

sufficiently responded to this argument through Amendment No. 2. As discussed at length above, the initial proposed rule text included language that tracked Federal practice pleading requirements. Such language, the commenters argued, could lead to a complex, lengthy, and expensive dispositive motions practice. By removing this potentially problematic language in Amendment No. 2, the Commission believes that the NASD has responded sufficiently to these concerns.

With respect to Argument No. 9, concerning the NASD's proposed rule text itself leading to an increase in expungements, the NASD disagreed. The Commission agrees with the NASD in that the proposed rule is clearly an improvement over the current expungement system in which there are no parameters placed on expungements being incorporated into arbitration awards.

With respect to Argument No. 13, concerning the NASD's inability to present serious opposition to expungement requests at the court confirmation level, the NASD provided some comfort. In Amendment No. 2, the NASD stressed that it is a federally registered self-regulatory organization that is required by the federal securities laws to enforce its rules.³⁵ Moreover, to the extent it fails in that regard, it must answer to the Commission. The Commission acknowledges that the extent to which the proposed rule will ultimately require the NASD to contest expungements at the court confirmation level cannot be divined. The Commission believes, however, that the proposal is an improvement over the current system for expungement. To the extent that the NASD's responsibilities at the court confirmation level ever became untenable, the Commission would expect the NASD to approach the Commission with a proposed rule change or in some way seek to alter the process to ensure that the NASD fulfills its self-regulatory obligations.

With respect to Argument No. 18, concerning the proposal's lack of respect for the arbitration process, the NASD responded in Amendment No. 2. The NASD noted that, rather than indicating a lack of respect for arbitration, the proposal demonstrates that the NASD is prepared to rely heavily on the fact-finding ability of arbitrators. Once an arbitrator makes an "affirmative determination" that one of the standards has been met, the NASD will waive its involvement at the court confirmation level. The Commission

believes that the proposal strikes the appropriate balance between providing arbitrators with sufficient flexibility in addressing issues, while at the same time placing appropriate parameters on the type of information that is potentially expungeable from the CRD system.

While Amendment No. 2 does not directly address Argument Nos. 12, 14–17, and 19–22, the Commission is not otherwise persuaded by these arguments. The Commission believes that the proposal strikes the appropriate balance between permitting members and associated persons to remove information from the CRD system that holds no regulatory value, while at the same time preserving information on the CRD system that is valuable to investors and regulators.

With respect to Argument No. 12, concerning the proposal's establishment of a privileged class of public records, the Commission is unconvinced. The Commission believes that, notwithstanding the state "public record" status of data in the CRD system, such data is expungeable under certain circumstances. Indeed, a process for the expungement of data from the CRD system has been in place since the establishment of the CRD system. The Commission also is not persuaded by this "states' rights" argument and notes that NASAA itself did not make this argument to the Commission.

With respect to Argument No. 14, concerning the rule's potential conflict with the states' books and records rules, the Commission is not persuaded. NASAA works closely with the NASD in the operation and enhancement of the CRD system. To the extent this is a valid concern of the states, the Commission would have expected NASAA to have raised this point. In fact, NASAA submitted a detailed comment letter on the proposal and did not raise this concern.

With respect to Argument Nos. 15 and 16, concerning a worsening of the already poor perception that investors have of the NASD arbitration process and of the integrity of CRD data, the Commission is not persuaded. These arguments appear to rely on the assumption that adopting explicit criteria for expungement will make expungement easier, compromise the process for expungement, and, ultimately, degrade the CRD system. As discussed at length above, the Commission believes that the proposal will have the opposite effect. Specifically, the Commission believes it will strengthen the expungement process, by ensuring that only information that is not valuable to

regulators and investors is expunged from the CRD system.

Argument Nos. 17 and 20–22 ostensibly relate to maintaining the accuracy of data that appears in the CRD system. Specifically, by making it more difficult to expunge information, the arguments aver, members and associated persons will be less likely and less able to expunge inaccurate information from the system—ultimately, degrading the system. The Commission appreciates these arguments and agrees that expungement of inaccurate information from the CRD system is crucial to the system's value. Further to that point, the Commission would clearly be opposed to any proposed rule that would place an unfair burden upon members and associated persons seeking to expunge inaccurate information from the system. The Commission, however, does not believe that the proposal will make expungement of *appropriate* information from the system overly or unfairly difficult. To the extent a member or associated person seeks to expunge *appropriate* information, the NASD should waive involvement at the court confirmation level. In such a circumstance, the process should function not unlike how it currently functions and should not require a significant rehearing of the issues and/or recalling of witnesses. The Commission believes that the proposal has been structured in such a way that the potential for divergent findings at the court confirmation level and the arbitration level has been minimized. In sum, the Commission believes that the proposal addresses the serious Commission concern that valuable information is being expunged from the CRD system through arbitration settlements that include negotiated expungement instructions.

Finally, with respect to Argument No. 19, asserting that the proposal should be acted upon in conjunction with NASD NtM 02–74, the Commission does not agree. The NASD is a registered national securities association and is owed a certain degree of latitude with respect to how it carries out its self-regulatory responsibilities. The Commission believes that the decision to file this proposal separately from the proposal that will follow from NtM 02–74 is the type of self-regulatory decision that the NASD has discretion to make. Moreover, NtM 02–74 has not yet been filed by the NASD and the Commission does not believe it would be in the interests of investors to delay the Commission's action on the instant proposal.

³⁵ See Section 19(g) of the Act, 15 U.S.C. 78s(g).