

PIABA STUDY: STOCKBROKER ARBITRATION SLATES WIPED CLEAN 9 OUT OF 10 TIMES WHEN “EXPUNGEMENT” SOUGHT IN SETTLED CASES

Troubling Findings Raise Question: Are Investors Being Kept in the Dark About Arbitration Cases? Case in Point: One Financial Professional Gets Investors’ Claims Expunged 35 Out of 40 Times.

WASHINGTON, D.C. – October 16, 2013 – Investors who rely on public records to check out the background of their current or potential stockbrokers are, in many cases, unlikely to be getting a complete picture, according to a major Public Investors Arbitration Bar Association (PIABA) study of more than 1,600 arbitration cases over a recent five-year period. [The report is available at http://www.piaba.org](http://www.piaba.org).

In reviewing all securities arbitration awards in cases filed between January 1, 2007 and December 31, 2011 in which the word “expungement” appears, PIABA found that:

- An “alarmingly” high percentage of arbitration cases resolved by settlement or stipulated awards where expungement relief has been granted. For the time period January 1, 2007 through mid-May 2009, expungement was granted in 89 percent of the cases resolved by stipulated awards or settlement. (The May 2009 end date reflects a change in reporting requirements mandating more information about arbitration cases.)
- For the most recent time period mid-May 2009 through the end of 2011, expungement relief was granted in nearly every instance -- 96.9 percent of the cases resolved by settlements or stipulated awards.
- Some stockbrokers have taken a particularly aggressive approach to wiping their slate clean. One individual associated with a brokerage firm requested expungement 40 times, and arbitration panels granted such relief to that individual 35 times.

In the securities industry, the term “expungement” refers to the process by which an individual stockbroker licensed through the Financial Industry Regulatory Authority (FINRA), the industry self-regulatory organization, can seek to have removed from his or her public regulatory record any record of a complaint or complaints made by investors arising from the conduct of the broker. This Central Registration Depository information is typically accessed by the public through state securities offices and FINRA’s BrokerCheck program. For its data, PIABA used the main independent arbitration case tracking system maintained by the Securities Arbitration Commentator.

Attorney Scott Ilgenfritz, president, PIABA, and author of the expungement study, said: **“To say that ‘expungement’ of customer claims from broker records is a major investor protection problem is an understatement. The result is that investors who**

are diligent enough to seek out information about brokers may be getting a woefully incomplete picture of the individual to whom they will entrust all or most of their nest egg. What is supposed to be an extraordinary relief measure is now being sought and granted in roughly nine out of the 10 settled cases that we studied. This clearly indicates that the current expungement procedures are seriously flawed. Regulators need to step in and crack down on the granting of expungements, particularly in settled cases.”

Commenting on the report, Rachel Weintraub, legislative director and senior counsel, Consumer Federation of America (CFA), said: **“One of the key recommendations we make to investors is to check the record of anyone they are thinking of trusting with their money. Consumer Federation of America has worked to ensure that the information provided to investors is complete and accurate. But when it is too easy for brokers to get complaints expunged from their records, investors who attempt to do the right thing and check out the broker’s disciplinary record may end up making their decision based on incomplete information. Worse, they may be led to believe that a broker has a clean disciplinary record when that is far from true. This leaves investors vulnerable to fraud and abuse.”**

Attorney Jason R. Doss, incoming president, PIABA, said: **“The expungement process for stockbrokers in arbitration cases is clearly broken today and needs fixing. We have believed for some time now that expungements are a significant investor protection issue, but this new study from PIABA now documents precisely just how bad the situation is. This is not some technical legal issue; the consequences for the information relied upon by investors and investor confidence in the financial markets must be seen as paramount here. This situation simply cannot be allowed to go unaddressed.”**

WHY INVESTORS NEED THE FACTS

FINRA maintains the qualification, employment and disclosure histories of 5100 broker/dealers and approximately 660,000 of their securities employees in the electronic CRD system. FINRA and the North American Securities Administrators Association (NASAA) established the CRD system in 1981. For each associated person licensed by FINRA, the CRD system contains disclosure information with respect to the associated person having been named in a criminal matter, having been the subject of a regulatory disciplinary action, having been the subject of a civil judicial action, and having been the subject of an investor arbitration proceeding.

While the Securities and Exchange Commission (SEC) approved FINRA rules related to expungement, the federal oversight agency did so on the understanding that the granting of such relief would be an extraordinary remedy. As the SEC noted in 2008: “[T]he Commission believes that having accurate and complete information in the CRD is vital; information that has regulatory value or that could assist investors in protecting themselves should not be removed from CRD.”

In 2009, FINRA stated the following: “Accurate and complete reporting in CRD, including the reporting of required customer dispute information, is an important aspect of investor protection. The new procedures ensure that arbitrators have the opportunity to consider the facts that support or weigh against a decision to grant expungement. The procedures add transparency to the process and safeguards designed to ensure that the extraordinary relief of expungement is granted only under appropriate circumstances.”

RECOMMENDATIONS FOR CHANGE

As the PIABA study makes clear, what the SEC and FINRA intended to happen with expungement – that it is to be an extraordinary remedy – does not track with the liberal application of the process to wipe clean the slates of stockbrokers, particularly with respect to cases resolved by settlement. Arbitrators do not appear to appreciate the importance of the accuracy of disclosure information in the CRD system to investor protection.

One possible issue is that the training required by FINRA for arbitrators to be able to rule upon a motion seeking expungement relief is limited. Arbitrators must take an online training course, which takes approximately one hour, and pass a test concerning the materials included in the online training course. More and better training for arbitrators is needed, according to PIABA: “Changes need to be made with respect to the content and thoroughness of the training arbitrators are required to complete before they can rule upon a motion seeking expungement relief. Changes should also be made with respect to the procedures applicable to motions seeking expungement relief.”

According to Ilgenfritz, “FINRA has very recently undertaken steps to better educate arbitrators concerning their roles in the expungement process and the critical importance of accurate customer claims information with respect to investor protection. FINRA’s arbitrator education efforts need to go further, and FINRA needs to propose rule changes.”

Specifically, the PIABA report recommends the following: “FINRA needs to propose a rule change with respect to respondents and their counsel bargaining for in settlement negotiations or conditioning a settlement upon an investor’s agreement to not oppose expungement or an agreement to expungement.”

The report notes: “Finally, for FINRA to fulfill its mission of investor protection, the procedures applicable to motions for expungement relief need to be changed. FINRA needs to play a more active role in arbitrators’ rulings on motions for expungement relief. FINRA needs to review and critically assess all motions for expungement relief, particularly those made in cases resolved by settlement. FINRA also needs to review and critically assess settlement agreements. A proposed rule change should include the requirement that the hearing on any motion for expungement relief be scheduled no sooner than 60 days after service of the motion on the customer and FINRA. In cases

resolved by settlement, FINRA should require respondents to provide to FINRA the settlement agreement along with the motion for expungement relief.”

Outlining needed remedies, the report continues: “Upon receipt of any motion for expungement relief and any settlement agreement, FINRA should provide those documents to the securities commissioner for the state in which the case was filed. The amended procedures should provide for FINRA and the designee of the state securities commissioner to have the right to appear at the hearing on the motion for expungement relief and to oppose expungement relief when such opposition is appropriate.”

ABOUT PIABA

Public Investors Arbitration Bar Association is an international, not-for-profit, voluntary bar association of lawyers who represent claimants in securities and commodities arbitration proceedings and securities litigation. The mission of PIABA is to promote the interests of the public investor in securities and commodities arbitration, by seeking to protect such investors from abuses in the arbitration process, by seeking to make securities arbitration as just and fair as systemically possible, and by educating investors concerning their rights. For more information, go to www.piaba.org.

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EDITOR’S NOTE: A streaming audio replay of the news event will be available on the Web at <http://www.piaba.org/> as of 5 p.m. EDT on October 16, 2013.