

Unpaid Arbitration Awards

The Case For An Investor Recovery Pool

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Acknowledgements²

Introduction / Executive Summary

“What dollars do you actually collect when somebody has done you harm? Because you can have a really strong standard, but if there are no dollars there, that’s a problem.”³

Those words, uttered by Jay Clayton, SEC Chairman, summarized the long-running problem underlying unpaid FINRA arbitration awards. Regardless of how strong the investor protection rules, regulations, and laws are, they are meaningless absent an investor’s ability to actually recover money when those rules, regulations, and laws are violated. Investors who fall prey to financial advisor misconduct all too often fall victim to a second abuse: the inability to collect an arbitration award issued against the financial advisor and/or firm found liable.

Chairman Clayton’s comments of one month ago address an old problem – one first raised seventeen years ago by the U.S. Government Accounting Office. Unfortunately, little has been done over the past two decades to address the problem. In

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² The Authors would like to thank Daniel Guernsey, and Andrew Zuckerman, of the University of Miami School of Law, and Valerie Hammel, of the St. John’s University School of Law, for their extensive efforts in analyzing the award history data, and broker registration data, utilized in this report. The students worked under the direction of the University of Miami School of Law Investor Rights Clinic Director Teresa Verges, and St. John’s University School of Law Securities Arbitration Clinic Director Christine Lazaro. Professor Lazaro is also PIABA’s executive vice president, and a member of its Board of Directors. Her help, as well as that of Michael Edmiston and Benjamin Edwards, in editing this Update is greatly appreciated by the Authors.

³ Crypto News, *Virtual Currencies: The Oversight Role of the U.S. Securities and Exchange Commission and the U.S. Commodity Futures Trading Commission*, YOUTUBE (Feb. 6, 2018), https://www.youtube.com/watch?v=NGgg_dXBpQo (SEC Chair Jay Clayton, testifying before the Senate Banking, Housing and Urban Affairs Committee).

2016, PIABA issued a report (the “PIABA Unpaid Awards Report”) which assessed the problem and offered potential solutions, including a national investor recovery pool (a “Pool”) to compensate those investors who otherwise would recover nothing.⁴ Almost two years later, on February 8, 2018, FINRA published a Discussion Paper (the “FINRA Discussion Paper”), a proposed rule, and updated statistics on unpaid awards. FINRA welcomed discussion on this long running problem, but did not indicate that it is pursuing any particular solution to the problem.

FINRA’s newly updated statistics indicated that, in the five years from 2012 through 2016, a total of 268 awards (27% of the cases where investors were successful) or \$199 million in awards (29% of total damages awarded to investors) have gone unpaid. PIABA studied the 2017 award data, and found that the trend continues: 36% of the investors who won their cases collected nothing, and 28 cents of each dollar awarded have gone unpaid. The data reveal that the problem is not fixing itself, and the steps taken by FINRA thus far have not effectively addressed the problem.

The problem is not a hypothetical one – it has meaningful effects on people from all walks of life. Bruce Wilkerson, a former NFL star, was harmed by a brokerage firm’s wrongful misconduct and awarded his full losses in arbitration. But, since the firm has gone under, Mr. Wilkerson has collected nothing and now must work far longer into his retirement years.

Of the potential solutions outlined by FINRA, several of which were previously discussed by PIABA, a Pool remains the viable and effective solution. FINRA is fully capable of funding the Pool out of fines levied on its members who violate its rules. FINRA member fines have been substantially larger than the unpaid awards for four of the last five years. Alternatively, a Pool could be funded from FINRA’s profits, or an assessment on its members. An annual assessment of between \$23 and \$120 per FINRA-registered broker would have covered the unpaid awards for the last five years. A Pool’s benefit to aggrieved investors would more than outweigh the modest cost to FINRA or its members. PIABA renews its call on FINRA to create such a Pool.

Background

The problem of unpaid awards was first addressed in the U.S. Government Accountability Office’s June 2000 report.⁵ Given the absence of publicly available data, the GAO conducted its own study. It surveyed a random probability sample of 247 of the 855 investors who received monetary awards in cases decided in 1998. Nearly all of the awards were from the NASD (FINRA’s predecessor) arbitration forum. Based on that sample, the GAO concluded that approximately 500 of the NASD awards to investors issued in 1998 were either unpaid, or only partially paid.⁶ It estimated that

⁴ See Hugh D. Berkson, *Unpaid Arbitration Awards, A Problem The Industry Created – A Problem The Industry Must Fix*, PIABA (Feb. 25, 2016), <https://piaba.org/piaba-newsroom/report-unpaid-arbitration-awards-problem-industry-created-problem-industry-must-fix>.

⁵ *Securities Arbitration: Actions Needed to Address Problem of Unpaid Awards*, U.S. GAO (June 26, 2000), <https://www.gao.gov/products/GGD-00-115>.

⁶ See *id.*

64% of NASD awards were unpaid in 1998.⁷ The GAO also presented an estimate of the dollar amount of the unpaid awards: \$129 million.⁸ Unsurprisingly, the GAO found that the larger awards were less likely to be paid: 44% of the awards under \$100,000 were paid in full while only 5% of the awards in excess of \$1.15 million were paid in full.⁹

The GAO made several recommendations, including that the SEC: “require NASD to adopt procedures for monitoring the payment of arbitration awards;” “develop and publicize information to focus investor attention on the possibility of unpaid arbitration awards;” and, “require NASD to develop procedures addressing the problem of unpaid awards caused by failed broker-dealers to help reduce costs and increase options for investors.”¹⁰ In addition, the GAO recommended that the SEC “periodically examine the extent of nonpayment of SRO arbitration awards to determine the effectiveness of actions taken to improve the payment of awards.”¹¹ The GAO stated that the SEC “should establish a process to assess the feasibility of alternative approaches to addressing this problem,” to the extent unpaid awards remain a problem.¹²

Over the next fifteen years, FINRA did not publicly disclose data relating to the number and dollar amount of awards that went unpaid, thwarting any independent analysis of the problem. In 2013, FINRA disclosed a portion of unpaid award data for 2011 to the Wall Street Journal, but did not offer any additional contextual information.¹³ FINRA simply disclosed that “\$51 million of arbitration awards granted in 2011 remain unpaid. That is 11% of the total awards that year, compared with the unpaid levels of 4% for 2010 and 2009.” No further context or methodology was provided for FINRA’s calculations.¹⁴ In 2015, FINRA provided unpaid award data for 2013 to its Dispute Resolution Task Force, which was made publicly available when the Task Force filed its report.¹⁵ The Task Force reported that, in 2013, “FINRA issued arbitration awards in 539 investor cases, of which 75 were not paid. The amount of damages awarded and not paid in these cases total \$62.1 million.”¹⁶

In 2016, PIABA issued its Unpaid Awards Report. Using the figures disclosed in the 2015 Task Force Report, PIABA recreated the data, and placed it in further context. PIABA found that one out of three awards went unpaid; and nearly 25% of the total amount awarded to investors went unpaid.¹⁷ Just hours before PIABA’s report was

⁷ See *id.*

⁸ See *id.*

⁹ See *id.*

¹⁰ *Id.*

¹¹ *Id.*

¹² *Id.*

¹³ See Jean Eaglesham and Rob Barry, *More than 5,000 Stockbrokers From Expelled Firms Still Selling Securities*, WALL ST. J., Oct. 4, 2013.

¹⁴ See *id.*

¹⁵ *Final Report and Recommendations of the FINRA Dispute Resolution Task Force*, FINRA DISPUTE RESOLUTION TASK FORCE (2015), <https://www.finra.org/sites/default/files/Final-DR-task-force-report.pdf>.

¹⁶ *Id.* (FINRA noted that the statistics did not include 19 unpaid awards that were the subject of judicial motions to vacate.)

¹⁷ PIABA did request more detailed data directly from FINRA, but was told that “compiling the data would require a great deal of staff resources and time,” and that it would take months to determine whether

made public, the Wall Street Journal again reported on unpaid awards, citing FINRA as its source, stating that in 2014, unpaid awards totaled more than \$34 million, which represented “15% of the total awards granted that year.”¹⁸

FINRA’s newly released comprehensive unpaid award data for the five year period from 2012 through 2016 puts the problem into focus. The table below summarizes FINRA’s data:

Summary of FINRA’s Unpaid Award Data 2012-2016

Year Award Issued	# Cases Awarded Damages	# Cases with Unpaid Awards	% Cases Awarded Damages that are Unpaid	Total Amount Awarded	Total Unpaid Award Amount	% Award Amount Unpaid
2012	255	76	30%	\$109,000,000	\$51,000,000	47%
2013	212	62	29%	\$181,000,000	\$75,000,000	41%
2014	177	44	25%	\$66,000,000	\$33,000,000	50%
2015	190	42	22%	\$203,000,000	\$26,000,000	13%
2016	158	44	28%	\$119,000,000	\$14,000,000	12%

In addition to FINRA’s newly released data, PIABA reviewed the arbitration awards issued in 2017, and determined that investor awards totaled \$73,280,880.¹⁹ PIABA then determined that \$20,649,164 of those awards were issued against brokers or firms which were no longer registered, a characteristic making it probable that the awards went unpaid.²⁰ Using this rule of thumb, PIABA concluded that 35.92% of

additional data would be made available. However, FINRA did make additional data available to the Wall Street Journal at about this same time.

¹⁸ Jean Eaglesham, *Arbitration Awards Against Stockbrokers Go Unpaid*, Wall St. J., Feb. 25, 2016.

¹⁹ PIABA has not included awards that have been the subject of vacature motions.

²⁰ In anticipation of drafting this report, and in the absence of data from FINRA, PIABA spent considerable time pulling every award issued in 2016 and 2017. FINRA has since reported the 2016 unpaid award experience, but the authors thought it important to describe the methodology used in PIABA’s analysis of the 2017 data.

All awards were pulled, and investor cases were then isolated for analysis and grouped into four categories: (1) those in which no respondent was suspended by or expelled from FINRA membership; (2) those in which all respondents were suspended by or expelled from FINRA membership; (3) those for which a motion to vacate the award was filed in court after the rendering of the award; and, finally (4) those in which some of the respondents were suspended/expelled and some were not.

FINRA promptly revokes the registration for respondents who fail to pay arbitration awards. With that in mind, if no respondent was expelled or otherwise lost its FINRA membership, we considered that award paid. If all the respondents were expelled, we considered that award unpaid. If only some of the respondents were expelled, we attempted to determine whether any collectible respondents remained. If there appeared that at least one collectible defendant maintained its FINRA membership, we considered

investor awards went unpaid (51 of 142 investor arbitration awards) and 28.18% of the dollars awarded to investors in 2017 were unpaid. PIABA anticipates these figures will be substantially similar to FINRA's official statistics for 2017, when those statistics are published.

Concerns about the Unpaid Award Problem

Shortly after PIABA released its Unpaid Awards Report, FINRA's then-CEO, Richard Ketchum, testified before a Senate subcommittee on Capitol Hill. When questioned by Senator Warren on the topic of unpaid awards, he acknowledged that "Something should be done about it."²¹ Senator Warren continued her questioning and Ketchum offered the following: "We are looking at whether, one way or another, there should be a fund to try to at least address the small investors that are terribly harmed."²²

The Securities Industry and Financial Markets Association ("SIFMA"), described as "the voice of the U.S. securities industry,"²³ has also expressed its consternation over the availability of data related to unpaid awards. While SIFMA's principal concern appears to lie with brokers who are unable to repay the loans their firms made to them, the securities industry's trade group has suggested that FINRA publish and track annual data on unpaid arbitration awards.²⁴ Specifically, SIFMA stated that FINRA should publish the total number of cases in which claimants won awards, the total dollar amount of those awards, the total number of awards paid, and the total amount of the awards paid.²⁵ FINRA responded to SIFMA's concerns, with the statement that it had heard the industry's concerns "loud and clear," and was considering the best course of action.²⁶

Since PIABA published its Unpaid Awards Report, FINRA made some efforts to address concerns related to unpaid awards. For example, FINRA discussed unpaid arbitration awards at its May 2017 Board meeting.²⁷ The FINRA Board authorized the publication of a Regulatory Notice seeking comment on proposed arbitration rule changes that would allow an investor to pursue claims in court, rather than arbitration, when a member firm becomes inactive during a pending arbitration, or when a broker became inactive before or during an arbitration proceeding. The Board also discussed other changes to the arbitration rules that would increase the options available to

that award paid (even though that respondent may have only paid the portion of the award attributable to it, and the balance of the award remained unpaid). Finally, we ignored all awards that were the subject of motions to vacate since no payment would be due while the award was under appeal. PIABA considered this the most conservative approach to the analysis.

²¹ Ann Marsh, *FINRA May Create Fund for Unpaid Arbitration Awards*, FINANCIAL PLANNING (Mar. 16, 2016), <https://www.financial-planning.com/news/finra-may-create-fund-for-unpaid-arbitration-awards>.
²² *Id.*

²³ See generally SIFMA, www.sifma.org (SIFMA's home page).

²⁴ Rita Raagas De Ramos, "Unpaid Finra Arbitration Awards are a Big Problem," Financial Advisor (Nov. 8, 2017), available at: <https://financialadvisoriq.com/c/1781883/208993>.

²⁵ See *id.*

²⁶ See *id.*

²⁷ Update: *FINRA Board of Governors Meeting*, FINRA (May 11, 2017), <http://www.finra.org/industry/update-finra-board-governors-meeting-051017>.

investors if a firm or broker became inactive during the arbitration process like, for example, permission to amend pleadings to name additional parties.²⁸ The Board additionally approved a change to the Form U4 to elicit information regarding brokers who did not pay arbitration awards, settlements, or judgments in full. In October 2017, FINRA finally issued the Regulatory Notice seeking comment on those proposed changes to the arbitration rules.²⁹

FINRA's measures called for greater transparency regarding associated persons who had not fully satisfied awards, settlements, or judgments; and provided investors with certain options if a broker or firm became inactive during the arbitration process. The measures did not, however, provide any relief to investors who went through the entire process and were given an award that went unpaid and therefore became worthless. The Board closed the "Unpaid Arbitration Awards" section of its May 2017 Board Meeting Update with the statement: "The Board also discussed additional steps to address unpaid arbitration awards that will be considered at a subsequent Board meeting."³⁰ No detail was provided, and no mention of *any* potential cure (i.e., increased net capital requirements, insurance requirements, or a national investor recovery pool) was made.

FINRA once again discussed "unpaid arbitration awards" at its July 2017 Board meeting; however, there appears to have been no discussion of any steps to get investors recovery if an award went unpaid. FINRA did focus on the "cockroaching" problem, looking to scrutinize more closely asset transfers that left behind a significant number of pending arbitration claims, unpaid arbitration awards, or settlements.³¹ In February 2018, FINRA filed a Regulatory Notice seeking comment on these proposed changes to the membership rules.³²

FINRA has reason to focus on these issues: unpaid awards undercut FINRA's legitimacy as a self-regulatory organization credibly committed to investor protection. Self-regulation works best when the industry bears the costs of industry misconduct. When the industry internalizes the costs of misbehavior, it is incentivized to police its own ranks efficiently. If the industry does not internalize the true cost of misbehavior and instead allows arbitration awards to go unpaid, FINRA itself may not be incentivized to devote sufficient resources to address the issue.³³ Conceptually, each

²⁸ See *id.*

²⁹ See FINRA Regulatory Notice 17-33, *Amendments to the Code of Arbitration Procedure for Customer Disputes to Expand the Options Available to Customers if a Firm or Associated Person Is or Becomes Inactive*, FINRA (Oct. 2017), <http://www.finra.org/industry/notices/17-33>.

³⁰ *Update: FINRA Board of Governors Meeting*, FINRA (May 11, 2017).

³¹ "Cockroaching" is the term commonly used to describe a situation in which a brokerage firm gets in trouble thanks to the improper conduct of its brokers and those supervising them. The firm is shut down, and the brokers scurry to find employment at other firms.

³² See FINRA Regulatory Notice 18-06, *FINRA Requests Comment on Proposed Amendments to Its Membership Application Program to Incentivize Payment of Arbitration Awards*, FINRA (Feb. 2018), <http://www.finra.org/industry/notices/18-06>.

³³ See Edwards, Benjamin, *The Dark Side of Self-Regulation* (September 14, 2016). UNIVERSITY OF CINCINNATI LAW REVIEW, Forthcoming. Available at SSRN: <https://ssrn.com/abstract=2829592> or

unpaid award is an instance where FINRA failed to fully achieve its stated investor protection mission.

Initiatives To Promote Payment

FINRA's efforts to date focused on increasing investor awareness of the potential for an unpaid award, as well as increasing investor litigation options if there is an increased likelihood of an unpaid award. Unfortunately, FINRA continues to avoid addressing the GAO's recommendation to improve award payments themselves if unpaid awards remained a problem. Based on FINRA's own data, the problem has continued.

FINRA's Discussion Paper identifies three possible initiatives to discourage unpaid awards: greater disclosure on the firm's Form BD, changes to the "statutory disqualification" definition, and Bankruptcy Code changes.³⁴ PIABA encourages all efforts to promote broader disclosure of unpaid awards. PIABA also supports the efforts to end the practice of brokers moving from firm to firm to avoid the import of significant complaints against them and unpaid awards from their former firms. There is a meaningful problem of the concentration of brokers with a long history of complaints concentrating in certain firms, raising the risk for *all* customers of those firms.³⁵

Greater disclosure, while a good thing in the abstract, will not incentivize brokers and firms who are no longer registered to pay outstanding arbitration awards. PIABA applauds FINRA's focus on recidivist brokers, and its suggestion to strengthen its member rules to ensure principals are held accountable for the misconduct of failed firms. However, more must be done to ensure investors actually collect when somebody has done them harm.

Helping Investors Victimized By Industry Misconduct Recover

The PIABA Unpaid Awards Report spent considerable time addressing a number of possible remedies to the unpaid award problem: expanding SIPC coverage, increasing net capital requirements, imposing insurance requirements, and/or creating an investor recovery pool. FINRA's Discussion Paper addressed each of these, but did not discuss any in detail, and failed to make any recommendation as to the viability of any option.

Expanding SIPC:

<http://dx.doi.org/10.2139/ssrn.2829592> ("When contractual relationships do not transfer the costs of misbehavior back to the industry, this incentive to self-police diminishes").

³⁴ *Discussion Paper – FINRA Perspectives on Customer Recovery*, FINRA (Feb. 8, 2018), http://www.finra.org/sites/default/files/finra_perspectives_on_customer_recovery.pdf.

³⁵ See Craig McCann, Chuan Qin, and Mike Yan, *How Widespread and Predictable is Stock Broker Misconduct*, SLCG (2016),

<http://www.slcg.com/pdf/workingpapers/McCann%20Qin%20and%20Yan%20on%20BrokerCheck.pdf>.

Both PIABA and FINRA noted that SIPC, as it is currently statutorily constructed, does not have the power to combat fraud, or to address investment losses from negligence. Rather, its mission is to ensure that investors do not lose securities from their accounts when the brokerage firms holding those accounts close.³⁶ What FINRA's Discussion Paper did *not* note, however, is the problem associated with the concern that SIPC's fund is in constant jeopardy of depletion. SIPC has long been criticized for its refusal to pay investor claims.³⁷ It is unlikely SIPC will adequately address the problem of unpaid awards.

Insurance:

The FINRA Discussion Paper identifies "other insurance options" as a possible remedy to unpaid awards. FINRA simply states that insurance could be required, perhaps in the form of commercial insurance products or a captive insurance program. What FINRA's Discussion Paper omits, and what PIABA pointed out in its Unpaid Awards Report, is the fact that FINRA has gone on record a number of times stating that insurance is too expensive and is therefore not a viable option. FINRA also fails to address fundamental coverage issues: specifically, that intentional fraud cannot be covered by insurance. Thus, fraud, selling away, and Ponzi schemes would be nearly impossible to cover under insurance policies.³⁸ While insurance requirements would offer investors some additional protections, it is unlikely required insurance will solve the problem of unpaid awards.

Investor Recovery Pool:

PIABA spent considerable time discussing the details of a Pool in its Unpaid Awards Report. Now, two years later, FINRA indicates that a Pool is one possible remedy. In its Unpaid Awards Report, PIABA discussed possible ways to structure a Pool and addressed concerns that would likely be raised about a Pool. Of the options PIABA and FINRA have set forth, a Pool is the most viable option available to address the payment of awards. Accordingly, PIABA again recommends that FINRA establish a Pool.

Funding A Pool

Investors who have taken their cases all the way through the arbitration process, won at their arbitration hearing, confirmed their awards with a court of competent jurisdiction, and have been unsuccessful in their collection efforts would be entitled to a recovery from a Pool, after assigning the unpaid award to the Pool. These steps address the main objections to a Pool; that specious claims would be made and paid, and that firms would be incentivized to walk away from pending claims without any fear of being held responsible for those claims.

³⁶ See generally SIPC, <http://www.sipc.org/about-sipc/sipc-mission>.

³⁷ See PIABA Unpaid Awards Report at 12 – 14 (contains more detailed discussion of the issues associated with SIPC coverage).

³⁸ See *id.* at 19 – 21 (contains a full discussion of the issues surrounding an insurance remedy).

The question then arises: how would a Pool be funded? There are three ready sources to fund a Pool. They are, in decreasing order of appeal: FINRA's fines levied against its rule-breaking members; FINRA's profits; and, an assessment made against *all* FINRA members. Each of these options is addressed below.

The most appealing source of funds for a Pool is the fines FINRA levies against its members who violate its rules. There is an undeniable logic to using the fines assessed against FINRA's bad actors to ensure that investors who fall victim to those violations are made whole. Focusing on the data available since PIABA's Unpaid Awards Report was released, the fines FINRA has collected are more than sufficient to fund a Pool. FINRA's report of unpaid awards and fines collected is summarized:

Year	Unpaid Awards (in millions)	Fines (in millions)
2014	\$33	\$132.6
2015	\$26	\$93.8
2016	\$14	\$173.8

The fines FINRA collected would have covered the unpaid awards, in full, sometimes by an order of magnitude.³⁹

FINRA is also capable of funding a Pool, and ensuring that every arbitration award is paid in full, simply out of its net profits. FINRA's report of unpaid awards and its annual net income is summarized:

Year	Unpaid Awards (in millions)	Net Income (in millions)
2014	\$33	\$129.0
2015	\$26	(\$39.5)
2016	\$14	\$57.7

FINRA's annual profits would have more than covered the unpaid awards for 2014 and 2016. While the SRO suffered a rare operating loss in 2015, the overwhelming profit from 2014 would have more than covered *all* the unpaid awards for 2014 through 2016. FINRA has not released its 2017 annual report, so PIABA is unable to determine whether it maintained a sufficient profit to cover the 2017 unpaid awards.

Finally, FINRA could fund a Pool with a modest assessment made on its members. FINRA boasts that more than 630,000 brokers are registered with the SRO.⁴⁰ Ignoring the administrative costs, a fee of \$23.24 per broker would ensure that a Pool covered every 2016 unpaid arbitration award. Turning to 2017, a fee of \$32.78 per broker would cover the unpaid arbitration awards. The highest amount of unpaid awards in the past five years was in 2013: \$75 million. Yet a fee of only \$119.05 per

³⁹ See *Statistics on Unpaid Customer Awards in FINRA Arbitration*, FINRA, <http://www.finra.org/arbitration-and-mediation/statistics-unpaid-customer-awards-finra-arbitration> (contains data concerning the unpaid awards); see also *Annual Reports & Financials*, FINRA, <https://www.finra.org/about/annual-reports-financials> (data concerning FINRA's fines levied against its members is found in its annual financial report).

⁴⁰ See *Statistics*, FINRA, <http://www.finra.org/newsroom/statistics>.

broker would cover that sum. Thus, based on the last five years of FINRA reported data, if FINRA chose to assess its brokers a fee to cover a Pool, that fee would not have exceeded \$120 per year, and could have been as low as \$23.25 per year.

While the Industry will undoubtedly claim it would be inequitable to force good brokers to pay for the wrongful conduct of bad brokers, the fact remains that the industry on the whole has chosen to require no safety net of any type thanks to its minimal net capital requirements and lack of insurance requirements for membership, leaving investors to bear the full risk of the industry's financial recklessness. A broker-funded Pool would serve to protect those investors where the industry has no other protection mechanisms.

Unpaid Awards Cause Real Harm to Investors

Investors suffering the dire effects of unpaid FINRA arbitration awards come from all walks of life. Take, for example, Bruce Wilkerson. Mr. Wilkerson, now 54 years old, is an accomplished former NFL player. After an All-SEC senior year at the University of Tennessee in 1986, he was drafted by the Los Angeles Raiders in the second round of the 1987 NFL Draft. He spent a decade playing football for the Raiders, the Jacksonville Jaguars, and the Green Bay Packers. After retiring from football, Mr. Wilkerson went to work as machinist at an Alcoa facility in Tennessee, where he has worked since.

Mr. Wilkerson trusted his hard earned life savings to his financial advisor, Robert A. Gist of Resource Horizon Group LLC. Gist gained Mr. Wilkerson's trust, and his investment portfolio, on the fraudulent pretense that he would invest conservatively in corporate bonds and other securities. In reality, Gist used the funds for a variety of improper purposes. He used Mr. Wilkerson's funds to pay his own personal expenses, to pay the expenses of a company he controlled, and to pay "dividends" and "proceeds" to other investors for false securities transactions he claimed to have made their behalf. In 2013, Gist entered into a \$5.4 million settlement with the SEC, after it alleged he converted funds from at least 32 investors.⁴¹

Mr. Wilkerson filed an arbitration claim against Resource Horizon for the actions of its broker, Gist.⁴² In March 2015, the arbitrators awarded Mr. Wilkerson his full

⁴¹ See SEC Litigation Release No. 22710, *Securities and Exchange Commission v. Robert A. Gist, et al.*, Civil Action No. 1:13-cv-01833-AT (N.D.Ga., May 31, 2013), <https://www.sec.gov/litigation/litreleases/2013/lr22710.htm>.

⁴² One of Resource Horizon's principals escaped being named in Mr. Wilkerson's arbitration claim thanks to her personal bankruptcy filing. That principal, Kelly Miller, settled one arbitration claim brought by a Gist victim, and lost an arbitration filed by another Gist victim. She filed for bankruptcy roughly one month after the arbitration award was issued against her. Immediately following Resource Horizons' closing, and contemporaneously with her bankruptcy filing, Miller joined Kovack Securities. Kovack Securities' principal, Brian Kovack, was elected to FINRA's Board of Governors later that year. In June of 2017, Reuters reported that 34% of Kovack Securities, Inc.'s brokers had a history of FINRA red flags See Benjamin Lesser and Elizabeth Dilts, *Wall Street's Self-Regulator Allows Safe Havens for Tainted Brokers* (June 12, 2017) <https://www.reuters.com/article/usa-finra-brokers/wall-streets-self-regulator-allows-safe-havens-for-tainted-brokers-idUSL1N1J91C3..>

losses of \$610,000, as well as other statutory damages.⁴³ Unfortunately, shortly before the award was issued, FINRA cancelled Resource Horizon's registration.⁴⁴ It turns out that it had already failed to pay another arbitration award related to the same misconduct affecting Mr. Wilkerson. No longer registered, Resource Horizon has failed to pay Mr. Wilkerson's award as well. Now 53 years old, Mr. Wilkerson, who thought he had smartly prepared for his golden years, has lost a substantial portion of his net worth. He will likely find himself working many years to make up those lost funds.

Conclusion

The landscape regarding unpaid arbitration awards remains largely unchanged since the GAO first addressed the issue in 2000. The publication of unpaid award data demonstrates that the figures are not improving. In 2013, nearly \$25 out of every \$100 awarded to investors went unpaid, and in 2017, more than \$28 out of every \$100 awarded to investors went unpaid. While 33 out of 100 investors who won their arbitrations in 2013 went unpaid, nearly 36 out of 100 investors who won their arbitrations in 2017 went unpaid.

While FINRA has stated it is "important to engage in a broader discussion with other regulators and policy makers, as well as other stakeholders in the issue, about investor recovery more generally,"⁴⁵ it is time for FINRA to take action. The best workable solution remains a simple one: a national investor recovery pool to be maintained and administered by FINRA. The SRO remains the best party to implement and maintain the system for several reasons: (i) it sets the standards for membership, including the financial responsibility required for its members; (ii) its members are the ones who are found to have engaged in the wrongdoing; (iii) it administers the arbitration system and has first-hand knowledge of the data generated by those arbitrations; and (iv) it is the one levying fines against its members for misconduct.

PIABA's call for the creation of a Pool remains unchanged since its 2016 Unpaid Awards Report. Unpaid awards must be verified, and there must be measures in place to ensure fraudulent claims against firms are not eligible for payment by a Pool. It must be designed to avoid the hoarding problem that SIPC suffers, and therefore exhaust its resources on an annual basis (aside from the funds needed for ongoing operations.) A Pool should be funded out of FINRA's fines it collects from its members, or FINRA's profits. Alternatively, a Pool should be funded by levying an assessment against each of FINRA's registered brokers.

PIABA welcomes FINRA's invitation to discuss this issue further, however, little has been done since PIABA outlined the scope of this problem in 2016. PIABA is encouraged that FINRA is seeking active engagement on this topic; however, FINRA has had decades to study this problem. Investors' experience collecting awards is not improving, and action must be taken without further delay. In the absence of any viable

⁴³ See *Wilkerson v. Resource Horizons Group LLC*, FINRA Case No. 14-00904 (Mar. 11, 2015).

⁴⁴ See Resource Horizons Group LLC's BrokerCheck Summary, <https://brokercheck.finra.org/firm/summary/104368>.

⁴⁵ FINRA Discussion Paper, at 19.

solution other than a national investor recovery pool, FINRA must be required to enact such a Pool either voluntarily or as a matter of legislative requirement.