

comments on the proposed rule change, as amended, from interested persons.

### **I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change**

NASD is proposing to adopt NASD Rule 2130 governing the expungement of customer dispute information from the Central Registration Depository ("CRD®" or "CRD system") and various internal guidelines to be adopted by NASD regarding the handling of requests to expunge customer dispute information from the CRD System. Below is the text of the proposed rule change. Proposed rule language is in italics.

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#### *2130. Obtaining an Order of Expungement of Customer Dispute Information from the Central Registration Depository (CRD System)*

*(a) Members or associated persons seeking to expunge information from the CRD system arising from disputes with public customers must obtain an order from a court of competent jurisdiction directing such expungement or confirming an arbitration award containing expungement relief.*

*(b) Members or associated persons petitioning a court for expungement relief or seeking judicial confirmation of an arbitration award containing expungement relief must name NASD as an additional party and serve NASD with all appropriate documents unless this requirement is waived pursuant to subparagraphs (1) or (2) below.*

*(1) Upon request, NASD may waive the obligation to name NASD as a party if NASD determines that the expungement relief is based on judicial or arbitral findings that:*

*(A) the claim, allegation or information is without factual basis;*

*(B) the complaint fails to state a claim upon which relief can be granted or is frivolous; or*

*(C) the information contained in the CRD system is defamatory in nature.*

*(2) If the expungement relief is based on judicial or arbitral findings other than those described above, NASD, in its sole discretion and under extraordinary circumstances, also may waive the obligation to name NASD as a party if it determines that:*

*(A) the expungement relief and accompanying findings on which it is based are meritorious; and*

*(B) the expungement would have no material adverse effect on investor protection, the integrity of the CRD system, or regulatory requirements.*

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### **II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change**

In its filing with the Commission, NASD included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. NASD has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

#### *A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change*

##### **1. Purpose**

The purpose of the proposed rule change is to establish procedures for expunging customer dispute information from the CRD system. The proposed rule will require all directives to expunge customer dispute information from the CRD system to be confirmed by or ordered by a court of competent jurisdiction. The proposed rule includes any such directives that may be in: (1) Judicial proceedings seeking expungement (including proceedings seeking expungement relief resulting from settlements in disputes between public customers and member firms or their associated persons in which the parties agree to expungement of customer dispute information as part of the settlement); (2) arbitration awards rendered in disputes between public customers and member firms or their associated persons in which the parties agree to expunge customer dispute information as part of the settlement and then present the settlement to the arbitration panel for inclusion in a stipulated award; and (3) arbitration awards issued after a decision on the merits.<sup>4</sup>

The proposed rule also will require member firms and associated persons seeking expungement to name NASD as an additional party in any judicial proceeding seeking expungement relief or confirming an arbitration award containing expungement relief. Under the proposed rule, NASD will participate in such judicial proceedings and generally will oppose expunging dispute information in such judicial proceedings unless the arbitrators or the

court have made specific findings that the subject matter of the claim or the information in the CRD system: (1) Is without factual basis (*i.e.*, is factually impossible or clearly erroneous); (2) fails to state a claim upon which relief can be granted or is frivolous; or (3) is defamatory in nature. NASD will retain discretion under the proposed rule not to oppose expungement relief in exceptional cases where the basis for the expungement does not fall within one of the three standards. NASD would exercise such discretion only if it determines that the expungement is meritorious and would have no material adverse effect on investor protection, the integrity of the CRD system or regulatory requirements.

The proposed rule will also permit member firms and associated persons to ask NASD to waive the requirement to name NASD as a party on the basis that the expungement order meets at least one of the standards for expungement articulated in the proposed rule. This will save members and NASD time and expense by enabling NASD to review the findings of the arbitrators or court and determine to waive participation in the judicial proceeding if NASD determines that the findings made by the arbitrators or the court meet at least one of the standards in the rule. If the expungement order fails to meet at least one of the standards in the rule, NASD will participate in the judicial proceeding and oppose the expungement.

Consistent with existing CRD policy, certain expungement directives will not be subject to the proposed rule. For example, NASD will continue to expunge certain information that is not customer dispute information, such as certain criminal information, pursuant to federal and state law. Also, NASD may execute, without a court order, an arbitration award rendered in a dispute between a member and a current or former associated person that contains an expungement directive in which the arbitration panel states that expungement relief is being granted based on the defamatory nature of the information.

The CRD system is an on-line registration and licensing system for the U.S. securities industry, state and Federal regulators, and self-regulatory organizations ("SROs"). The CRD system contains broker-dealer information filed on the Uniform Application for Broker-Dealer Registration ("Form BD") and the Uniform Request for Withdrawal from Broker-Dealer Registration ("Form BDW") and information on associated persons filed on the Uniform

<sup>4</sup> NASD Dispute Resolution will draft training materials for arbitrators and informational materials for parties regarding the standards under which customer dispute information may be expunged. No amendment to the Code of Arbitration Procedure is currently anticipated.