

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 subparagraph (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 *affirmative* judicial or arbitral findings that:

(A) the claim, allegation, or information is [without factual basis] *factually impossible or clearly erroneous*;

(B) the [complaint fails to state a claim upon which relief can be granted or is frivolous] *registered person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation, or conversion of funds*; or

(C) the [information contained in the CRD system is defamatory in nature] *claim, allegation, or information is false*.

(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.

(c) *For purposes of this rule, the terms "sales practice violation," "investment-related," and "involved" shall have the meanings set forth in the Uniform Application for Securities Industry Registration of Transfer ("Form U4") in effect at the time of issuance of the subject expungement order.*

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II. Summary of Comments and Response to Comments

A. Comments Received

As stated above, the Commission received 28 comments from a variety of sources.⁶ The majority of comments received were in favor of the NASD putting a rule in place on this topic, but had a variety of suggestions as to how to make the proposed rule text more

⁶ See Letter to Margaret H. McFarland, Deputy Secretary, Commission, from Charles W. Austin, Jr., Executive Vice-President, Public Investors Arbitration Bar Association (March 28, 2003) ("PIABA Comment"); letter to Secretary, Commission, from Joel A. Goodman and Stephen Krosschell, Goodman & Nekvasil, P.A. (March 29, 2003) ("G&N Comment"); electronic mail ("e-mail") to Secretary, Commission, from Barry D. Estell (March 28, 2003) ("Estell Comment"); letter to Secretary, Commission, from C. Thomas Mason III (March 31, 2003) ("Mason Comment"); letter to Jonathan G. Katz, Secretary, Commission, from Stuart J. Kaswell, Senior Vice President and General Counsel, Securities Industry Association (March 31, 2003) ("SIA Comment"); e-mail to Commission Rule Comments from Steven M. Sherman (March 31, 2003) ("Sherman Comment"); e-mail to Commission Rule Comments from Alan L. Sachs (March 28, 2003) ("Sachs Comment"); e-mail to Commission Rule Comments from Helen Mangano (March 28, 2003) ("Mangano Comment"); e-mail to Commission Rule Comments from John J. Miller (March 30, 2003) ("Miller Comment"); letter to Jonathan G. Katz, Secretary, Commission, from Gerald S. Siegmyer, Siegmyer, Oshman & Geddie, L.L.P. (April 7, 2003) ("SO&G Comment"); letter to Commission from Donald G. McGrath, McGrath & Polvino, PLLC (March 27, 2003) ("M&P Comment"); letter to Commission from A. Daniel Woska, Woska & Hasbrook (March 31, 2003) ("W&H Comment"); letter to Jonathan G. Katz, Secretary, Commission, from Dan Jamieson (April 25, 2003) ("Jamieson Comment"); letter to Commission from Kenneth R. Hyman, President, Partnervest Securities, Inc. (May 19, 2003) ("Partnervest Comment"); e-mail to Commission from Steven K. McGinnis (May 19, 2003) ("McGinnis Comment"); letter to Commission from Robert L. Hicks, President, Finance 500 (May 19, 2003) ("Finance 500 Comment"); e-mail to Commission Rule Comments from Robert Eastmann (June 3, 2003) ("Eastmann Comment"); letter to Margaret H. McFarland, Deputy Secretary, Commission, from Deborah Bortner, North American Securities Administrators Association CRD Steering Committee Co-Chair and Washington State Director of Securities (June 4, 2003) ("NASAA Comment"); e-mail to Commission Rule Comments from Tammy McQuade (June 7, 2003) ("McQuade Comment"); e-mail to Commission Rule Comments from Fired Broker (June 9, 2003) ("Fired Broker Comment"); e-mail to Commission Rule Comments from Mike Marchetta (June 10, 2003) ("Marchetta Comment"); e-mail to Commission Rule Comments from David Macias (June 10, 2003) ("Macias Comment"); e-mail to Commission Rule Comments from djs (June 10, 2003) ("djs Comment"); 23 substantially identical form letters to Commission from John Schooler, President, WFP Securities (May 21, 2003) ("Form Letter Comment"); e-mail to Commission Rule Comments from Richard Lavoice (July 29, 2003) ("Lavoice Comment"); e-mail to Commission Rule Comments from Steve Kus (July 2, 2003) ("Kus Comment"); e-mail to Commission Rule Comments from David Haburjak (July 8, 2003) ("Haburjak Comment"); and e-mail to Commission Rule Comments from Jim Aldendifer (October 12, 2003) ("Aldendifer Comment").

effective. The arguments put forth in the comments are summarized as follows.

Argument #1—The criteria adopted with respect to when the NASD will waive its involvement at the court confirmation level should be the criteria used by arbitrators for granting expungement. In short, rather than simply the criteria for NASD joining the court confirmation proceeding, the standards should be applied directly to arbitrators through the NASD's Code of Arbitration Procedures.⁷

Argument #2—Member firms and associated persons will be in a position to "buy clean records" through an arbitration award containing unwarranted expungement criteria that includes one of the three standards proposed.⁸

Argument #3—The standard for proving a defamation claim varies by jurisdiction and, in conjunction with the proposed standard language invoking defamation principles, the result will be confusion as to which law should be applied.⁹

Argument #4—An absolute or partial privilege exists for defamation claims that arise out of quasi-judicial proceedings (e.g., arbitration) in most jurisdictions, but not all. Thus, confusion could result from the lack of uniformity in this regard.¹⁰

Argument #5—Extensive collateral litigation will be required to resolve which jurisdiction's defamation standard should apply.¹¹

Argument #6—The proposal will cause a "chilling effect." Investors will be disinclined to bring any arbitration claims because of the near certainty that members and associated persons will raise defamation as a defense and counterclaim.¹²

Argument #7—The proposal will result in a "dispositive motions practice." The formal pleading requirements established by the proposal will give rise to an expensive and legally complex motions practice (thus defeating the main goal of arbitration—informal and inexpensive conflict resolution).¹³

⁷ See PIABA Comment and Mason Comment.

⁸ See PIABA Comment; G&N Comment; Estell Comment; Mason Comment; SO&G Comment; W&H Comment; and Jamieson Comment.

⁹ See PIABA Comment.

¹⁰ See PIABA Comment; G&N Comment; Mason Comment; Mangano Comment; and SO&G Comment.

¹¹ See PIABA Comment.

¹² See PIABA Comment; G&N Comment; Estell Comment; Mason Comment; Sachs Comment; Mangano Comment; Miller Comment; SO&G Comment; M&P Comment; and W&H Comment.

¹³ See PIABA Comment; G&N Comment; Estell Comment; Mason Comment; Sachs Comment; Mangano Comment; Miller Comment; SO&G Comment; M&P Comment; and W&H Comment.