

March 21, 2019

Robert W. Cook
President and CEO
Financial Industry Regulatory Authority
1735 K Street NW
Washington, D.C. 20006

Dear Mr. Cook,

I am writing today regarding efforts by the Financial Industry Regulatory Authority (FINRA) to update the processes by which brokers can expunge customer dispute information from their records. As FINRA continues to consider changes to its expungement rules, I hope to draw your attention to recent research highlighting the need for smart broker expungement rules that ensure the availability of complete and transparent information about brokers.

FINRA and the broker disclosure system it regulates help protect the investing public. FINRA is an independent, self-regulatory organization that promotes “investor protection and market integrity” through regulation of the securities industry. FINRA oversees 3,700 financial firms and 630,000 individual brokers.¹ Broker-dealers and brokers are required to register with FINRA before engaging the public in securities transactions.² Registered brokers must comply with FINRA rules, pass qualification exams, and engage in continuing education programs to remain in good standing with the organization.

FINRA maintains a variety of records on individual broker dealers, some of which FINRA makes public in an effort to enhance transparency and protect investors. To register a broker with FINRA, financial firms must file a Uniform Application for Securities Industry Registration or Transfer (a “Form U4”), which includes information on the broker’s employment history and qualifications.³ When a registered broker leaves, or is terminated from, his or her job, firms must file a Uniform Termination Notice for Securities Industry Registration (a “Form US”), which includes information on the reasons for the broker’s termination.⁴

FINRA, along with state securities regulators, operates the Central Registration Depository (CRD), the “central licensing and registration system for the U.S. securities industry” that “contains ... the qualification, employment and disclosure histories” of brokers.⁵ The CRD houses information contained in Forms U4 and US. FINRA shares some of this information with the public through its BrokerCheck database. BrokerCheck records include details about brokers’

¹ FINRA, “About FINRA,” <http://www.finra.org/about>.

² FINRA, “Registration and Qualification,” <http://www.finra.org/industry/registration-qualification>.

³ FINRA, “Form U4: Uniform Application for Securities Industry Registration or Transfer,” <https://www.finra.org/sites/default/files/form-u4.pdf>.

⁴ FINRA, “Terminate an Individual’s Registration,” <http://www.finra.org/industry/terminate-individuals-registration>.

⁵ FINRA, “Central Registration Depository (WEB CRD),” <http://www.finra.org/industry/crd>.

credentials, qualifications, and employment records—including disclosures related to “customer disputes, disciplinary events, and certain criminal and financial matters.”⁶

Under current FINRA rules, registered broker dealers may take steps to expunge customer dispute information from their CRD records. These steps are outlined in Rules 2080, 12805, and 13805. Rule 2080 permits FINRA members to “expunge information from the CRD system arising from disputes with customers” by obtaining “an order from a court...directing such expungement or confirming an arbitration award containing expungement relief.”⁷ Courts and arbitration panels can grant expungement when “the claim, allegation or information” upon which the customer complaint is based “is factually impossible or clearly erroneous,” when the broker “was not involved in the alleged misconduct,” or “the claim, allegation, or information is false.”⁸ Rules 12805 and 13805 outline the hearing procedure that FINRA-appointed arbitrators must follow during expungement cases.⁹

FINRA has taken a series of steps in recent years to reform its expungement procedures to ensure that it only grants expungements in accordance with FINRA rules. In December 2017, FINRA offered new expungement regulations. Those new regulations built upon previous guidance by (1) obligating the broker seeking expungement to appear at his or her expungement hearing; (2) requiring that a three-person panel of arbitrators unanimously agree on the appropriateness of expungement; (3) limiting requests for expungement of customer dispute information to a one-year period; and (4) establishing a minimum filing fee for expungement requests, among other reforms.¹⁰ However, to date, FINRA has also not filed these proposals with the SEC, meaning the more lenient expungement rules are still in effect.¹¹

Meanwhile, in December 2018, the FINRA Board approved amendments to the FINRA rules to codify its Notice to Arbitrators and Parties on Expanded Expungement Guidance.¹² The Notice, first released in 2014 and updated in 2017, provides additional instruction and direction for arbitrators to consider when processing expungement requests. This guidance clarifies the role of arbitrators, affirms the importance of customers and counsel participation in hearings, and provides other expungement recommendations.¹³ However, FINRA has not yet filed this proposal with the Securities and Exchange Commission (SEC), meaning that the proposal is not yet in effect.¹⁴

⁶ FINRA, “About BrokerCheck,” <http://www.finra.org/investors/about-brokercheck>.

⁷ FINRA Rule 2080,

http://finra.complinet.com/en/display/display_viewall.html?rbid=2403&element_id=8468&record_id=11616&filtered_tag.

⁸ *Ibid.*

⁹ FINRA Rule 12805, http://finra.complinet.com/en/display/display.html?rbid=2403&element_id=7229; FINRA Rule 13805, http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=7230.

¹⁰ FINRA, “Regulatory Notice 17-42: Expungement of Customer Dispute Information,” December 6, 2017, https://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-17-42.pdf.

¹¹ See FINRA, “Rule Filings,” <http://www.finra.org/industry/rule-filings>.

¹² FINRA, “Update: FINRA Board of Governors Meeting,” December 21, 2018, <http://www.finra.org/industry/update-finra-board-governors-meeting-122118>.

¹³ FINRA, “Notice to Arbitrators and Parties on Expanded Expungement Guidance,” updated September 2017, <https://www.finra.org/arbitration-and-mediation/notice-arbitrators-and-parties-expanded-expungement-guidance>.

¹⁴ See FINRA, “Rule Filings,” <http://www.finra.org/industry/rule-filings>.

As FINRA continues to consider changes to its expungement rules, it is important that it consider the impact of expungements on FINRA's ability to protect investors. A recent analysis of FINRA expungement records found that expungement attempts are most often successful—yet are often associated with wrongdoing. Of the roughly 6,700 expungement attempts that took place between 2007 and 2016, 70% were successful.¹⁵ The study also found that “successful...and unsuccessful expungement attempts” by brokers “are a significant predictor of future misconduct,” and that “successful expungements increase recidivism.”¹⁶

These findings have significant implications for FINRA and its expungement process. In particular, the study suggests that FINRA's current method of assessing expungement requests—which approves the vast majority of expungements—is failing to safeguard information needed for investor protection. In addition, the study shows that the disclosure of both successful and unsuccessful expungement attempts provides important information for investors.

Given FINRA's crucial role in promoting safe markets and regulating the securities industry, it is of utmost importance that the organization consider the impact of broker expungement on the future misconduct of industry brokers. Therefore, I am requesting that you answer the following questions by April 4, 2019.

1. According to the recent analysis of FINRA expungement records, 70% of expungement attempts were successful from 2007-2016. In FINRA's view, what components of the existing process enable such high rates of expungement approvals? What steps does FINRA plan to take, if any, to assess whether such high rates of expungement are warranted?
2. The recent analysis of FINRA expungement records suggests that a broker's decision to request an expungement—whether or not that attempt is successful—is associated with future misconduct. Has FINRA considered disclosing broker expungement attempts on BrokerCheck or in the CRD? If not, why not?
3. What steps does FINRA take to ensure that arbitrators are adhering to the guidance provided in the Notice to Arbitrators and Parties on Expanded Expungement Guidance? Beyond codifying this guidance, does FINRA believe any other steps are necessary to ensure expungement is not granted inappropriately?
4. When does FINRA expect to submit its proposed rule changes related to the codification of the Notice to Arbitrators and Parties on Expanded Expungement Guidance to the SEC for approval?
5. When does FINRA expect to submit its new expungement regulations (Regulatory Notice 17-42) to the SEC for approval?

¹⁵ Notably, this success rate does not account for the hundreds of expungements labeled “unsuccessful” because the underlying claims against the broker were separately denied or dismissed, making the original expungement request moot.

¹⁶ Colleen Honigsberg and Matthew Jacob, “Deleting Misconduct: The Expungement of BrokerCheck Records,” November 2018, <https://www-cdn.law.stanford.edu/wp-content/uploads/2018/11/SSRN-id3284738.pdf>.

6. What additional efforts, if any, is FINRA considering to strengthen its expungement proceedings? In particular, has FINRA considered adopting a rule to govern the expungement of information that does not pertain to customer disputes (and therefore is not governed by Rule 2080)?

Sincerely,



Elizabeth Warren
United States Senator