Barry D. Estell
ATTORNEY AT LAW
6140 Hodges Drive
Phone (913) 722-5416 **Mission, Kansas 66205** E-mail bestell@kc.rr.com

Marcia E. Asquith
FINRA Office of the Corporate Secretary

In re Expungement Procedures for Persons Not Named in a Customer-Initiated Arbitration

I am a lawyer and industry arbitrator who has represented customers in NASD/FINRA arbitration for 19 years and served as an expert witness in forced securities arbitration since its inception. I currently provide expert services to customers and represent several brokers and brokerage firms in regulatory matters.

This is a terrible rule contrary to any concept of customer protection. It denies the investing public meaningful information in selecting a financial advisor while also denying the same information to brokerage firms and state regulators. Small firms have a limited ability to pay for extensive background checks when recruiting experienced reps and rely on the CRD as do state regulators for registration and investigation. There is at least one registered person out there with more than 20 expunged arbitration settlements, mostly purchased; laughing all the way to his next fraud victim. That is not acceptable and FINRA should not make it worse.

There is absolutely no need for this rule. The three stated reasons given by FINRA are nonsense.

> (1) Its unfair for an unnamed rep to rely on a current or former firm to request expungement. Well it's really unfair for an elderly widow to have to depend on a current or former firm to protect her from a predatory broker, but they do to their detriment. If the broker believes that the firm has not treated him or her fairly, they can file an employment case against the firm for misrepresenting the customer claim. It's not like the CRD reports accurately describe the complaint. They are in most cases self-serving and dismissive of the customer. If the customer loses the arbitration, it will reflect that. If the firm settles, it will report that it did so solely for the purpose of avoiding the costs of litigation for a meritless claim. The exception is when the firm is retaliating against a broker for one reason or another. In that instance, it's an employment issue and the customer should be left out of it.
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> (2) FINRA believes the customer's arbitration case should not be disrupted or delayed to address an issue that may have no bearing on the outcome of relief granted. What nonsense. In order to not delay the underlying case FINRA proposes to drag the customer into months of further motion practice, abuse, and harassment. That is simply ridiculous. To subject a customer to further expense even after the award or settlement should not be allowed. If the unnamed party

believes he or she can demonstrate the claim meets any of the requirements for expungement, the introduction of the evidence doing so belongs in the underlying hearing where all of the evidence is presented, not later without opposition.

(3) FINRA believes that neither the firm nor the customer should be required to incur the additional expense of participating. The customer may have no choice. There being only one party to please, the arbitrator is unlikely to deny discovery and appearance orders to the party seeking relief. In all likelihood the current employer is backing the effort in order to assist a compliance challenged but highly profitable rep. Customer's will be subjected to unrelenting harassment until they write a letter to the "appointed" arbitrator confessing to making the entire story up and asking for expungement.

Customers will be further discouraged from filing any arbitration claims, especially smaller claims, as they are subjected to additional harassment. Consider the gauntlet confronting a defrauded customer:

(1) They must pay thousands of dollars in filing fees that they would not be forced to pay if allowed to go to court;

(2) They face the likelihood of thousands of additional dollars in costs for the prehearing motion practice before the even more expensive hearing fees.[1]

(3) Win or lose, the investor would, under this rule, be subject to post hearing costs for production of documents and possible travel expense to a distant hearing site. Even if the customer "wins" an award in the underlying case, the rep can still file for expungement since he or she wasn't represented at the hearing and can claim to be an innocent bystander. This would be especially true in product cases.

(4) Attorneys willing to accept smaller cases from working people without substantial up-front cash will become even scarcer. The prospect of either dumping the client after the evidentiary hearing or agreeing to further months of FINRA motion practice on a pro bono basis is not attractive in an already low margin practice area. The result will be that small cases will be without an experienced lawyer where the customer "win" ratio is even worse.

(5) Discovery subpoenas (enforceable in court) can be expected to be far more extensive and invasive than for the evidentiary hearing. Especially if the customer is given some modest award, the broker will be demanding bank records and highly personal and confidential financial records to prove to the single arbitrator that a major miscarriage was done and had the broker had the opportunity to participate

[1] In the 40% of cases where customers are awarded anything, it is not uncommon for fees to amount to a very high percentage of the award even before attorney fees.

with the relevant evidence, it would have been different. What is an unrepresented customer to do except fold and give the brokers (and FINRA) everything they want. It will even make FINRA's pathetic win percentage and award to damages ratio look better with all these people admitting frivolous claims.

In fact, the multi-page discovery subpoena issued to the customer months after the award is issued or the motion to vacate is decided, may be the customer's first notice that "it ain't over." In addition to the now common practice of some firms to move to vacate each and every monetary award, customers can expect another round with the expungement proceeding as standard. Except for the most well-heeled investor the prospect of seemingly endless costs and fees even after the arbitration hearing can only serve as further disincentive for a defrauded investor to file a claim in the first place; which may be the intended result of this rule if not the stated intent.

One needs to consider why investors in arbitration do not "name" the individuals responsible for the complaint. It is because FINRA arbitration is designed to disadvantage investors and favor member firms. If a defrauded investor names both the broker and the firm, two things can happen, both bad for the investor:

(1) There may be two separately represented parties which together dominate the list selection procedure, insuring that any arbitrator who has ever hinted sympathy for defrauded widows and orphans is stricken leaving only industry dependable names who will never give a customer a fair hearing;

(2) In the unlikely case that a customer is given a substantial award, it may be awarded only against the individual representative who is judgment proof and not against the firm which has the ability to pay. This is a practice cultivated by FINRA even though contrary to state and federal law. Many, perhaps most claimant lawyers believe it foolish to name an individual who can not pay and risk an empty award.

After engineering the arbitration rules to discourage naming a rep, FINRA maintained that if an arbitration claim didn't name the individual representative, it wasn't a "written customer complaint" and didn't need to be reported. Thousands of instances of misconduct were effectively hidden from investors, state regulators, and other brokerage firms by this SRO sleight of hand. Having made the rational decision that a written arbitration claim was a written customer complaint even if not naming the individual, FINRA now seeks to circumvent the fix for this outrageous practice by circumventing its own rules. Because investors lose the majority of cases that go to a hearing[2], most of those cases as well as those that result in a settlement will seek expungement.

[2] Historically, customers receive, on average, zero in 60% of the cases reported and the "lucky" 40% can expect only 30% of their damages for an effective 12% recovery rate, half of which awards were never fully paid. For large wire houses the percentage of customer "wins" is lower and the few awards given are closer to 10% of damages. Securities fraud is a very profitable business with little downside courtesy of FINRA.

Customers who settle will be forced to agree to it or face additional motion practice from the unnamed broker with no opportunity for any additional compensation. FINRA will "appoint" a special arbitrator who will be asked to expunge the record without opposition. The arbitrator has little choice but to go along. Only one side will be represented. It's like a default judgment. Alternatively, the customer could, at great personal expense, hire counsel to fight the expungement. But it is unlikely that many investors having already been defrauded by the broker and betrayed by FINRA would use any portion of the money they have left to prevent an expungement that FINRA encourages.

By colluding with the brokers of the most questionable character to deny investors, state regulators and other brokerage firms a true picture of a registered representative, FINRA continues to be a huge part of the problem. Expungement should not be allowed in any case and certainly not in a procedure designed to produce a default judgment with extensive additional cost and inconvenience to the now unrepresented customer.