

PIABA AND THE PIABA FOUNDATION

2021 UPDATED STUDY ON FINRA EXPUNGEMENTS

**A SERIOUSLY FLAWED PROCESS
THAT SHOULD BE FIXED NOW
TO PROTECT THE INTEGRITY OF THE PUBLIC RECORD**

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On Behalf of PIABA and The PIABA Foundation



ABOUT THE GROUPS AND ACKNOWLEDGMENTS

The Public Investors Advocate Bar Association is an international bar association whose members represent investors in disputes with the securities industry. Currently, there are members from 44 states, Puerto Rico, and Japan. The mission of PIABA is to advocate for equal access to justice for investors in all forums. PIABA works to promote fairness in the rules governing dispute resolution for investor claims against securities and commodities brokerage firms, registered investment advisory firms, and their associated representatives. PIABA also works toward creating, improving, and enforcing statutes, rules, regulations, case law, and policies designed to promote investor rights and to prevent misconduct by those who sell investments to the public. www.piaba.org @piabanews

The PIABA Foundation is a 501(c)(3) charitable organization that was formed in 2012 by attorneys who are devoted to representing investors in disputes with brokers and brokerage firms in FINRA arbitrations. The Foundation's mission is to promote investor protection through investor education. The Foundation's research and work to release this Study was performed by attorney volunteers with experience in representing parties in FINRA's arbitration process and the funds to purchase the data for this Study were paid for through charitable donations. The Foundation would like to thank our donors for making this important Study a reality.

PIABA and the PIABA Foundation would like to thank Peter Mougey, Richard Frankowski, Jennifer Shaw, Richard Lewins, Sam Edwards and Thomas Mauriello as well as the members of the PIABA Board for your input and support. Special thanks to Michael Edmiston and Benjamin P. Edwards for your input and edits. Also special thanks to the students in the 2021 Public Policy Clinic at the University of Nevada, Las Vegas William S. Boyd School of Law for sharing insights they gained by representing non-party customers in expungement hearings.

BROKERCHECK AND EXPUNGEMENT

FINRA's BrokerCheck tool provides critical information about brokers that helps investors make informed decisions about who they allow to manage their life savings. Accurate and complete complaint history on brokers is also critical to preserve the ability of state and federal securities regulators to identify bad brokers to help these regulators perform their regulatory functions.

For years, PIABA and the PIABA Foundation ("Foundation") have documented and studied how FINRA's expungement arbitration process has allowed brokers and brokerage firms to erase valid complaints from their publicly available complaint histories. The findings of those studies are documented in reports published in 2013, 2019, and now in 2021.

In 2013, PIABA released a report that analyzed approximately 1,600 arbitration awards rendered in cases initiated by investors against brokerage firms and/or brokers for cases filed during the five-year time period between January 1, 2007 and December 31, 2011. Most of these arbitration awards were rendered by a panel of three arbitrators and expungement requests were made in the underlying customer arbitrations. That "2013 Study" showed that arbitrators granted expungement requests approximately 90% of the time ("2013 Study"). A copy of PIABA's 2013 Study can be found on the Foundation's website at www.piabafoundation.org.

At that time, brokers and brokerage firms were gaming the expungement process by conditioning settlements with investors on their agreement not to oppose expungement requests in the underlying customer disputes. PIABA recommended that FINRA prohibit its members from conditioning settlements on investors' agreement not to oppose expungements. PIABA also recommended that FINRA provide additional arbitrator training to try and solve the problem of arbitrators granting expungement requests too frequently.

2013 AND 2019 FINDINGS & FINRA CHANGES

After the release of the 2013 Study, FINRA changed the rules to prohibit its members from conditioning settlement on an investor's agreement not to oppose subsequent expungement requests. FINRA's current guidance on expungements states in pertinent part:

Effective July 30, 2014, FINRA Rule 2081 prohibits firms and registered representatives from conditioning settlement of a customer dispute on—or otherwise compensating a customer for—the customer's agreement to consent to, or not to oppose, the firm's or representative's request to expunge such information from CRD.¹

FINRA also committed to provide additional expungement training to arbitrators to try and ensure only appropriate expungement requests were granted, thus reducing the number of expungements being granted. Additional training did not work. Moreover, brokers and brokerage firms found new ways to game the expungement process.

In October 2019, the Foundation released a study which examined 1,078 expungement arbitration awards from January 1, 2015 to July 31, 2019 (“2019 Study”). The 2019 Study found that beginning in 2014-2015, brokers changed tactics from requesting expungement in underlying customer arbitrations to waiting until the conclusion of customers’ dispute and filing a new separate arbitration solely against their brokerage firm requesting expungement of the customer claims, i.e., straight-in expungements. A straight-in expungement case is an arbitration initiated by a broker against their current or former brokerage firm solely for the purpose of seeking expungement. The customer who made the complaint is not a party.

Brokers and brokerage firms also started gaming FINRA’s arbitration process by including a bogus demand for \$1.00 in damages to reduce the number of arbitrators considering expungement requests from a panel of three arbitrators to a single arbitrator. The “\$1.00 trick” also saved brokers and brokerage firms thousands of dollars per case. The 2019 Study found that by allowing its members to file these cases, FINRA lost over \$6 million in revenue.

The 2019 Study also found that not much had changed: brokers requested that over 2,000 customer complaints be expunged from their records and arbitrators granted those requests in over 80% of the cases. Clearly, despite more training, expungement requests were not treated as an extraordinary remedy.

SUMMARY OF 2021 UPDATED STUDY FINDINGS

¹ See <https://www.finra.org/arbitration-mediation/notice-arbitrators-and-parties-expanded-expungement-guidance>.

PIABA and the Foundation provide this updated Study (“2021 Updated Study”), which analyzes seven hundred (700) additional expungement awards from August 1, 2019 to October 31, 2020.

The results are clear. Arbitrators have continued to grant expungement requests 90% of the time, and the data shows that FINRA’s arbitration process allows brokers and brokerage firms to make expungement requests to arbitrators that are unopposed the vast majority of the time.

FINRA’s expungement process does not provide those with an interest in the outcome of the expungement request, *e.g.*, securities regulators and the customers who submitted the complaints, a meaningful opportunity to present evidence opposing expungement when appropriate.

The solution is simple. To effectively prevent expungements of valid customer complaints, FINRA must provide a meaningful opportunity for those with an interest in the outcome of the expungement request, *e.g.*, securities regulators and the customers who submitted the complaints, to present evidence opposing expungement, when appropriate. FINRA’s current expungement arbitration process provides no notice to state regulators until after an award granting expungement is issued and broker seeks to have a final arbitration award confirmed by a court of law. In addition, FINRA’s arbitration rules do not provide a way for state regulators to participate in the expungement arbitration where they can review the validity of the claim and present evidence opposing the expungement request.

While the current expungement process provides notice to customers so they can appear, it does not have safeguards to ensure that customers can participate in a meaningful way.

While FINRA’s current rule proposal purports to stop some of the abusive tactics used by brokers and brokerage firms in the arbitration proceedings that were identified in the 2019 Study, the proposed changes will not decrease the high percentage (90%) of expungements being granted. Without an opposing party in the expungement arbitrations, brokers and brokerage firms will continue to obtain expungements of customer complaints that are valid and valuable to securities regulators and the investing public.

The Securities Exchange Commission (“SEC”) is currently considering whether to approve FINRA’s proposed rule changes. The deadline for the SEC to approve FINRA’s proposed rule change is May 28, 2021.

While PIABA and the Foundation appreciate FINRA efforts to improve its process, the data all from all three PIABA/Foundation studies, which analyzed a total of 3,378 expungement awards over a period spanning fourteen (14) years, shows that FINRA’s current proposed plan to require a panel of three randomly selected arbitrators from a special roster will not significantly reduce the percentage of expungement requests. This is because the proposed rule will still allow brokers to present unopposed expungement requests. More training will not work. As the data conclusively demonstrates, since FINRA implemented enhanced expungement training in 2014, expungements are still being granted approximately 90% of the time. The data strongly indicates that arbitrators are granting expungement requests 90% of the time because they are being provided with one-sided presentations about the merits of the customer complaints, not because of lack of training.

This Updated Study also provides an example in a currently pending straight-in expungement arbitration of gamesmanship used by brokers and brokerage firms that demonstrate that the process is not designed for customers to meaningfully participate and oppose expungement requests without an attorney willing to handle the case *pro bono*.

If the SEC approves FINRA’s current proposed incremental rule changes, it will likely be several more years until this issue is revisited. In the meantime, brokers and brokerage firms will find new ways to game the system and thousands of additional valid customer complaints will be wrongfully erased from the public record. These erasures not only hurt the investing public who need accurate background information on brokers when selecting a trusted financial professional, but it also will harm securities regulators’ ability to perform their critical regulatory functions.

Now is the time to fix the systemic problem and craft a solution that ensures that arbitrators treat expungement as an extraordinary remedy. The time has come for state securities regulators and customers to have a meaningful opportunity to participate in these expungement proceedings directly or through an advocate so that, when appropriate, evidence opposing expungement can be presented to arbitrators.

Finally, recognizing the reality that customers are not going to pay an attorney to represent them in these expungement proceedings, the Foundation started a program that coordinates with attorneys and law school clinics to represent customers who wish to participate and oppose expungement requests *pro bono*. The costs necessary to administer this *pro bono* program and the expenses for customers and attorneys to participate in these expungement proceedings in arbitration, (*e.g.*, court reporter costs) will also be funded through charitable donations. If you wish to support this important work, please visit our website, www.piabafoundation.org.

CRD AND STANDARD FOR GRANTING EXPUNGEMENT

The Financial Industry Regulatory Authority (“FINRA”) works with state securities regulators to maintain a database, known as the Central Registration Depository (“CRD”), of information on individuals working as current and former registered representatives in the brokerage industry. Complaints by investors, for example, are included in the CRD records. Those records can be accessed by the public through FINRA’s BrokerCheck tool on FINRA’s website, as well as obtained from some state securities regulators. FINRA and state and federal securities regulators actively encourage investors to use FINRA’s BrokerCheck tool and look for customer complaints when deciding whether to hire a particular broker to manage the customer’s life savings. Therefore, as FINRA recognizes, it is important that the information on the CRD system, and by extension BrokerCheck, be complete and accurate.

To remove customer complaint information from the CRD system, a broker must request that the information be expunged. A broker can request expungement in the customer arbitration if one is filed. A broker also may request expungement in a separate case. If an arbitration panel grants the request and the broker obtains court confirmation of the arbitration award, FINRA removes the information from the CRD system. FINRA instructs arbitrators that customer complaints should be removed from a broker’s CRD only in **extraordinary circumstances**. FINRA instructs arbitrators to grant the extraordinary remedy of expungement only after they make an affirmative finding that:

- (A) the claim, allegation or information is factually impossible or clearly erroneous;
- (B) the registered person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation, or conversion of funds; or

(C) the claim, allegation or information is false.

Over time, FINRA has expanded the type of customer complaints that must be reported on a broker's CRD. In May 2009, FINRA expanded its rules to require CRD reporting of customer complaints even if the financial advisor is not named as a party to the arbitration. That change resulted in a drastic increase in the number of complaints being reported, and in turn, a drastic increase in the number of expungements being sought. Since then, advocates for and against the expungement process have debated the best way to effectively balance the competing interests of full and complete disclosure and protection of brokers' reputations.

The 2019 Study illustrated that FINRA's expungement arbitrations were being systematically gamed, exploited and abused with one-sided hearings. The gamesmanship also involved the manipulation of arbitrator selection, the expungement of large groups of customer complaints in one arbitration proceeding and included abusive conduct by the brokers and broker-dealer respondents to such an extent that the Foundation recommended that the entire process be frozen until it could be repaired.

CURRENT FINRA PROPOSAL

After the release of the 2019 Study, FINRA proposed changes to the expungement process that, if approved, it claims would correct many of the problems identified in the 2019 Study. The Securities Exchange Commission ("SEC") is currently considering whether to approve FINRA's proposed rule changes and the current deadline for the SEC to make a decision on whether to approve FINRA's proposed changes is May 28, 2021.

PIABA and the Foundation appreciate FINRA efforts to incrementally improve the process. However, the data illustrated below shows that FINRA's proposed changes will not fix the systemic problem of arbitrators continuing to grant expungement requests too frequently, because the expungement process does not provide state regulators and customers, who have a vested interest in the outcome of the expungement requests, a meaningful opportunity to participate and present evidence opposing the expungement.

FINRA concedes that arbitrators historically have not treated expungement requests as an extraordinary remedy. FINRA's current proposed solution is to create a roster of specially trained expungement arbitrators from the chair-qualified

arbitrator roster to decide expungement cases and require a panel of three (3) randomly selected arbitrators from that roster to decide expungement requests. As explained below, an analysis of historical arbitration awards going back more than a decade demonstrates that these methods have already been tried and have failed. These changes will not reduce the percentage of expungement requests being granted.

DATA SHOWS FINRA PROPOSAL IS NOT THE SOLUTION

A summary of the pertinent data showing why FINRA's proposal is fatally flawed is below:

I. Summary of Findings

A. Number of Expungement Requests Remains High

2019 Study:

The 2019 Study showed that there was an explosive increase in the filing of what are known as straight-in expungement cases, which rose 924% from 59 in 2015 to 545 in 2018. As explained above, a straight-in expungement case is an arbitration initiated by a broker against their current or former brokerage firm solely for the purpose of seeking expungement. The customer who made the complaint is not a party.

2021 Update Study:

The updated data finds that the number of expungement requests per year remains very high. For example, there were 700 expungement awards from August 1, 2019 to October 31, 2020.

B. Average Number of Complaints Sought to be Expunged per Case Remains Steady

2019 Study:

The 2019 Study showed that the number of customer complaints requested to be expunged increased by 1016% from 102 in 2015 to 1,026 in 2018. For example, brokers requested that 2,194 customer complaints be expunged in 1,078 arbitration awards issued during the time-period analyzed, an average of two complaints per

case. In 2018, the highest number of customer complaints put at issue in one case was thirteen (13).

2021 Updated Study:

The updated data shows that the number of expungement requests per case continues to be high. For example, brokers requested that 1,360 customer complaints be expunged in the 700 awards, approximately two complaints per case. The highest number of complaints sought to be expunged in a single case was twenty-nine (29).

C. Brokerage Firms Continue to Consent to Expungement Requests by Brokers

2019 Study:

The 2019 Study showed that expungement proceedings are rarely adversarial. Of the 1,078 cases analyzed, the respondent brokerage firm did not object or otherwise oppose the individual broker's expungement request 1,055 times – over 98% of the time. This demonstrated that brokers and their firms have a common interest in erasing customer complaints from the brokers' records and, as a result, are not truly in opposition to each other in a straight-in expungement case.

2021 Updated Study:

The updated data shows that straight-in expungements have continued as non-adversarial proceedings and that broker-dealer respondents continued not to oppose expungement requests 98% of the time.

D. Customer Participation in Expungement Proceedings Remains Low

2019 Study:

The 2019 Expungement Study shows that of the 1,078 expungement cases filed between 2015 and 2019, customers appeared to oppose the expungement requests only 141 times – approximately 13% of the time.

2021 Updated Study:

The updated data shows that customers continue not to participate in the vast majority of expungement proceedings. Customers appeared to oppose the expungement requests of brokers only 106 times – approximately 15% of the time. That arbitrators are routinely deciding expungement requests without input from anyone other than the broker and brokerage firm, which have a common interest in expungement.

E. Whether One Arbitrator or Three Arbitrators – FINRA Expungements Are Granted at About the Same Rate

2019 Study:

The 2019 Study showed that overall, expungement requests were granted 81% of the time. A panel of three arbitrators was only slightly more likely to deny expungement requests than a single arbitrator. The data showed that in 2018, panels of three arbitrators granted expungement 88% of the time, and single arbitrator panels granted expungement 87% of the time.

2021 Updated Study:

The updated data shows that from July 2019 to October 31, 2020, expungement requests were granted in part in 90% of the straight-in expungement cases and a panel of three arbitrators is only slightly more likely to deny expungement requests than a single arbitrator. The data shows that panels of three arbitrators grant expungement 89% of the time and single arbitrator panels grant expungement 84% of the time.

F. FINRA’s Proposal of Three-Arbitrator Panels of Specialists Will Not Solve the Problem

FINRA’s proposed rule seeks to reduce the rate at which expungements are granted by requiring that the cases be heard by a panel of three arbitrators, instead of a single arbitrator. The 2019 and 2021 data show that a panel of three arbitrators is only slightly less likely to grant expungement as a single arbitrator. The systemic problem is that the expungement requests are treated by the parties and arbitrators as unopposed motions.

This conclusion is further supported by PIABA's 2013 Expungement Study, which analyzed approximately 1,600 expungement requests rendered in customer-initiated arbitrations or as a separate straight-in cases filed during the five-year time period between January 1, 2007 and December 31, 2011. Most, if not all, of these arbitration awards were rendered by a panel of three arbitrators and the data showed that expungement requests were granted approximately 90% of the time. In the 2013 Study, PIABA recommended that FINRA provide additional training with the hope that more training would reduce the high rate of expungements being granted. FINRA did provide more expungement training to arbitrators, but as shown in the 2019 Study and 2021 Updated Study, additional training has not reduced the high rate of expungements being granted.

G. Arbitrators Are Much More Likely to Deny Expungement Requests When Interested Parties Oppose the Request.

2019 Study:

The 2019 Study showed that arbitrators are 4 times more likely to deny expungement requests when customers oppose expungement. The 2019 Expungement Study shows that of the 1,078 expungement cases filed between 2015 and 2019, customers appeared to oppose the expungement requests only 141 times – approximately 13% of the time. Over the entire period analyzed, the study found, however, that when customers opposed expungement, arbitrators denied the requests 36% of the time. In contrast, when customers did not object or participate, arbitrators denied the expungement request only 9% of the time. Based on this data, the 2019 Expungement Study concluded that arbitrators are 4 times more likely to deny an expungement request when customers object.

2021 Updated Study:

The updated data shows that arbitrators are 5.4 times more likely to deny expungement when the respondent brokerage firm opposes expungement and are 4.3 times more likely to deny expungement when customers oppose expungement.

RECOMMENDATION: ESTABLISH AN INVESTOR ADVOCATE

FINRA should provide a meaningful opportunity for those with an interest in the outcome of the expungement request, such as state securities regulators and customers who lodged complaints at issue, to present evidence opposing the request, when appropriate. FINRA's current rule proposal does not solve the systemic problem that arbitrators do not treat expungement requests as an extraordinary remedy.

Expungement is a regulatory decision that should be placed in the hands of regulators. If the expungement process is going to remain in FINRA arbitration, however, PIABA and the Foundation recommend that FINRA and the SEC create and embed an advocate ("Advocate") into the expungement process similar to the role that a *guardian ad litem* serves in a court case. The purpose of the Advocate would be to protect the integrity of CRD data, which are state records and which the investing public is encouraged to rely on as current and accurate.

At this time, state securities regulators are not notified when a broker files a petition for expungement. FINRA should provide state securities regulators with notice of the expungement request at the time that the petition for expungement is filed **and give them a meaningful opportunity to participate in the arbitration proceeding –either by permitting them to intervene in the arbitrations directly or permitting them to participate indirectly through the Advocate.**

Under the current system, the notice FINRA provides to state regulators – through NASAA, the association representing state regulators – is provided only after a petition for expungement has been granted and the broker seeks to confirm that arbitration award in a court of law. At that time, states must very quickly decide whether to intervene and oppose expungement without having adequate information to make that decision.

Under FINRA's current proposal, FINRA would notify NASAA within thirty (30) days of when a "complete" expungement request is filed in arbitration, which is earlier in the process. But, as NASAA explained in its comment letter in response to the proposed rule change, earlier notice to state securities regulators is meaningless if the regulators are not provided a meaningful opportunity to participate in the expungement arbitration proceeding. NASAA explains this problem in its comment letter as follows:

While it is true that NASAA would receive earlier notice, this notice alone would not address the fact that NASAA members would have no opportunity to intervene during the arbitration hearing. Although states would be notified that a broker is requesting an expungement and the occurrence number, there would be no meaningful disclosure of information on which to assess the expungement request, nor would there be a legal mechanism to facilitate regulator involvement, the critical part of our 2018 framework that is missing from the current Proposal. The bottom line is that the Proposal fails to provide a pathway to contest the expungement relief request during the arbitration should a state determine it is appropriate to do so. Without NASAA's members having a legal mechanism to intervene at this stage of the arbitration, notice is either meaningless or could force an investigation into every situation in which a broker requests expungement. While NASAA appreciates FINRA's willingness to give it earlier notice of expungements, NASAA strongly prefers this relief be deferred to a proposal that would allow states to act on it.²

The Advocate, acting independently or through state securities regulators, would serve to advocate for the integrity of the CRD regulatory record and would be responsible for investigating the validity of the customer complaint, obtaining and reviewing relevant documents, as well as interviewing the customer, customer's counsel, and any other relevant witnesses. The Advocate would assist those customers who want to appear and oppose the request, when appropriate. The Advocate could also participate in the expungement hearing by making an opening statement, cross examining the individual broker, presenting testimony and documents, and providing a written report with a recommendation to the arbitration panel on whether expungement should be granted.

Logistically, this could be accomplished in several ways. The Advocate role could be embedded into the arbitration process to assist the arbitrators in gathering information and making a recommendation on whether to grant expungement. The Advocate could assist customers interested in opposing expungement as well.

² See NASAA Comment Letter dated October 22, 2020 at <https://www.sec.gov/comments/sr-finra-2020-030/srfinra2020030-7936105-224674.pdf>.

Alternatively, the Advocate could work with state securities regulators to help them decide whether to participate in and oppose expungement.

For those customers who settled their cases, there is the real risk of the broker or brokerage firm suing them for breach of confidentiality or non-disparagement provisions in their settlement agreements and potentially forfeiting their settlement payments. FINRA's rules do not allow brokerage firms to condition settlement on a customer's agreement not to oppose expungement, but it not reasonable to believe that a customer without an attorney could find that rule and navigate other the legal considerations of opposing expungement. As a result, without an Advocate, *pro se* customers will largely continue to choose not to participate in expungement proceedings regardless of when they are notified that a petition for expungement has been filed.

Rather than create a mechanism through state regulators and/or an Advocate to present evidence opposing expungement request, FINRA's rule proposal places the burden solely on arbitrators to investigate and oppose expungement when appropriate. Arbitrators are required to be neutral, not advocates for or against a position. Imposing such a burden on arbitrators in unopposed straight-in expungements is wholly inconsistent with their role as neutral factfinders and decisionmakers. As a result, the solution is not (1) to increase the number of arbitrators per case or (2) to blur the traditional roles of arbitrator and advocate or (3) to require additional training or (4) to create a special roster of arbitrators as FINRA has proposed. The data shows that arbitrators are treating straight—in expungement requests like unopposed motions. The solution is to have someone like the Advocate represent stakeholders in the integrity of the CRD system. The Advocate and/or state securities regulators must have a meaningful opportunity to inquire into facts indicating that expungement should be denied and present those facts in the expungement proceeding.

In further support of this recommendation, in October 2019, the Foundation created a *pro bono* expungement program where attorneys who are experienced in FINRA arbitrations volunteer to represent customers in opposing expungement. The Foundation is pleased to announce it has successfully represented several customers in opposing expungements. The Foundation is also grateful for the insights of students and faculty from The University of Nevada, Las Vegas, William S. Boyd School of Law's Public Policy Clinic, which also provided *pro bono* representation of customers opposing expungement.

The Foundation has found the process to be rewarding not only through obtaining awards denying expungement requests, but also in gaining a better

understanding of the obstacles to customers being able to oppose expungement requests. Expense is the greatest obstacle. Because the expungement process is simply too daunting for the vast majority customers to represent themselves *pro se* (it is opaque and difficult for attorneys to navigate), customers who want to oppose expungement are facing having to spend thousands of dollars to retain an attorney to represent them. FINRA's Revised Proposal for earlier notice to customers does not cure this problem.

If the SEC approves FINRA's current proposed rule changes, it will likely be several more years until this issue is revisited. In the meantime, thousands of additional customer complaints will be wrongfully erased from public records. These erasures not only hurt the investing public who need accurate background information on brokers when selecting a trusted financial professional but erasing records harm securities regulators' ability to perform their regulatory functions.

STUDY METHODOLOGY

In preparing this 2021 Updated Study, the Foundation supplemented its data from the 2019 Study and reviewed data that it requested Securities Arbitration Commentator (SAC) to provide with respect to all arbitration awards issued in straight-in expungement cases filed from July 1, 2019 through October 31, 2020 (the "Review Period"). The data from 2019 Study is listed below along with the new updated data to better demonstrate long-term trends.

The Foundation requested that SAC extract the following information for each award and for each case:

- (a) Docket No;
- (b) Venue;
- (c) Date Case Filed;
- (d) First Date of Evidentiary Hearing;
- (e) Date Award Issued;
- (f) Name of Respondent(s);
- (g) Name of Respondents' Attorney (Firm);
- (h) Name of Claimant Broker;
- (i) Name of Broker's Attorney (Firm);
- (j) Whether Respondent BD Objected to Expungement;
- (k) Whether Customer Objected to Expungement;
- (l) Number of customer complaints requested to be expunged;
- (m) Name of broker requesting expungement;

- (n) Name of Arbitrator;
- (o) Number of Hearing Sessions.

See SAC Spreadsheet #1 attached as Exhibit A.

To prepare the report, the Foundation used the information from Exhibit A to create a Consolidated Spreadsheet, which is attached as Exhibit B.

DETAILED FINDINGS

I. Expungements Are Not Treated As An Extraordinary Remedy, As They Were Intended.

1. FINRA has always taken the position that expungement is an extraordinary remedy and should only be granted in appropriate circumstances.³ Yet, from 2015 to mid-2019, FINRA arbitrators granted expungement requests over 80% of the time. The updated data from August 1, 2019 - October 31, 2020 (“Updated Data”) further supports that expungements are not being treated as an extraordinary remedy, showing that expungement requests were granted at least in part in 636 out of 700 awards, a rate of 90%.

Year	Expungements Granted (%)
2015	93
2016	81
2017	81
2018	81
Updated Data	90

³ FINRA Regulatory Notice 12-42 (“It has been FINRA’s long-held position that expungement of customer dispute information is an extraordinary measure, but it may be appropriate in certain circumstances.”)

https://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-17-42.pdf

Once these complaints are expunged, they disappear completely from the CRD system and BrokerCheck – making them no longer visible to investors.

II. The Number of Straight-In Expungements Has Skyrocketed Since January 1, 2015.

2. The number of straight-in expungements filed with FINRA continues to increase.

Year	Cases filed
2015	59
2016	135
2017	339
2018	545
Updated Data	700

III. Multiple Customer Complaints Are Being Expunged Per Case.

3. Individual brokers frequently request that multiple customer complaints be expunged in a single expungement case. As a result, the 2019 Study showed that while the total number of straight-in expungement cases for the 2015-2018 period was 1,078, the number of customer complaints that the brokers asked be expungement was 2,194, which is an average of approximately two (2) customer complaints per case.

The updated data shows that the number of expungement requests per case continues to be high. Brokers requested that 1,360 customer complaints be expunged in the 700 awards, i.e., again approximately two (2) complaints per case.

4. The number of customer complaints that brokers requested be expunged from CRD increased significantly.

Year	Number of customer complaints brokers requested be expunged
2015	102
2016	300

Year	Number of customer complaints brokers requested be expunged
2017	756
2018	1036
Updated Data	1360

In the Updated Data, one broker in a single expungement case asked for the erasure of twenty-nine (29) customer complaints from their CRD record.

IV. Expungement Requests are Rarely Opposed by Brokerage Firms or Customers

A. Expungement Requests Are Not Opposed by Respondent Brokerage Firms 98% Of The Time.

5. Brokerage firms very rarely oppose brokers' requests for expungement. The 2019 Study showed that of the 1,078 cases, the respondent brokerage firm did not object or otherwise oppose the individual broker's expungement request 1,055 times out of 1,078 – over 98% of the time. Brokerage firms objected to these expungement requests in only 21 of the 1,078 total requests. That is less than 2% of the time.

6. The 2021 Updated Study reflected similar results. In the seven hundred (700) awards issued between August 1, 2019 to October 31, 2020, the respondent brokerage firm did not object or otherwise oppose the individual broker's expungement request 684 times out of 700 awards – over 98% of the time. Brokerage firms objected to these expungement requests in only 16 of the 700 total requests. Again, that is approximately 2% of the time.

B. Customers Rarely Participate and Oppose Expungement Requests.

7. Customers are not named parties in straight-in expungement cases so they are not required to appear. The Foundation does not recommend that customers be named as parties to these cases. Customers should not be required to essentially relitigate cases they have settled or otherwise resolved. The 2019 Study found that of the 1,078 straight-in expungement cases, customers whose complaints are the

subject of expungement requests participated and objected to brokers' expungement requests only 141 times, 13% of the time.

8. The 2021 Updated Study found similar results. Of the 700 straight-in expungement cases, customers whose complaints are the subject of expungement requests participated and objected to brokers' expungement requests only 106 times, 15% of the time.

C. Panels of Three Arbitrators Will Not Reduce the High Rates of Expungements Being Granted.

9. Expungement rates show that expungement is not treated as extraordinary remedy and three arbitrators are no better than one.

2019 Study	(%)
% of expungements granted in part (2018)	87
% of expungements granted- 3 Arbitrators	88
% of expungements granted- 1 Arbitrator	87

Updated Data	(%)
% of expungements granted in part	90
% of expungements granted- 3 Arbitrators	89
% of expungements granted- 1 Arbitrator	84

10. FINRA's proposed rule seeks to reduce the rate in which expungements are granted by requiring that the cases be heard by three arbitrators, instead of a single arbitrator. Our data shows that a panel of three arbitrators is just as likely to grant expungement as a single arbitrator. The systemic problem is that the expungement requests are treated by the parties and arbitrators as unopposed motions.

D. Arbitrators Are Significantly More Likely to Deny Expungement Requests When Someone Objects.

11. The 2019 Study found that, even though respondent brokerage firms opposed expungement less than 2% of the time, when brokerage firms opposed expungement, arbitrators denied the expungement request 48% of the time. In contrast, when brokerage firms did not object, arbitrators denied the expungement request only 11% of the time. Therefore, arbitrators are 4.36 times more likely to

deny expungement requests when a brokerage firm objects to the expungement request.

12. Even though customers opposed expungements only 13% of the time, when customers opposed expungement, arbitrators denied the requests 36% of the time. In contrast, when customers did not object, arbitrators denied the expungement request only 9% of the time. Arbitrators are four (4) times more likely to deny an expungement request when a customer objects.

13. The 2021 Update Study results show similar results. The updated data shows that arbitrators are 5.4 times more likely to deny expungement when the broker-dealer respondent opposes expungement and are 4.3 times more likely to deny expungement when customers oppose expungement.

14. This data supports the conclusion that the most effective way to reduce the rate in which arbitrators grant expungement is to present the arbitrators with evidence opposing the request.

E. Without an Opposing Party, There Are No Procedural Safeguards to Prevent Brokers and Brokerage Firms from Presenting One-Sided and/or False Information to Arbitrators.

15. Brokers and brokerage firms are the only parties to straight-in expungement cases, and both have an incentive to expunge customer complaints from brokers' CRD records. The customers whose complaints are the subject of the expungement request are not parties to the straight-in expungement arbitration and if they participate, their role is akin to a fact witness. They cannot conduct discovery, engage in motion practice, or have the other due process rights given a party to an arbitration.

16. Since brokerage firms do not oppose brokers' expungement requests 98% of the time and customers oppose expungement in only 13%-15% of cases, it logically follows that there should be procedural safeguards in place to prevent brokers from presenting one-sided, false or misleading information to arbitrators, who are ethically required to remain neutral in the pending arbitration.

17. FINRA puts the burden of ensuring that only valid expungement requests are granted on arbitrators. But imposing such a burden on arbitrators in unopposed straight-in expungement cases is wholly inconsistent with their role as neutral factfinders and decisionmakers.

18. In fact, FINRA’s arbitrator training materials prohibit arbitrators from conducting their own independent investigations into the validity of the underlying customer complaints. FINRA Dispute Resolution Arbitrator’s Guide states in pertinent part:

Questions by Arbitrators and Factual Investigations

Each case must be judged solely on the written and testimonial evidence presented at the hearing. Each arbitrator has a right to question witnesses. Even though it is proper for an arbitrator to ask questions, every effort should be made to avoid taking over a hearing or becoming an advocate. Parties and their attorneys should be permitted to try their own cases. Generally, arbitrators should refrain from questioning a witness until all parties have finished their examination.

Arbitrators should not make independent factual investigations of a case. When arbitrators are in doubt about an issue, legal or otherwise, they should request briefs from the parties. If cases are cited in a party’s motion or brief, and the arbitrators wish to read the full court opinions, the arbitrators should ask the parties to supply copies. Arbitrators generally should review only those materials presented by the parties.

See FINRA Arbitrator’s Guide at page 60 (emphasis added).

19. While FINRA’s expungement training materials encourage arbitrators to ask questions during the expungement hearing and request additional documents from the parties, this does not change the fact that arbitrators must remain neutral. As such, arbitrators cannot be the sole gatekeeper to protect the integrity of the CRD database and valid customer complaints from being erased.

F. Brokers and Firms Continue to Find New Ways to Game the Arbitration Process to Obtain Expungement Awards.

20. The example below is happening right now in a currently pending straight-in expungement case where the customer hired attorneys through the Foundation’s *pro bono* expungement program to oppose expungement. This example shows how brokerage firms and brokers engage in gamesmanship and why state regulators need early notice of expungements and the ability to participate directly or through the proposed Advocate. This example also illustrates how FINRA’s expungement process is not designed for investors to meaningfully

participate without an attorney and why the Foundation's *pro bono* expungement program provides valuable services.

Case Study

The Foundation's Expungement Project, through which attorneys represent customers opposing expungement on a *pro bono* basis, has discovered some of the new and innovative tactics that brokers and firms are using in violation of FINRA's directive that customers be permitted to appear and oppose a broker's request to oppose expungement.

For example, in a pending case, the customer filed a FINRA arbitration against the broker-dealer for unsuitable investment recommendations by the firm's broker. The arbitration settled late last year for an undisclosed amount. The customer believed that his dispute was over and dismissed the arbitration proceeding against the broker-dealer. In January 2021, the broker filed a straight-in expungement arbitration against the broker-dealer seeking to expunge the customer's complaint.

The customer retained a *pro bono* attorney through the Foundation Expungement Project to oppose the straight-in expungement arbitration. Now, the brokerage firm is objecting to the customer using documents the firm produced in the original arbitration that support denial of the expungement relief on the basis that those documents were designated as confidential and could only be used in the original arbitration. In an email exchange attached hereto, the attorney representing the brokerage firm made the following objection:

... [Firm] objects to you, your firm, or any other individual reviewing any confidential documents and information produced by [Firm] in Customer v. Firm. Given the confidential and proprietary nature of those documents, the parties in the [Customer] matter expressly agreed that the documents would be used solely in connection with prosecuting, defending, and settling that matter. Further dissemination of the documents would destroy or diminish the value of such information, causing [Firm] severe and irreparable harm. That concern is heightened by your vague reference below to sharing documents with your "firm [] and other counsel" for [Customer]. Moreover, those documents are irrelevant and beyond the scope of what is necessary to decide the pending expungement claim. The documents potentially responsive to the expungement claim—such as the Statement of Claim,

the Answer, the settlement agreement, and [Customer's] account documents—are within [Customer's] possession already.

Here, the brokerage firm attempts to prohibit the customer and his attorneys from using documents the firm produced in the prior case to oppose the expungement relief in the subsequently filed straight-in expungement arbitration. The brokerage firm is also improperly and unilaterally defining what documents and information are relevant to the expungement request.

Simply put, without an attorney, there is no way that customers can effectively represent themselves in these straight-in expungements. Resolving the discovery issue described above will require the filing a motion to compel before the arbitration panel or filing a declaratory judgment action in a court of law. This spurious discovery dispute will likely take hours to resolve and would have cost thousands of dollars in attorney's fees to resolve were the customer not represented on a *pro bono* basis. Customers cannot and should not be asked to bear that cost.

CONCLUSION

PIABA and the Foundation have conducted studies of FINRA's expungement awards for over a decade and the results are clear. Increasing the number of arbitrators per case and providing arbitrators with more training will not lower the incidence of granting expungement or get arbitrators to treat expungement as an "extraordinary remedy."

The data unquestionably leads to the conclusion that the most effective way to reduce the rate in which arbitrators grant expungement is to stop the practice of arbitrators deciding expungement based on a one-sided presentation of evidence. FINRA should provide a meaningful opportunity for parties with an interest in the outcome of the expungement request, such as state securities regulators and customers who lodged complaints at issue, to present evidence opposing the request, when appropriate.

The data shows that the current system of deciding expungement through straight-in expungement arbitrations requires the establishment of an Investor Advocate, who will be charged with helping to preserve the integrity of CRD data.