup>7</sup> See, e.g., *SEC Regulation Best Interest and Form CRS: What You Need to Know*, FINRA (Sept. 1, 2022, 9:42 AM), <https://www.finra.org/investors/insights/sec-regulation-best-interest-and-form-crs-what-you-need-know> (explaining that information on the Form CRS about the whether the firm or its investment professionals have reportable disciplinary history is intended to facilitate discussions between the customer and the broker regarding the relationship).

them to request expungement during the simplified arbitration case.<sup>8</sup> This suggested procedure, which only applies in simplified cases, makes an unnecessary distinction between simplified and non-simplified proceedings. The new rules for requesting expungement in simplified cases should mirror those for non-simplified cases: A named associated person *must* request expungement during the arbitration of the customer’s claim.

FINRA’s proposed new rules allow associated persons to file straight-in expungement requests after the conclusion of a simplified arbitration because FINRA believes that the expedited nature and limited discovery process warrants the option to seek expungement separately and in front of a three-person randomly selected panel from the Special Arbitration Roster.<sup>9</sup> However, the only difference between an expungement hearing that is bifurcated from, but decided within, the simplified hearing versus an expungement hearing held in front of a three-person panel from the Special Arbitration Roster is that the bifurcated hearing would be in front of a single arbitrator.<sup>10</sup> This difference would not change the likely outcome of the expungement hearing. As the SEC notes in its request for comments, where members sought disclosures during a non-simplified or simplified customer arbitration, “a similar percentage of [expungement] requests were awarded by a one-person panel . . . as were awarded by a three-person panel.”<sup>11</sup> And, by holding a separate expungement hearing within a simplified arbitration case, the arbitrator could request from the associated person and the firm “any documentary, testimonial or other evidence that the [arbitrator] deems relevant to the expungement request.”<sup>12</sup> Because the arbitrators in simplified arbitrations are “experienced public arbitrators” who have “the same enhanced expungement training as the arbitrators on the Special Arbitrator Roster,” the arbitrator in a simplified arbitration case would have the appropriate training to request any documents and testimony needed to make an informed decision on the merits of the expungement request.<sup>13</sup>

Permitting a named associated person the option to file a straight-in expungement request in a simplified customer-related arbitration, therefore, is not necessary because the arbitrator would obtain from the associated person and the firm any relevant evidence that the parties did not present during the arbitration. In other words, the named associated person and the firm would still have a fair opportunity to present their evidence to a trained, qualified arbitrator. Requiring notice of the associated person’s request for expungement in the manner contemplated

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<sup>8</sup> See Proposed Rule 12800(d)(1)(A) (“An associated person named as a respondent in a simplified investment-related, customer-initiated arbitration *may* request expungement during the arbitration of the customer dispute information associated with the customer’s statement of claim . . . .”) (emphasis added).

<sup>9</sup> Notice of Filing a Proposed Rule, *supra* note 1, at 50187.

<sup>10</sup> See *id.* at 50187–88.

<sup>11</sup> *Id.* at 50191.

<sup>12</sup> See Proposed Rule 12805(c)(6) and 13805(c)(7).

<sup>13</sup> See Notice of Filing a Proposed Rule, *supra* note 1, at 50187–88.

by Proposed Rule 12800(d)(1)(B) would also encourage participation by the customer in the expungement hearing following the close of arbitration because (1) it would be closer in time to the complained-about conduct and therefore easier for the customer to recall the facts and (2) it would give the customer the opportunity to prepare testimony or preserve documents to oppose expungement.<sup>14</sup> Thus, having a uniform system for expungement requests would further FINRA's and the SEC's goal of increasing the accuracy and reliability of the information available to securities regulators and investors on the CRD and BrokerCheck.<sup>15</sup> Although simplified arbitrations typically concern smaller dollar amounts, these losses are incredibly harmful to the Clinic's low-income clients. Because the harm caused by brokers in such cases can have devastating consequences for investors, and the proposed Rule's goal is to encourage investor participation in the expungement process, the rules for simplified arbitration proceedings should follow those for requesting expungement in non-simplified arbitrations.

#### **b. Member Firms' and Associated Persons' Opportunities for Gaming the System**

The Clinic supports FINRA's efforts to curb the incidence of "arbitrator shopping." By explicitly prohibiting the named associated person from withdrawing a request for expungement during arbitration and refile it as a straight-in request, associated persons can no longer have "two bites of the apple" in deciding who hears their expungement requests. This proposed change serves to increase the fairness of the system and confidence of the investing public.

However, firms and associated persons also participate in a second kind of gamesmanship: consolidated requests for expungement. The current Industry Code does not offer effective limits as to the hearing location in which associated persons must file their request by allowing that: "Before arbitrator lists are sent to the parties under Rule 13403, the parties may agree in writing to a hearing location other than the one selected by the Director."<sup>16</sup> The "parties," in the instance of a straight-in request are the associated person and the member firm, whose interests often align. Thus, as permitted by the rules, a pattern has emerged whereby associated persons consolidate many customer-related disputes into one expungement request filing it in a jurisdiction completely unrelated to the underlying claims. This allows brokers to file expungement requests in hearing locations with arbitrator pools that the brokers deem more

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<sup>14</sup> While recognizing the burden that filing expungement requests to preserve the opportunity to expunge would impose on associated persons, arbitrators, and the DRS arbitration forum, the burden is outweighed by the potential benefit of having customer input for the arbitrators to consider when deciding expungement requests. *See id.* at 50175.

<sup>15</sup> *See id.* at 50170–71.

<sup>16</sup> FINRA Rule 13213(a)(2); FINRA Rule 13213(a)(1) provides that the Director "will generally select the hearing location closest to where the associated person was employed at the time of the events giving rise to the dispute," discouraging opposition from affected customers and state regulators in the case of requests for expungement of multiple disputes arising from conduct in different cities or states.

likely to grant expungement.<sup>17</sup> As a result, these “group requests” before expungement-friendly arbitrator pools increase the incidence of granted expungement requests. Despite the efficiencies of consolidating expungement requests, associated persons game the system by volume-filing multiple, unrelated requests in one action to sanitize their CRD in one quick proceeding. Such group expungement requests harm the investing public because this unfairly skews the probability that the arbitrators, even if randomly selected, will grant expungement.<sup>18</sup> The new proposed time limitations on filing straight-in requests will help to curtail abuses of this practice. The rule will limit the number of customer complaints an associated person can request to expunge to those that occurred in the last two or three years—rather than the last twenty or more. But firms and associated persons may still find opportunities to file consolidated expungement requests if additional measures are not taken to curtail this practice.

The Clinic therefore urges FINRA and the SEC to further investigate the prevalence of associated persons and member firms that request consolidated expungement hearings of unrelated customer complaints in hearing locations that bear no relation to the location of the alleged customer-related conduct. In addition to implementing new time limits on filing straight-in requests, the Clinic suggests that the Industry Code require that expungement requests in a consolidated claim be related in some way. If the Code required that the alleged conduct in the expungement request occurred in the same state and involved the same group of customers or investment products, then the arbitrator or panel deciding expungement would have a common

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<sup>17</sup> For example, PIABA found in a study that, between 2015 and 2018, the number of arbitrators who issued three or more expungement awards increased 6000%, and the three arbitrators most often selected granted expungement requests 95% of the time. Jason R. Doss & Lisa Bragança, The PIABA Found., 2019 Study on FINRA Expungements 4 (2019), <https://www.piaba.org/system/files/2021-05/REPORT%20-%20The%20PIABA%20Foundation%202019%20Study%20on%20FINRA%20Expungements.pdf>.

<sup>18</sup> See, e.g., Award, FINRA Office of Dispute Resolution, In re Springer v. UBS Fin. Servs., Inc., Arbitration No. 20-01606 (Jan. 8, 2021) [hereinafter Springer FINRA Award] (awarding expungement of seven customer complaints based largely on what was indicated on the customers’ account applications); Award, FINRA Office of Dispute Resolution, In re Davis v. UBS Fin. Servs., Inc, Arbitration No. 16-00164 (Sept. 27, 2016) (awarding expungement of three unrelated customer complaints based on UBS’s records and broker’s unchallenged characterization of customers’ financial information, risk tolerance, investment objectives, and experience); Award, FINRA Office of Dispute Resolution, In re Bobroff v. UBS Fin. Servs., Inc., Arbitration No. 18-00092 (Dec. 24, 2018) (granting expungement awards for three associated persons based on UBS records and brokers’ unchallenged characterization of customer’s testimony); Award, FINRA Office of Dispute Resolution, In re Glasman v. Prudential Equity Group, LLC, Arbitration No. 17-02461 (Mar. 8, 2013) [hereinafter Glasman FINRA Award] (consolidating expungement requests for twenty-one unrelated customer complaints and granting expungement for six of the customer complaints based on broker’s uncontroverted testimony); Award, FINRA Office of Dispute Resolution, In re Wilson v. J.B. Hanauer & Co., Arbitration No. 21-01365 (May 16, 2022) (granting expungement for four unrelated customer complaints at two different firms based, in two of the cases, on the broker’s unchallenged testimony).

set of facts upon which to deliberate. The Code should also require a nexus between the requested hearing location and the location of the complained-about conduct, even in cases where the parties agree on a hearing location. If the Code required the expungement hearing to take place in the state where the complained-about conduct occurred, for example, then customers and state regulators would have more incentive to participate.

## **II. The Proposed Rules Will Increase Customer Participation in Expungement Hearings**

Straight-in requests often decrease the chance that customers will participate in expungement hearings, enabling associated persons to obtain expungement without opposition. The proposed new rules include two important provisions that would address this problem by increasing the likelihood that a party representing the customer's—and the investing public's—interests is present at the expungement hearing: time limits for straight-in requests and automatic notification of state regulators regarding expungement requests.

First, by requiring that associated persons file straight-in requests for expungement within a certain amount of time after the closing of the dispute with the customer,<sup>19</sup> the proposed new rules make it more likely that customers participate in the expungement hearing. These time constraints would especially benefit the Clinic's many elderly and/or ill clients.<sup>20</sup> Moreover, requiring the associated person to file an expungement request closer in time to the alleged misconduct mitigates the risk of spoliation of evidence and increases the likelihood that the firm would still possess relevant documents and evidence.<sup>21</sup> Lastly, the time limits would provide a safeguard against associated persons filing one expungement request for several unrelated claims that happened many years apart.

Second, the proposed new rule requiring that FINRA notify state regulators about expungement requests<sup>22</sup> will help address the problem of unopposed expungement hearings. If a customer is not present at the hearing, then a state regulator could instead represent the interests of not only the specific customer, but also the investing public, including investors in the

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<sup>19</sup> See Notice of Filing a Proposed Rule, *supra* note 1, at 50193 (“[T]he proposed rule change would require an associated person to file a straight-in request within two years of a customer arbitration or civil litigation closing, or if there is no customer arbitration or civil litigation, within three years from the initial reporting of the customer complaint to the CRD system.”).

<sup>20</sup> See, e.g., Glasman FINRA Award, *supra* note 18, at 6 (explaining that many of the customers in the underlying complaints that the broker requested be expunged were deceased because so much time had passed).

<sup>21</sup> See, e.g., *id.* at 7, 9 (explaining that since the majority of the complaints the broker requested be expunged were over twenty years old, none of the settlement agreements in the underlying claims were available for the arbitrator to review and the arbitrator had to rely heavily on the broker's testimony because documentary evidence was unavailable).

<sup>22</sup> See Notice of Filing a Proposed Rule, *supra* note 1, at 50185 (“The proposed rule change would require FINRA to notify state securities regulators . . . of an expungement request within 15 days of receiving an expungement request.”).

regulator's state.<sup>23</sup> There are many cases where a broker's expungement request goes completely unopposed, resulting in the arbitrator granting expungement without hearing any evidence or testimony on behalf of the customer. This proposed new rule will likely impact the outcome of these cases.

For example, in one case a broker, following a settlement of the claim by the brokerage firm, sought expungement of the disclosure.<sup>24</sup> After a hearing in which the customer did not participate, the arbitrator awarded expungement of the claim as well as an unrelated claim where the customer had died. The respondent party firms did not contest the request, and the arbitrator noted the prior settlement.<sup>25</sup> Despite hearing no testimony challenging the broker's assertions, the arbitrator found the underlying customer's claims "factually impossible or clearly erroneous" based on the customer's account application and the broker's characterization of a conversation between the customer and her son.<sup>26</sup>

Rubberstamped expungement cases such as this are not unique.<sup>27</sup> If this proposed rule had been in effect at the time, the state securities regulator would have known about the straight-in request, would have had the opportunity to investigate the facts, and then could have challenged the credibility of the broker's representations during the expungement hearing. Thus, had the proposed new rule been in effect, the arbitrator would have had the opportunity to weigh competing arguments to arrive at a more objective, informed, and fair decision, rather than reaching findings of fact based solely on the broker's uncontroverted testimony and evidence.<sup>28</sup>

For these reasons, the Clinic suggests that FINRA additionally consider notifying state securities regulators about bifurcated expungement hearings in simplified arbitrations. Allowing state regulators to participate in the separate, expungement-only hearings would increase the likelihood that the customer's interests are adequately represented without interfering with a claimant's presentation of their case-in-chief or raising concerns about confidentiality. It is imperative that FINRA also reduce the prevalence of unopposed expungement requests in simplified arbitration cases because even brokers who have small claims against them pose a high risk to investors with modest savings, such as the Clinic's clients.

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<sup>23</sup> *See id.* at 50186 (noting that the participation of state securities regulators may provide meaningful opposition to unopposed expungement requests, which would help develop the factual record used by the panel to decide the request).

<sup>24</sup> *See* Award, FINRA Office of Dispute Resolution, *In re Shawver v. Independent Fin. Grp., LLC, Merrill Lynch Pierce Fenner & Smith Inc.*, Arbitration No. 18-02665 (Feb. 6, 2019).

<sup>25</sup> *Id.* at 2–3.

<sup>26</sup> *Id.* at 4–5.

<sup>27</sup> *See, e.g.*, Springer FINRA Award, *supra* note 18 (awarding expungement of *seven* customer complaints based largely on what was indicated on the customers' account applications).

<sup>28</sup> *See* Notice of Filing a Proposed Rule, *supra* note 1, at 50186 (explaining that allowing state securities regulators to appear in otherwise unopposed expungement hearings would help develop a more complete factual record on which the arbitrators can rely).

### III. Conclusion

The Clinic is committed to protecting the savings of investors of modest means. For the reasons stated above, the Clinic strongly supports FINRA's efforts to strengthen the integrity of the expungement process so that the expungement remedy is only available under extraordinary conditions, as intended, and not as a matter of course. The accuracy and reliability of information available on the CRD, BrokerCheck, and Form CRS is crucial to protecting investors; thus, FINRA must ensure that claims are expunged from a broker's record only if that broker sufficiently proves the customer dispute information falls under the narrow circumstances prescribed by the rules.<sup>29</sup> Although the Clinic encourages FINRA to continue to monitor and strengthen the expungement process, FINRA's proposed new rules would improve the current system so that the spirit of this expungement policy is properly implemented. The Clinic thanks FINRA for the opportunity to comment on this important topic.

Respectfully,

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<sup>29</sup> See *id.* at 50173.