

**PIABA AND THE PIABA FOUNDATION**

**2023 UPDATED STUDY ON FINRA EXPUNGEMENTS**

**A NEW HOPE TO PROTECT THE INTEGRITY OF THE PUBLIC  
RECORD**

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## **ABOUT THE GROUPS AND ACKNOWLEDGMENTS**

The Public Investors Advocate Bar Association (PIABA) is a 501(c)(6) non-profit international bar association whose members represent investors in disputes with the securities industry. Currently, there are members from 44 states and Puerto Rico. PIABA's mission 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](http://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, brokerage firms and investment advisers in 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. The funds to purchase the data for this Study were provided by charitable contributions and grant funds. The Foundation would like to thank our donors for making this important Study a reality.

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## **CRD AND STANDARD FOR GRANTING EXPUNGEMENTS**

The Financial Industry Regulatory Authority (“FINRA”) works with state securities regulators to maintain a database, known as the Central Registration Depository (“CRD”). The database contains information on individuals working as current and former registered representatives in the brokerage industry.

Complaints by investors are included in the CRD database and the information can be accessed by the public through FINRA’s BrokerCheck tool on FINRA’s website as well as from many state securities regulators. FINRA as well as state and federal securities regulators actively encourage investors to use FINRA’s BrokerCheck to search for customer complaints against brokers when deciding whether to hire one to manage their investments. It is crucial that the information on the CRD system, and by extension BrokerCheck, be complete and accurate.

FINRA provides a mechanism through its arbitration forum for brokers to seek removal of customer complaints from their complaint history in a process referred to as expungement. Typically, brokers request that the information be expunged through FINRA’s arbitration forum. A broker can request expungement in FINRA arbitration in two ways – (1) in an arbitration filed by their customer, if one is filed and (2) request expungement in a separate arbitration filed by brokers against their brokerage firms, known as “straight-in” expungement arbitrations.

If an arbitration panel issues an award granting the expungement request, brokers are required to obtain court confirmation of the arbitration award before FINRA removes the information from the CRD database.

FINRA instructs its arbitrators in deciding requests for expungement that customer complaints against brokers should only be removed from the CRD database under extraordinary circumstances. It further directs arbitrators that they should only grant the extraordinary remedy of expungement, if 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 the years, FINRA has expanded the type of customer complaints that must be reported on its CRD database. In May 2009, FINRA expanded its rules to require CRD reporting of customer complaints even if the broker 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 expungement requests.

Since then, securities regulators and 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.

## **BRIEF HISTORY OF ADVOCACY AND CHANGES TO FINRA'S EXPUNGEMENT PROCESS**

For years, PIABA and The PIABA Foundation ("Foundation") have documented and studied how FINRA's expungement process has allowed brokers to erase valid and meritorious complaints from their publicly available professional histories. The findings of those studies are documented in reports that were published in 2013, 2019, 2021, and now in this 2023 updated study.

### **2013 STUDY AND FINDINGS**

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 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").

At that time, brokers and brokerage firms were gaming the expungement process by making settlement agreements with investors conditioned on investors not opposing subsequent expungement requests by brokers about investors' underlying complaint(s).

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.

## **CHANGES MADE BY FINRA AFTER THE 2013 STUDY**

After the release of the 2013 Study, FINRA changed its rules to prohibit its members from conditioning settlements on investors' 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.<sup>1</sup>

FINRA also committed to providing additional expungement training to arbitrators to try and ensure that only appropriate expungement requests were granted, with the intended effect of reducing the number of expungement awards being granted. As explained below, additional training did not work and brokers and brokerage firms found new ways to game the expungement process.

## **2019 STUDY AND FINDINGS**

As a follow up to PIABA's 2013 Study, in October 2019, the Foundation released a study which examined 1,078 expungement 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' disputes and then filing new, separate arbitrations against their brokerage firms requesting expungement of the customer claims. These are commonly referred to as "straight-in" expungement arbitrations.

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

The 2019 Study found that even though brokerage firms were named as respondents, they almost never opposed brokers' expungement requests. Therefore, brokers and their firms were not adversarial parties, which allowed them to coordinate and subvert FINRA's arbitration rules. For example, brokers and brokerage firms were able to coordinate in the selection of arbitrators who were more likely to grant expungement requests. Brokers also began including a demand for only \$1.00 in damages and then they withdrew the request at the final expungement hearing. Including the initial request for \$1.00 in damages, however, allowed the parties under FINRA's arbitration rules to reduce the number of arbitrators considering expungement requests from a panel of three to a single arbitrator. The 2019 Study found that by allowing brokers to file these cases, FINRA lost over \$6 million in revenue.

The 2019 Study found that not much had changed in terms of expungement results. Brokers requested that over 2,000 customer complaints be expunged during the period and despite the additional training provided by FINRA, arbitrators granted expungement requests over 80% of the time. Clearly, expungement requests were not being treated as an "extraordinary remedy" by FINRA's arbitrators.

Importantly, the 2019 Study showed that arbitrators were four times more likely to deny expungement requests when an interested party participated in the straight-in arbitration and opposed expungement. For example, the 2019 Study found that of the 1,078 expungement cases filed between 2015 and 2019, customers opposed the expungement requests only 141 times – approximately 13% of the time. Over the entire period analyzed, the study found 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 were four times more likely to deny an expungement request when a customer objected.

Recognizing the reality that customers were not going to pay an attorney to represent them in these expungement proceedings, The PIABA Foundation implemented a program that coordinates with attorneys to provide customers with *pro bono* representation for customers who wish to participate and oppose expungement requests. 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), were funded through grants and charitable donations.

## **FINRA’S PROPOSED CHANGES AFTER 2019 STUDY**

After the release of the 2019 Study, FINRA proposed new rules to improve the expungement process. The proposed rule change sought to close many of the loopholes that were being exploited by the parties in straight-in expungement arbitrations. One of the proposed rule changes was to require a panel of three randomly selected arbitrators from a special roster to decide straight-in expungement requests, rather than allowing brokers and brokerage firms to coordinate and select a single arbitrator to decide the cases.

The proposed rules went through the comment period and the Securities Exchange Commission (“SEC”) considered whether to approve FINRA’s proposed rule changes.

Critics of the proposed rule changes, which included PIABA and the Foundation, expressed concerns that they did not go far enough, and that they would not reduce the rate of arbitrators granting expungements. The deadline for the SEC to approve FINRA’s proposed rule change was May 28, 2021.

## **2021 STUDY AND FINDINGS**

In May 2021- prior to the deadline - PIABA and the Foundation released an updated Study (“2021 Study”), which analyzed 700 additional expungement awards from August 1, 2019, to October 31, 2020. The 2021 Study found that arbitrators continued to grant expungement requests 90% of the time and the data showed that the reason was that they were virtually always unopposed.

The 2021 Study illustrated that FINRA’s proposed rule change to require a panel of three randomly selected arbitrators from a special roster would not significantly reduce the percentage of expungement requests granted, because the data showed that there was no meaningful difference in expungement results whether they were being decided by one arbitrator or three.

The crux of the problem was that arbitrators were being provided with one-sided presentations about the merits of customer complaints and no evidence was being introduced to oppose brokers’ expungement requests.

The 2021 Study's updated data confirmed the findings in the 2019 Study and showed that arbitrators are 5.4 times more likely to deny expungement requests when the respondent brokerage firm opposed expungement and were 4.3 times more likely to deny expungement requests when customers oppose expungement.

Based on the 2021 Study data, PIABA and the Foundation recommended, among other things, that FINRA provide state securities regulators with notice of the expungement request at the time that the petition for expungement was filed, *and to give state securities regulators a meaningful opportunity to participate in the arbitration proceeding – either by permitting them to intervene in the arbitrations directly or by permitting them to participate through a designated representative.*

The 2021 Study argued that the purpose of the state regulators' participation would be to protect the integrity of their CRD data, which are state records that the investing public are encouraged to rely upon as being current and accurate.

#### **FINRA TEMPORARILY WITHDREW ITS PROPOSED RULE CHANGES AFTER THE RELEASE OF 2021 STUDY.**

After the release of the 2021 Study, on May 28, 2021, FINRA temporarily withdrew its proposed rule changes from consideration by the SEC. In a press release issued that day entitled, *FINRA Statement on Temporary Withdrawal of Specialized Arbitrator Roster Rule Filing*, FINRA stated in part,

Following consultations with the SEC staff, we temporarily withdrew from SEC consideration our rule filing establishing specialized arbitration panels for expungement requests so that we can further consider whether modifications to the filing are appropriate.

FINRA remains committed to working with the SEC and other stakeholders who share a common interest in revising the process for reviewing the information on a broker's record in the Central Record Depository (CRD<sup>®</sup>). Protecting the integrity of the information in the CRD system and BrokerCheck<sup>®</sup> is critical to our mission of investor protection. FINRA is committed to limiting the expungement process so that it operates as intended—as an extraordinary remedy, only appropriate in limited circumstances when the CRD information is clearly inaccurate. We continue to take meaningful steps to enhance controls on the existing expungement process in the near term,



including our specialized panels proposal, while we work concurrently to support the development of fundamental, multi-stakeholder solutions.<sup>2</sup>

**IN 2022, FINRA REFILED PROPOSED RULE CHANGES THAT ARE MORE COMPREHENSIVE AND INCLUDE ALLOWING STATE SECURITIES REGULATORS TO PARTICIPATE IN STRAIGHT-IN EXPUNGEMENT ARBITRATIONS. THE PROPOSED RULE WENT INTO EFFECT ON OCTOBER 16, 2023.**

In August 2022, FINRA filed a new rule proposal with the SEC, SR-FINRA 2022-24, which added needed enhancements to the expungement process. The proposed changes were significantly stronger than FINRA’s prior rule proposal and were met with support from investor advocates, including PIABA and the Foundation. SR-FINRA 2022-24 was approved by the SEC and went into effect on October 16, 2023.

The changes to the expungement process are significant and should make it more difficult for brokers to expunge valid customer complaints. See FINRA Regulatory Notice 23-12 for a complete description and explanation of the new rules. Some of these significant changes are:

- Three Randomly Selected Arbitrators from the Special Arbitrator Roster will decide straight-in expungement requests.

A panel of three arbitrators must be randomly selected from the Special Arbitrator Roster to decide the expungement request. The parties cannot agree to fewer than three arbitrators to decide the expungement request. As a result, parties in straight-in expungement cases (brokers and brokerage firms) are prohibited from ranking and striking the arbitrators, stipulating to an arbitrator’s removal, or stipulating to the use of pre-selected arbitrators – the parties won’t have a say in who will decide the expungement request.

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<sup>2</sup> <https://www.finra.org/media-center/newsreleases/2021/finra-statement-temporary-withdrawal-specialized-arbitrator-roster>

- Straight-in expungements must be filed against the brokerage firm where the complaint arose.

Straight-in expungement requests must be filed under the Industry Code, rather than the Customer Code, against the member firm at which the person was associated at the time the customer dispute arose. Thus, brokers can no longer file expungement cases against a subsequent firm that had no knowledge of the underlying facts about the customer complaint in a proceeding where the customer is not a party.

- Decisions about expungement requests must be unanimous.

The three arbitrators appointed must unanimously agree to award expungement based only on the narrow grounds specified in the rules, (*i.e.*, the claim, allegation or information is factually impossible, clearly erroneous, or false, or the associated person was not involved in the alleged misconduct).

- Strict Time Limitations.

FINRA will deny the arbitration forum for an expungement request if the request is filed: (1) more than two years after the close of the customer arbitration or civil litigation associated with the customer dispute information; or (2) more than three years after the date the customer complaint was initially reported in CRD (if the customer complaint does not evolve into a customer arbitration or civil litigation).

- Direct notice by FINRA to customers whose complaint is the subject expungement request.

The Director of FINRA-DR must now notify all customers whose customer arbitrations, civil litigations or customer complaints are the subject of the expungement request, of the time, date and place of any prehearing conferences and the expungement hearing.

FINRA will also provide the notified customers with access to all documents that are relevant to the expungement request that are filed in (a) the straight-in request and (b) any prior customer arbitration brought by the customer that is a subject of the expungement request. This gives notified customers access to

documents concerning the request for expungement prior to their attendance and participation in the expungement hearing.

- Participation by State Securities Regulators.

FINRA will notify state securities regulators - in the manner determined by the Director in collaboration with state securities regulators - of an expungement request within 15 days of receiving a straight-in expungement request. The new rules also provide a mechanism for state securities regulators to attend and participate in expungement hearings as a non-party in person, or by video conference. Almost all these hearings are conducted virtually.

If an authorized representative of a state securities regulator notifies the Director of FINRA Dispute Resolution no later than 30 days after the last Answer is due that the representative intends to participate in the hearing, the Director will notify the representative of the time, date and place of prehearing conferences and the expungement hearing.

At the expungement hearing, the authorized representative may: (1) introduce documentary, testimonial, or other evidence; (2) cross examine witnesses; and (3) present opening and closing arguments if the panel allows any party to present such arguments. The other participants appearing at the expungement hearing may state objections to the authorized representative's evidence and cross-examine the authorized representative's witnesses. *See* FINRA Regulatory Notice 23-12.

**STATE SECURITIES REGULATORS ARE JOINT OWNERS OF THE DATA CONTAINED IN THE CRD DATABASE, INCLUDING CUSTOMER COMPLAINT INFORMATION.**

As explained above, complaints by investors (customers), including settled FINRA arbitration proceedings, are included in the CRD database and are public records under state laws. Customer complaint information is critical to state securities regulators in carrying out their responsibilities and protecting their states' citizens. State regulators rely on CRD records in deciding whether to permit broker-dealers, investment advisers and their agents to register to do business in their states. Regulators rely on a broker's CRD data in determining whether to discipline an individual and whether the information demonstrates a pattern of unlawful or unprofessional conduct, which may play an important role in a regulator's decision to commence an examination, audit, or regulatory review to determine if an enforcement action is warranted against the broker. Access by state securities

regulators to timely, accurate, and complete information about a securities professional is vital for regulators to carry out their regulatory and investor protection mandate.

FINRA administers the CRD database pursuant to an agreement (“CRD Agreement”) between it and the North American Securities Administrators Association (“NASAA”) on behalf of NASAA’s member states. However, expungement rules are developed and administered solely by FINRA. *See* CRD Agreement, Appendix-A. Section 3.10 (a) of the CRD Agreement states in pertinent part:

**The data on CRD Uniform Forms filed with the CRD shall be deemed to have been filed with each CRD State in which the applicant seeks to be licensed and with the NASD and shall be the joint property of the applicant, NASD, and those CRD States (and, in the case of Forms BD and BDW, the Securities and Exchange Commission). The compilation constituting the CRD database as a whole shall be the property of NASD.**

The CRD Agreement also states that state governments are third party beneficiaries of the CRD Agreement. For example, on page one of the CRD Agreement, the signatories agreed that:

**WHEREAS**, the parties acknowledge that, by virtue of the process established by the CRD for the sharing of Licensing information and the collection of Licensing fees to be paid to the state governments and the proper accounting for and distribution of those fees, state governments are third party beneficiaries of this CRD Agreement; and

Courts have recognized that states' ownership of CRD data and regulatory prerogatives provide a right to intervene in court proceedings seeking to confirm an expungement award.<sup>3</sup>

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<sup>3</sup> *See, e.g., Karsner v. Lothian*, 532 F.3d 876, 885 (D.C. Cir. 2008) (holding the Maryland Securities Commissioner entitled to intervene in proceeding to confirm FINRA expungement award because, *inter alia*, “Maryland has a recognized property interest in the CRD (pursuant to the agreement between NASAA and NASD and Maryland law)”; *In re UBS Fin. Servs., Inc.*, 851 N.Y.S.2d 75 (N.Y. Sup. Ct. 2007) (permitting New York Attorney General to intervene in proceeding

Since state securities regulators are joint owners of the data contained in the CRD database, the information is a public record under state laws. Since under the new rules they will be given notice of expungement requests at the beginning of straight-in expungement arbitrations and have the opportunity to participate and oppose the request(s), it is imperative that state securities regulators evaluate - in each case - whether customer complaint information can and should be erased from the CRD database and their states' public records.

#### **FACTORS THAT MAY IMPACT STATE SECURITIES REGULATORS ABILITY TO EFFECTIVELY PARTICIPATE IN FINRA'S STRAIGHT-IN EXPUNGEMENT ARBITRATIONS.**

While PIABA and the Foundation applaud FINRA for amending its rules to provide state securities regulators with notice and opportunity to participate and oppose expungement requests prior to an award being issued, state securities regulators may need to adapt to FINRA's new rules to be able to effectively participate in the proceedings. Here are several factors that may impact the effectiveness of state securities regulator participation in straight-in expungement arbitrations:

- Limited Resources.

Under the new expungement rules, each state securities regulator in states where a broker is registered will be given notice within 15 days after the straight-in expungement arbitration is filed with FINRA. However, given the current demands and limited budgets of state agencies, it is likely that some states may not have the current resources to fully participate.

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to confirm FINRA expungement award based on New York's property interest in CRD data and fact that "Attorney General clearly has an interest which may be affected by the court's judgment"); *Hernandez v. E\*Trade Securities LLC, et. al.*, (Pa. Ct. Com. Pl. July 22, 2015) (permitting the Delaware Attorney General to intervene and granting in part the Delaware Attorney General's Motion to Oppose confirmation of a FINRA expungement award).

- Short Deadline to Notify FINRA.

Once notified, state securities regulators or their authorized representatives are required to notify the Director of FINRA Dispute Resolution no later than 30 days after the last answer is due whether it intends to attend and participate in the expungement hearing. It is likely that some state securities regulators (particularly those with the most limited available resources) will not be able to evaluate the merits of the expungement requests in a timely manner and make decisions about whether to oppose the expungement request.

- Ability of State Regulators to Obtain Authority to Retain an Authorized Representative.

The new rules contemplate that state securities regulators or their “authorized representative” can participate in straight-in expungements. States widely differ, however, on what steps must be taken to obtain authority from the appropriate state actor to participate in a legal proceeding such as a FINRA arbitration. They also differ on whether and how they can engage a representative, such as outside counsel, to act on their behalf.

Some states prohibit hiring outside counsel altogether, while others permit them in limited circumstances. The differences in processes among states may be an impediment to participation and cause further delays in making decisions about whether to participate. This could limit the effectiveness of FINRA’s intent to make it easier for states to participate by including the “authorized representative” language in the rule.

- Differences in standards applied by state securities regulators in determining whether to oppose expungement.

While FINRA Rule 2080 sets forth the basis for when an arbitrator may grant expungement of customer complaints,<sup>4</sup> state securities regulators are not limited by

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<sup>4</sup> Rule 2080 states that expungement may be granted if (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.

the strict language of the rule about whether to take regulatory action against members of the securities industry.

As a result, state regulators may differ in how they evaluate whether to oppose expungement. They may not give the same weight to certain evidence supporting or refuting the customer complaint and may differ in placing a regulatory value on the substance of the complaint. All of this could lead to differing opinions among state securities regulators about whether to even participate. This issue is particularly important where a broker is registered in multiple states.

It is important to note that any State where a broker is registered may participate in the expungement process. State participation is not limited to the home state of the brokers seeking expungement and there is no prohibition on more than one state participating in the same straight-in expungement arbitration. State regulators have historically and routinely coordinated activities in licensing, registration, examination, and enforcement matters. A similar approach may be appropriate under the new Rules to mitigate potential concerns as mentioned herein.

- Deferring to the Home State of the Broker to Oppose Expungement.

Every broker must be registered with the securities regulators in each state where the broker intends to do business. As a result, it is common for brokers to be simultaneously registered in multiple states. For example, in deciding whether to take regulatory action against a broker, it is customary for state securities regulators to defer to the home state of the broker about whether the home state would prefer to act. This process could very well lead to delays in decision-making and inconsistent evaluations. Coordinated information or review processes or procedures could potentially mitigate these concerns, as the States have tackled similar issues in the past.

- Unfamiliarity with Arbitration Process.

State securities regulators are familiar with court and/or administrative proceedings in carrying out their duties and responsibilities but practicing law in FINRA arbitration will be somewhat foreign to many regulators. The arbitration procedural rules contained in FINRA's Codes of Arbitration are different in many ways from administrative and court procedures. Many of the legal claims arbitrated before FINRA arbitration are different from those pursued by state securities regulators in enforcement actions.

FINRA's discovery process is more limited than what is available in court, (e.g., depositions are not typically permitted). The documents that are relevant to prove the claims and defenses asserted in arbitration can be different from what may be relevant to typical actions taken by state securities regulators. Finally, and importantly, arbitrators act as the judge *and* jury and they may analyze the strength of an investor's complaint differently from the way regulators do.

Navigating through a hearing with limited documents and information to oppose expungement will likely entail a learning curve for state regulators' effective participation.

## **STUDY METHODOLOGY**

In preparing this 2023 Updated Study, the Foundation supplemented its analyzed data from the 2019 and 2021 Studies that it requested and received from Securities Arbitration Commentator (SAC). The Foundation is grateful to SAC. In the newest compilation of data, SAC provided all arbitration awards issued in straight-in expungement cases from November 1, 2020, through August 31, 2023 (the "Review Period"). The results of the analysis from 2019 and 2021 Studies, January 1, 2015-October 31, 2020, are also listed below along with the updated data to better demonstrate long-term trends.

The Foundation requested SAC to 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) CRD No. of Broker;
- (j) Name of Broker's Attorney (Firm);
- (k) Whether Respondent BD Objected to Expungement;
- (l) Whether Customer Objected to Expungement;
- (m) Number of customer complaints requested to be expunged;
- (n) Result of Expungement Request



- (o) Name of broker whose request was granted;
- (p) Name of broker whose request was denied
- (q) Name of Arbitrator;
- (r) Number of Hearing Sessions.

*See SAC Spreadsheet #1, Appendix-B.*

The Foundation also relied on the data from the 2021 Study and combined it with the new data to analyze 2506 awards issued from January 1, 2019, to August 31, 2023, to identify the home states of the brokers who requested expungement. The Foundation received the home state information for each broker from the Alabama Securities Commission. (*See Spreadsheet #2, Appendix-C.*)

This Study supplements PIABA's and the Foundation's 2019 and 2021 Studies and provides updated data about the outcomes of 1501 straight-in expungement awards issued from November 1, 2020, through August 31, 2023.

This Study also analyzed 2506 awards issued from January 1, 2019 to August 31, 2023 to identify the home state(s) of the brokers who requested expungement. Our hope is that this information will help state securities regulators coordinate and share resources to participate in straight-in expungement arbitrations more efficiently and effectively.

The 2019, 2021, and 2023 Studies collectively provide a comprehensive view and analysis of the straight-in expungement award outcomes for eight and-a-half years - from January 1, 2015, to the end of August 2023. Since FINRA's new expungement rules went into effect on October 16, 2023, this Study provides a snapshot about key data points on expungement rates that can be used as a comparison for future studies to evaluate whether FINRA changes were effective.

## **RESULTS OF 2023 STUDY**

### **I. Summary of Award Analysis**

#### **A. Expungements Are Not Being Treated as an Extraordinary Remedy.**

##### **2019 Study:**

The 2019 Study showed that from January 1, 2015, to June 30, 2019, expungement requests were granted 81% of the time. There was no significant difference between expungement rates between a panel of three arbitrators and a single arbitrator. The data further showed that in 2018, panels of three arbitrators granted expungement requests 88% of the time, and single arbitrator panels granted expungements 87% of the time.

##### **2021 Study:**

The data showed that from July 2019 to October 31, 2020, expungement requests were granted in 90% of the straight-in expungement cases and that a panel of three arbitrators was not more likely to deny expungement requests than a single arbitrator. The data shows that panels of three arbitrators granted expungement requests 89% of the time and a single arbitrator granted them 84% of the time.

##### **2023 Updated Study:**

The new data from January 1, 2019, through August 31, 2023, shows that expungements were granted in approximately 90% of the straight-in expungements. Out of 2506 awards issued, expungement was granted in 2259 cases (90%).

Comment: PIABA and the Foundation are hopeful that the new expungement rules will result in a significant reduction in the percentage of expungements being granted as a result of participation by state securities regulators and enhanced notice to customers. As PIABA and Foundation showed in the Studies arbitrators are many times more likely to deny expungement requests when they are presented with evidence opposing the relief.

## **B. Number of Expungement Requests Remained High.**

### **2019 Study:**

The 2019 data from January 1, 2015, to June 30, 2019, 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. A straight-in expungement case is an arbitration initiated by a broker against their own member firm solely for the purpose of seeking expungement of a customer complaint on their record. The customer who made the complaint is not a party to such proceedings.

### **2021 Study:**

The 2021 data from July 1, 2019, through October 31, 2020, showed that the number of expungement requests per year remained exceedingly high. There were 700 expungement awards from August 1, 2019, to October 31, 2020.

### **2023 Updated Study:**

The newest data from January 1, 2021, to August 31, 2023, confirmed that the number of expungement awards remained high. In 2021, there were 758 awards.

Comment: PIABA and the Foundation anticipate that the new expungement rules will significantly reduce the number of straight-in expungement requests because, under the new rules, FINRA will deny the arbitration forum for an expungement request if the request is filed: (1) more than two years after the close of the customer arbitration or civil litigation associated with the customer dispute information; or (2) more than three years after the date the customer complaint was initially reported in CRD (if the customer complaint does not evolve into a customer arbitration or civil litigation).

**C. Average Number of Complaints Sought to be Expunged per Case Remained 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. Brokers requested that 2,194 customer complaints be expunged in 1,078 arbitration awards issued from January 1, 2015, to June 20, 2019, an average of two complaints per case. In 2018, the highest number of customer complaints put at issue in one case was 13.

**2021 Study:**

The new data from July 1, 2019, through October 31, 2020, showed that the number of expungement requests per case continued to be high. Brokers requested arbitrators to expunge 1,360 customer complaints in 700 cases, averaging two complaints per case. The highest number of complaints sought to be expunged in a single case was 29.

**2023 Updated Study:**

The data from November 1, 2020, through August 31, 2023, is consistent with the previous Studies. Brokers requested to expunge 3,213 customer complaints in 1501 cases, averaging more than two customer complaints per case. The highest number of complaints sought to be expunged in a single case was 32.

Comment: Under the new rules, brokers can still bring cases involving multiple occurrence numbers, but now must comply with all the other requirements (naming all the appropriate firms as respondents, serving all the investors, etc.) PIABA and the Foundation are hopeful that this additional safeguard will curtail the number of complaints per case and may serve as a red flag to securities regulators that may lead to their increased participation.

**D. Brokerage Firms Do Not Oppose Expungement Requests.**

**2019 Study:**

The 2019 Study showed that expungement proceedings were rarely adversarial. Of the 1,078 cases analyzed, respondent brokerage firms did not object

or otherwise oppose brokers' expungement requests 1,055 times – that is, over 98% of the time. This demonstrated that brokers and their firms had and still have a common interest in erasing customer complaints from brokers' records and, as a result, are not truly in opposition to each other in straight-in expungement cases.

### **2021 Study:**

The data showed that straight-in expungements continued as non-adversarial proceedings and that brokerage firms continued not to oppose expungement requests 98% of the time.

### **2023 Updated Study:**

The new data from January 1, 2019, through August 31, 2023, showed that straight-in expungements continued as non-adversarial proceedings and that brokerage firms continued not to oppose expungement requests 92% of the time.

Comment: The new rules require brokers to name the brokerage firm that received the customer complaint, not the current brokerage firm with whom the broker is associated, which typically has no direct knowledge about the complaint and has an incentive to erase the customer complaint. PIABA and the Foundation are hopeful that this additional safeguard will curtail the number of complaints per case and may result in brokerage firms objecting more frequently to straight-in expungement requests. We also hope that a brokerage firm objection may serve as a red flag to securities regulators and may lead to their increased participation.

### **2019 Study:**

The 2019 Expungement Study revealed that of the 1,078 expungement cases filed between 2015 and 2019, customers opposed the expungement requests only 141 times – that is, approximately 13% of the time.

### **2021 Study:**

The 2021 data showed that customers continued not to participate in the vast majority of expungement proceedings. Customers opposed expungement requests only 106 times – that is, approximately 15% of the time. Arbitrators were routinely deciding expungement requests without input from anyone other than the broker and brokerage firm, which have a common interest in expungement relief being granted.

### **2023 Updated Study:**

The new data from January 1, 2019, through August 31, 2023, shows investors continued to not participate in straight-in expungement cases. During this period, customers participated in only about 10% of the cases.

Comment: To help facilitate customer awareness of and participation in straight-in requests, the amendments require a broker seeking expungement relief *and* the Director of FINRA Dispute Resolution provide notifications to customers.

Specifically, the amendments require that the associated person (broker) serve all customers whose customer arbitrations, civil litigations or customer complaints are the subject of the expungement request with a copy of the statement of claim requesting expungement and any answer within 10 days of filing. The associated person must provide a current address for the customer, or the expungement request will be considered deficient and will not be served. The associated person must also file with the panel proof of service to the customers of the statement of claim filed by the associated person and any answers filed by a member firm, copies of all documents provided by the associated person to the customers and copies of all communications sent by the associated person to the customers and any responses received from the customers.

Furthermore, the amendments require the Director to notify all customers whose customer arbitrations, civil litigations or customer complaints are the subject of the expungement request of the time, date and place of any prehearing conferences and the expungement hearing. The Director will also provide the notified customers with access to all documents that are relevant to the expungement request that are filed in (a) the straight-in request and (b) any prior customer arbitration brought by the customer that is a subject of the expungement request. This provides the notified customer with access to documents surrounding the request for expungement prior to their attendance and participation in the expungement hearing.

PIABA and the Foundation are expanding their *pro bono* expungement program, which arranges for attorneys to provide free representation to investors who wish to participate and oppose expungement. We are hopeful that this more robust notice to investors and the expanded *pro bono* expungement program will result in more investors choosing to participate and oppose expungement when appropriate.

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

### **2019 Study:**

The 2019 Study showed that arbitrators are four 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 opposed expungement requests only 141 times – approximately 13% of the time. Over the entire period analyzed, the study found 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 four times more likely to deny an expungement request when customers object.

### **2021 Study:**

The 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.

### **2023 Updated Study:**

The new data shows that when customers opposed expungement, arbitrators denied expungement requests about 31% of the time as opposed to 10% when no one objected. So, arbitrators are over three times more likely to deny expungement requests when customers participate, which confirms the value of having someone appear to present evidence in opposition to expungement and that the Foundation's *pro bono* program works. This figure is consistent with the findings in our prior studies.

## **II. Arbitration Awards Analysis of the Home States of Brokers Seeking Expungement.**

As stated above, this Study also analyzed 2,506 awards issued from January 1, 2019 to August 31, 2023 to identify the home state(s) of the brokers who requested expungement. It is customary for securities regulators to defer to the home state of brokers to determine whether that state intends to take regulatory action. As explained below, however, deferring solely to brokers' home states may not be the most equitable, efficient or effective way to decide whether and how state securities

regulators participate in straight-in expungement arbitrations. The results of the straight-in expungement awards by brokers' home state are graphically illustrated in the attached map entitled, *Expungement Awards by Brokers' Home State*.

#### **A. Review of Expungement Awards by Brokers' Home State(s).**

As illustrated in the attached map, the first tier ("Tier 1") home states in terms of number of straight-in expungement awards (range of 91-400 awards) included, California (315), Florida (388), New Jersey (179), New York (262), and Texas (157).<sup>5</sup> The total number of awards in Tier 1 is 1,301 or 54% of all straight-in expungement awards.

The second tier ("Tier 2") home states in terms of the number of straight-in expungement awards (range of 51-90 awards) included, Arizona (64), Connecticut (65), Illinois (69), Massachusetts (55), Pennsylvania (88), and Washington (55). The total number of awards in Tier 2 is 396 or 17% of all straight-in expungements awards.

The third tier ("Tier 3") home states in terms of number of straight-in expungement awards (21-50 awards) included, Alabama (22), Colorado (41), Georgia (47), Illinois (69), Indiana (21), Louisiana (27), Maryland (28), Michigan (47), Missouri (27), North Carolina (46), Nevada (24), Ohio (42), Oregon (22), South Carolina (27), Tennessee (28) and Utah (22). The total number of awards in this Tier 3 is 540 or 23% of all straight-in expungement awards.

The fourth tier ("Tier 4") home states in terms of number of straight-in expungement awards (10-20 awards) included, Iowa (11), Kansas (19), Kentucky (15), Minnesota (20), Nebraska (10) and New Hampshire (16). The total number of awards in Tier 4 is 91 or 4% of all straight-in expungement awards.

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<sup>5</sup> It is worth noting that Puerto Rico was the home territory for 118 straight-in expungement awards, which is a significant number. Going forward, however, the authors do not believe that Puerto Rico will continue to have such a large number because the expungement requests related to the failure of an investment that was unique to Puerto Rico and the new two-year, three-year time limitations will likely preclude many new requests from being eligible for expungement. As a result, the Study exclude the 118 awards from computing the overall percentages of awards by state.



The fifth tier (“Tier 5”) home states in terms of number of straight-in expungement awards (1-9 awards) included, Alaska (1), Arkansas (4), District of Columbia (6), Delaware (6), Hawaii (5), Idaho (7), Maine (1), Mississippi (2), Montana (5), North Dakota (1), New Mexico (3), Oklahoma (9), Rhode Island (4), South Dakota (6), Vermont (5), West Virginia (3), Wyoming (1). The total number of awards in Tier 5 is 69 or 3% of all straight-in expungement awards.

**B. The number of awards per home state correlates to the number of brokers registered in those states.**

The number of straight-in expungement awards by state is consistent with the number of brokers registered in those states, (i.e., more state registrations = more awards). According to FINRA’s 2023 *Financial Industry Snapshot* report, Tier 1 home states with the most expungement awards also had the most broker registrations in the country in 2022, i.e., California (324,424); Florida (329,382); New York (309,303); New Jersey (236,303); Texas (303,897).<sup>6</sup> See Appendix-D, FINRA’s 2023 *Financial Industry Snapshot* at pg.11-12.

Except for New Jersey, these same states had the most branch offices in the country in 2022, i.e., California (15,626); Florida (11,200); New York (9,363); New Jersey (4,463); and Texas (10,757).<sup>7</sup> As stated above, the five Tier 1 home states collectively had 1,301 or 54% of all straight-in expungement awards.

Likewise, Tier 5 home states with the fewest expungement awards tended to have the fewest broker registrations in 2022, e.g., North Dakota (121,819); Alaska (131,171); South Dakota (137,215); West Virginia (138,832); Wyoming (139,468). These five Tier 5 home states collectively had 12 or .5% of all straight-in expungement awards.

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<sup>6</sup> <https://www.finra.org/sites/default/files/2023-04/2023-industry-snapshot.pdf>

<sup>7</sup> See FINRA’s 2023 *Financial Industry Snapshot* at 22-23.

**C. It is Common for Brokers to be Simultaneously Registered in Multiple States. On average, Brokers are Registered in Approximately 16 Different States at the Same Time.**

In 2022, there were a total of 620,882 registered representatives regulated by FINRA and in turn, state securities regulators.<sup>8</sup> The 2023 *Financial Industry Snapshot* provides a geographic breakdown by state of the number of registered representatives registered in each state.<sup>9</sup> The chart shows that the total number of registered representatives registrations in all states is 10,164,903, which means that on average, brokers are registered in approximately 16 different states at the same time.

**D. Because Brokers are Registered in Multiple States, Significant Opportunities Exist for State Securities Regulators to Benefit From Coordinating and Sharing the Responsibility of Participating in Straight-in Expungements with Negligible Impact on Existing State Resources.**

As explained above, any state where a broker is registered may participate in the expungement process. State participation is not limited to the home state of the brokers seeking expungement and there is no prohibition on more than one state participating in the same straight-in expungement arbitration.

If the historical trends hold true, the five Tier 1 states, California, Florida, New Jersey, New York, and Texas will continue to be the home states for at least 50% of all straight-in expungement awards. The other 50% of awards, however, will be divided between the other states and territories.

The data showed a significant drop in the average number of straight-in expungement awards between the home states among the tiers described above. For example, from January 1, 2019 to August 31, 2023, the average number of awards in Tier 1 home states was 260; Tier 2 home states (66); Tier 3 home states (34); Tier 4 home states (15); and Tier 5 home states (4).

Broken down annually, the numbers equate to Tier 1 home states (75/year); Tier 2 (19/year); Tier 3 (10/year); Tier 4 (4/year); and Tier 5 (1/year).

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<sup>8</sup> See 2023 *Financial Industry Snapshot* at page 2.

<sup>9</sup> *Id.* at 11-12.

It is anticipated that the new rules will significantly reduce the number of straight-in expungement requests annually. The strict times lines and additional procedural safeguards included in the new rules, it is very likely that the total number of straight-in expungement requests filed per year will drop at least 50%.

As a result, relying solely on the brokers' home state to decide whether to participate in expungements may not be the most equitable, efficient, or effective approach, especially for Tier 1 states, since it is extremely likely that the brokers whose home states are in Tier 1 will also be registered in some or all of the other states in Tiers 2-5.

It is certainly plausible that is states coordinated and shared the responsibility of participating in straight-in expungements – even if brokers are not in their home state – they could achieve 100% participation in straight-in expungement arbitrations with negligible additional impact on existing state resources.

Coordination among state regulators will also mitigate the factors described above that may impact the effectiveness of participation in straight-in expungement arbitrations, i.e. (1) solve the limited resource issue; (2) overcome risk of not participating as a result of the short deadlines to notify FINRA; (3) increase likelihood of obtaining authority to participate; (4) create a more uniform standard to determine whether to oppose expungement; and (5) more efficiently become familiar with the arbitration process.

## **CONCLUSION**

PIABA and the Foundation have conducted multiple studies analyzing FINRA's expungement awards for over a decade and the results are clear. The studies have had a positive influence on improving the process.

The data unquestionably leads to the conclusion that the most effective way to reduce the rate of expungements of valid customer complaints being granted is to stop the practice of arbitrators deciding expungement based on one-sided presentations of evidence. FINRA's new expungement rules are a significant improvement to the expungement process, particularly for straight-in expungement cases.

PIABA and the Foundation are hopeful that the changes will provide a meaningful opportunity for state securities regulators and aggrieved investors to participate and present evidence opposing invalid expungement requests.

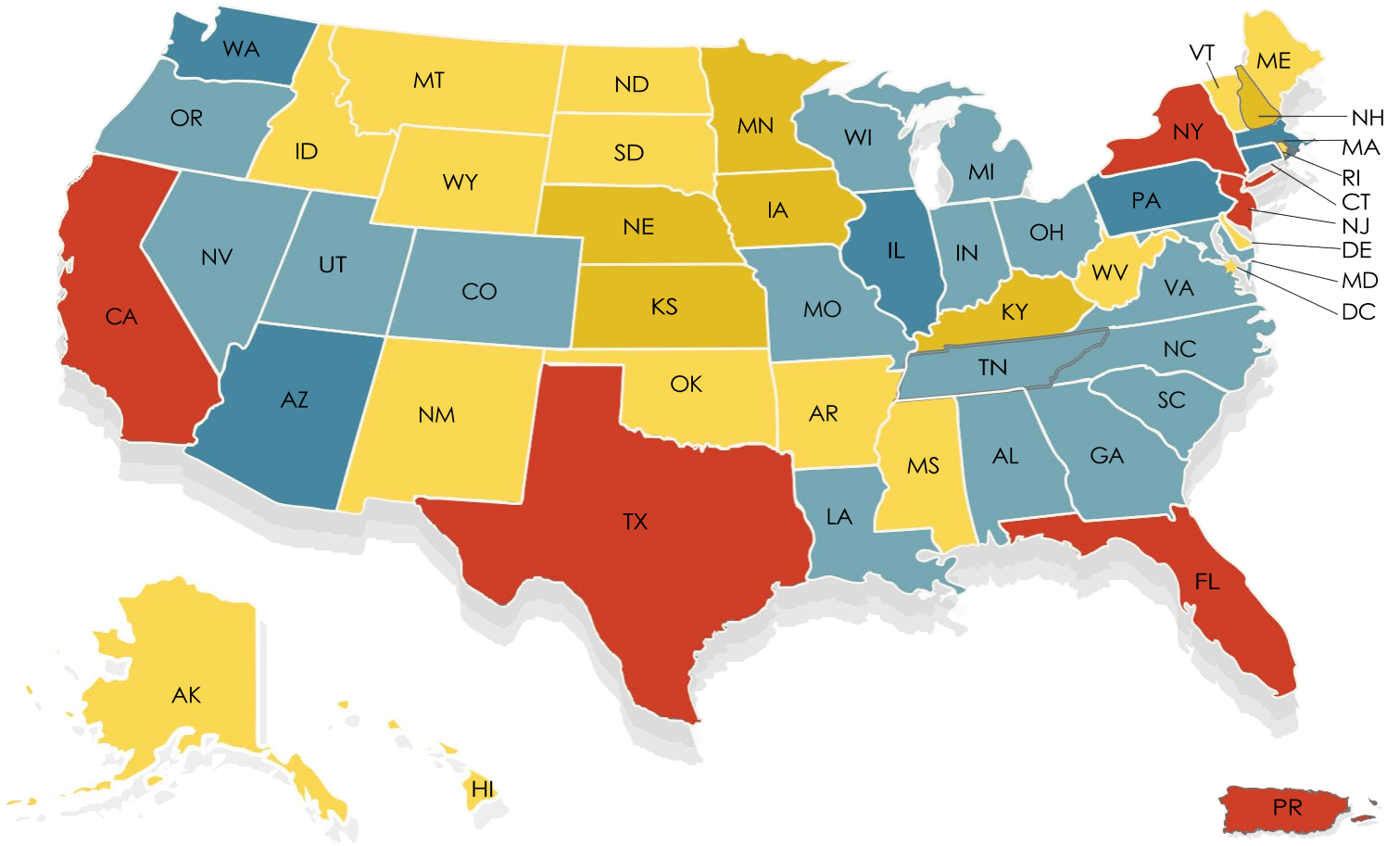
The attorneys who represent investors in FINRA arbitration, including the PIABA's membership and those who work with the PIABA Foundation, are also stakeholders in the outcome of expungement requests, because the integrity of their clients' claims and the integrity of FINRA's arbitration forum hang in the balance. One-sided and misleading, and/or incomplete presentations of facts and law by brokers and their firms to chair-qualified arbitrators in straight-in expungements risks leading the arbitrator pool to believe that many, if not most, customers and lawyers representing customers make false complaints. This permanently damages the fundamental fairness of FINRA's arbitration process in future customer arbitrations.

As a result, PIABA and Foundation volunteers should have a meaningful role in improving what has been a broken system. It is our hope that by continuing to study this issue, volunteering our time representing investors through the *pro bono* expungement program, and helping state securities regulators effectively and efficiently participate in FINRA's straight-in expungement arbitration, PIABA and the Foundation can do our part to improve the process to protect the integrity of the regulatory record.

# EXPUNGEMENT AWARDS BY BROKERS' HOME STATE

(January 1, 2019 – August 31, 2023)

(On average, brokers are registered in 16 different states at once)



TOTAL NUMBER OF EXPUNGEMENTS PER STATE



Alaska-1	Illinois-69	North Dakota-1	South Dakota-6
Alabama-22	Indiana-21	Nebraska-10	Tennessee-28
Arkansas-4	Kansas-19	New Hampshire-16	<b>Texas-157</b>
Arizona-64	Kentucky-15	<b>New Jersey-179</b>	Utah-22
<b>California-315</b>	Louisiana-27	New Mexico-3	Virginia-36
Colorado-41	Massachusetts-55	Nevada-24	Vermont-5
Connecticut-65	Maryland-28	<b>New York-262</b>	Washington-55
District of Columbia-6	Maine-1	Ohio-42	Wisconsin-24
Delaware-6	Michigan-47	Oklahoma-9	West Virginia-3
<b>Florida-388</b>	Minnesota-20	Oregon-22	Wyoming-1
Georgia-47	Missouri-27	Pennsylvania-88	
Hawaii-5	Mississippi-2	Puerto Rico-118	Total Awards-2506
Iowa-11	Montana-5	Rhode Island-4	
Idaho-7	North Carolina-46	South Carolina-27	