October 12, 2020

Via Electronic Submission
J. Matthew DeLesDernier
Assistant Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090
rule-comments@sec.gov

Re: File Number SR-FINRA2020-030

Dear Assistant Secretary DeLesDernier:

I write to comment on the series of changes to FINRA's expungement process proposed by SR-FINRA 2020-030 (the Proposal) and thank the Commission for requesting comment on the Proposal. I am an Associate Professor of Law at the University of Nevada, William S. Boyd School of Law. I have carefully studied the current FINRA-facilitated expungement process and do not believe that the Proposal addresses the core problems with the process. Many of my concerns about the current process are detailed in the attached law review article, *Adversarial Failure*, which is forthcoming in the *Washington & Lee Law Review*.[1] I have also personally represented customers opposing expungement requests on a pro bono basis. My experiences with the process only increased my concern about the current expungement system.

The Commission should require more significant changes to the expungement process from FINRA because the Proposal does not address the core problem underlying the current, fundamentally broken expungement process. In essence, the Proposal's expungement process improperly relies on an adversarial system to surface information relevant to whether customer dispute information should be expunged. This adversarial system fails to function in any reliable way because expungement hearings generally proceed as one-sided affairs which are functionally *ex parte* proceedings. In these functionally *ex parte* proceedings, arguments and evidence submitted by brokers seeking expungement never receive any real scrutiny by anyone well-situated to carefully consider these expungement requests. When arbitrators recommend expungement, courts—which are generally precluded from closely reviewing the underlying arbitration absent the rarest of circumstances—then confirm the arbitration awards. Judicial review under these circumstances provides no meaningful check on this process and only serves as a dubious veneer.

The Commission should carefully consider the Proposal because the current expungement process frustrates investor protection goals, the ability of state securities regulators to oversee their markets, and FINRA's own ability to oversee its member firms and associated persons. In my comments below, I address general concerns with the current process and explain how the Proposal fails to cure the core problems.

[1] I have attached the most recent proof of the article to this letter as Exhibit A.

I. The Expungement Process Facilitates Suppressing Information Vital to Investor Protection

The Proposal must be evaluated in light of what we know about the current expungement process. Significant evidence indicates that the expungement process actually suppresses important public information and tends to increase financial misconduct. A study forthcoming in the *Journal of Financial Economics* helps to quantify how the current process suppresses information indicating that particular brokers pose significant risks to the public.[2] Notably, the authors find that a broker who secures an expungement through the current process "are 3.3 times as likely to engage in new misconduct as the average broker."[3] This finding establishes that the current expungement process frustrates investor protection goals because it removes information with tremendous predictive power. Notably, the Proposal cites to an earlier version of this study yet fails to direct the Commission to the most recent draft.[4]

The removal of this information substantially harms the public interest. When information disappears from the CRD database, state regulators cannot use it to target limited enforcement and oversight resources. Investors also suffer in multiple ways. At the outset, investors cannot easily discover and use deleted misconduct information to avoid higher-risk brokers. Other investors who are later harmed by these brokers will also struggle to introduce information about past misconduct into arbitration hearings. Deprived of relevant information with significant predictive power, arbitrators may not be as ready to believe a customer's claims when a broker appears to have a "clean" record. The current expungement process also frustrates FINRA's ability to hold brokers accountable in disciplinary proceedings.

II. Expungements Now Make Brokers More Likely to Engage in Misconduct

The Proposal also requires close review because significant evidence indicates that the current expungement process apparently makes brokers more dangerous to the public. In the same academic study referenced above and also cited by FINRA in its Proposal, the authors found "evidence that brokers who receive expungement are more likely to reoffend than brokers denied expungement."[5] Honigsberg & Jacob explained reasons why brokers who receive expungements may be more likely to reoffend than similarly situated brokers whose expungement requests were unsuccessful. Successful expungements may embolden a broker to engage in more misconduct because of "overconfidence that he can obtain another expungement" or because of "the incentives created by FINRA's accelerating sanctions regime."[6] FINRA's sanctions regime imposes heightened penalties as brokers accumulate complaints. This means that brokers with complaints on their records face potentially harsher penalties than the brokers who have successfully deleted their prior customer complaints. At the

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[2] Colleen Honigsberg & Matthew Jacob, *Deleting Misconduct: The Expungement of BrokerCheck Records*, J. FIN. ECON. (forthcoming 2020) (hereinafter *Deleting Misconduct*) . A copy of this article has been attached as Exhibit B.

[3] *Id.* at 4.

[4] *See* Proposal at 81, Footnote 189 (citing to the 2018 draft). The Proposal also does not highlight the finding that brokers who receive expungements pose more than three times as much future risk to investors as the average broker.

[5] *Deleting Misconduct*, at *Abstract*.

[6] *Id.* at 5-6.

margin, this means that brokers with complaints on their records have a greater incentive to avoid misconduct than the brokers who successfully expunge customer dispute information. Expungements reduce the incentive to avoid misconduct and, predictably, generate significant harm to investors.

III. Expungements Are Functionally *Ex Parte Hearings* And Require Full Candor from Any Party Seeking Expungement

Our adversarial system of justice implicitly assumes arbitral tribunals will reach informed decisions because each side will investigate the matter and bring forward facts relevant to the dispute. In theory, clashing parties will hold each other accountable and point out any errors, allowing adjudicators to reach informed decisions.[7]

But this does not happen in expungement proceedings. Only in rare circumstances will any party bring forward facts militating against recommended expungements. Only in the rarest circumstance will any respondent even attempt to address any error which might bias an arbitration panel. In reality, these expungement hearings most closely resemble *ex parte* hearings. The law already requires expanded duties of candor from all parties and representative advocates. The Commission cannot rely on an adversarial system to generate informed decisions by arbitrators attempting to decide whether or not to recommend expungement. In "straight-in" expungement filings, the interests of the broker seeking expungement and the broker's current employer (named as a nominal defendant) align. To the extent a broker identifies a former employer, the former employer generally lacks any real incentive to invest time and treasure to oppose the broker's expungement request.

Using an adversarial arbitration process to uncover truth makes little sense when both the claimant and the respondent desire the same outcome. Under these circumstances, the Commission can have no confidence that arbitration processes will surface any information indicating an expungement should be denied.

A. Claimant and Respondent Interests Often Align in Expungement Hearings

In "straight-in" expungement requests, the claimant (a broker seeking an expungement) and the respondent (a firm which will benefit if its employee has a clean record) want the same outcome.[8] Tellingly, law firms often sue their own clients to obtain expungements for brokers employed by their brokerage firm clients. As a general matter, conflict of interest rules prohibit lawyers from suing their own clients if their obligations to a client would materially limit their ability represent another client. Concurrent representation of one client against another also requires informed consent from all clients involved.[9] Clients consent to their own lawyers suing

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[7] *See* MODEL RULES OF PROF'L CONDUCT, preamble [8] (AM. BAR ASS'N 2020) ("When an opposing party is well represented, a lawyer can be a zealous advocate on behalf of a client and at the same time assume that justice is being done.").

[8] The proposal refers to expungement requests separate from a customer arbitration as "straight-in" requests. Proposal at 1-2.

[9] *See* ABA Model Rule, 1.7, cmt. [6] ("absent consent, a lawyer may not act as an advocate in one matter against a person the lawyer represents in some other matter, even when the matters are wholly unrelated. The client as to

them because they benefit if an expungement action naming them as a respondent succeeds. Consider two different arbitration awards involving lawyers at Ulmer & Berne, LLP. In one action, Ulmer & Berne lawyers successfully represented a claimant seeking an expungement in an arbitration naming Cetera Advisor Networks as a respondent.[10] The arbitration was filed on or around December 6, 2018 and concluded on August 5, 2019.[11] At the same time, Ulmer & Berne lawyers defended Cetera Advisor Networks in an arbitration filed on April 21, 2017 and concluding on May 6, 2019.[12] Industry firms likely consent to these practices because they benefit if their employees prevail in the "straight-in" expungement arbitrations filed against them.

Ulmer & Berne is not the only law firm to represent a broker seeking an expungement in an action against a client the firm represents. An attorney at Bressler, Amery & Ross P.C. simultaneously represented both the claimant seeking an expungement and the respondent brokerage firm in *the same arbitration*.[13] The attorney represented both the claimant and the respondent in the same proceeding despite New Jersey's ethics rule which prohibits such representations whenever the concurrent representation involves "the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal."[14] Without any opposing voice in the room, the arbitrator recommended expungement. The broker continues to work for the respondent and his public BrokerCheck profile reveals no information about the past dispute.

This type of concurrent representation of brokers seeking expungement against the law firms' own clients appears routine and widespread. Lawyers at Bressler, Amery & Ross P.C. and other firms regularly bring actions seeking expungements against their firms' own clients—while simultaneously representing those clients on other matters.[15] Riker, Danzig, Scherer, Hyland & Perretti LLP has also brought expungement actions "against" the firm's own clients.[16] These representation patterns occur because the current expungement process generally lacks any adversarial character.

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whom the representation is directly adverse is likely to feel betrayed, and the resulting damage to the client-lawyer relationship is likely to impair the lawyer's ability to represent the client effectively.").

[10] In the Matter of the Arbitration Between: Claimant, Daniel J. Lauletta, FINRA Case No. 18-04142, 2019 WL 3857923 (Aug. 5, 2019).

[11] *Id.*

[12] In the Matter of the Arbitration Between: Claimant, Peter Frederick Butler, FINRA Case No. 17-01012, 2019 WL 2161328 (May 6, 2019).

[13] In the Matter of the Arbitration Between: Claimant, Brett Hina, FINRA Case No. 15-00221, 2015 WL 5561971 (Apr. 8, 2016).

[14] New Jersey, R.P.C. 1.7(b)(4).

[15] *E.g.* In the Matter of the Arbitration Between: Claimant, Gonzalo Castano, FINRA Case No. 19-03718, 2020 WL 5499973 (Sept. 3, 2020) *and* In the Matter of the Arbitration Between: Claimants, Ivanna Jazmin Freddi, Monica Mariana Kuclik, Rosario Freddi, & Juan M. Freddi, FINRA Case No. 18-03652, 2019 WL 7377012 (Dec. 18, 2019).

[16] *E.g.* In the Matter of the Arbitration Between: Claimant, Robert Calhoun Curtis, FINRA Case No. 18-04052, 2019 WL 2464989 (June 10, 2019) *and* In the Matter of the Arbitration Between: Claimant, Daniel Paul Motherway, FINRA Case No. 17-02799 *consolidated with* FINRA Case No. 17-02773, 2020 WL 278532 (Jan. 7, 2020).

B. The Commission Must Require Expanded Duties of Candor

To the extent that the Proposal continues to use adversarial procedures to inform arbitrators about whether they should recommend expungement, the Commission must require that the parties operate under expanded duties of candor and diligence when seeking these expungement recommendations. The ethics rules already impose an expanded duty of candor on advocates in *ex parte* proceedings. The ABA's Model Rules instruct that in an *ex parte* proceeding "a lawyer shall inform the tribunal of all material facts known to the lawyer that will enable the tribunal to make an informed decision, *whether or not the facts are adverse*."[17]

The comment to the Model Rule explains why disclosure is required in *ex parte* proceedings. In an ordinary situation, "an advocate has the limited responsibility of presenting one side of the matters that a tribunal should consider in reaching a decision."[18] In our adversarial system, "the conflicting position is expected to be presented by the opposing party."[19] Yet in *ex parte* situations, such as a request for "a temporary restraining order, there is no balance of presentation by opposing advocates."[20] Despite this, the comment instructs that the object of the proceeding "is nevertheless to yield a substantially just result."[21] To accomplish this goal, it requires a lawyer for the represented party "to make disclosures of material facts known to the lawyer and that the lawyer reasonably believes are necessary to an informed decision."[22]

In describing a lawyer's ethical obligations in *ex parte* proceedings, the Restatement goes further and also prohibits lawyers from presenting "evidence the lawyer reasonably believes is false" and instructs lawyers to also comply with "any other applicable special requirements of candor imposed by law."[23] The comment recognizes that the "potential for abuse is inherent in applying to a tribunal in absence of an adversary."[24]

Identifying the situations where a lawyer must operate under an expanded duty of candor remains challenging because the ABA's Model Rules do not define *ex parte* proceedings. Although technical definition would exclude all cases where some other party appears in the action, this would overly limit the rule's impact. One Idaho court read Idaho's rule as applying when one of the parties, after having received notice, failed to appear in a proceeding. It read the comment as suggesting "that the application of the rule is not meant to hinge on a technical definition of the term *ex parte*, but is instead intended to ensure that the tribunal is informed of facts necessary to render a just decision."[25] It found that the underlying rationale applied when

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[17] MODEL RULES OF PROF'L CONDUCT 3.3(d) (emphasis added).
[18] *Id.* at cmt. [14].
[19] *Id.*
[20] *Id.*
[21] *Id.*
[22] *Id.*
[23] RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 112 (2000).
[24] *Id.* at cmt. b.
[25] *See In re* Malmin v. Oths, 895 P.2d 1217, 1220 (Idaho 1995) ("The judge has an affirmative responsibility to accord the absent party just consideration.").

"'there is no balance of representation by opposing advocates'" applied when one of the parties was simply absent from a proceeding.[26]

Policy rationales also support extending the requirement beyond purely technical situations. The Restatement recognizes that in some special proceedings, "public policy requires unusual candor from an advocate."[27] It identifies child custody proceedings, involuntary commitment proceedings, and class action settlement proceedings. Expungement proceedings also implicate significant public concerns. The Central Registration Depository tracks customer complaints to assist regulators in doing their jobs, and to provide information to investors so that they can make decisions about the person to whom they will entrust their life savings. These are public goals that, if left to an "adversarial" system, require greater candor from counsel.

Massachusetts also treats class action settlement proceedings as *quasi ex parte* proceedings requiring lawyers to be fully candid with the court. The comment to its ethics rule explains that when:

> [A]dversaries present a joint petition to a tribunal, such as a joint petition to approve the settlement of a class action suit or the settlement of a suit involving a minor, the proceeding loses its adversarial character and in some respects takes on the form of an *ex parte* proceeding.[28]

As the Proposal fails to address the truly *ex parte* character of these proceedings, the Commission must require more. The Proposal should be altered to require any broker or broker's representative seeking an expungement to agree to operate under an expanded duty of candor. This would include duties to conduct a reasonable investigation and to disclose all known material facts, regardless of whether they are adverse.

The Commission might also accomplish some of this in its release by affirmatively stating that the Commission believes that these proceedings now go forward as de facto *ex parte* proceedings and that all parties and representatives must proceed under the ethical rules applicable to those situations. Although this minor change would not solve many of the problems with the system, it would create ethical obligations for attorneys to approach these expungement hearings differently. It would also put arbitrators on notice of the need to switch out of a traditionally passive role to conduct greater oversight.

IV. The Proposal Must Do More To Increase Customer Participation

The Proposal recognizes that the customers who made the underlying customer complaints have relevant information.[29] Customer complaints against brokers involve interactions between the broker and the customer. The persons most likely to know what happened in an interaction between a broker and a customer will invariably be the broker and the

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[26] *Id.*

[27] RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 112 cmt. c (2000).

[28] MASS. RULES OF PROF'L CONDUCT r. 3.3. cmt. 14A (2015).

[29] *See* Proposal, at 46 ("Customer participation during an expungement hearing provides the panel with important information and perspective that it might not otherwise receive").

customer. Between these two, the customer will likely have the most significant recollection of events because customers do not interact with brokers every day. In contrast, brokers interact with customers regularly, making them less likely to recall the specifics of any particular interaction.

Any competent fact-finder seeking to determine whether a customer falsified a complaint would desire to hear from the customer. Yet despite the need for customer participation, customers only rarely participate in the current expungement process. One recent study by the PIABA Foundation found that customers participate in less than one out of seven expungement hearings.[30] This means that in six out of seven expungement hearings, arbitrators will not hear from the person most likely to understand the basis for the customer's complaint—the customer.

Despite recognizing, again and again, that customers usually do not participate in expungement hearings and the relevance of a customer's participation, the Proposal does not create any incentive for a customer to participate. At the outset, it has long been clear that customers have little incentive to oppose a broker's request to expunge information from public records. Harmed customers have no need to ensure that public information about the broker is accurate once they have settled or otherwise resolved their dispute. These customers already know to avoid the broker who swindled them. Wronged customers may also decline to participate for a variety of reasons. In many instances, they may be ashamed that they were ripped off, or simply embarrassed. Others are overwhelmed by the process, especially elderly customers.

The Commission has previously been provided with information about the disincentives to customer participation in expungement hearings. In 2008, the North American Securities Administrators Association explained that customers opposing expungement "would incur additional costs, in the way of attorney's fees and time, in order to participate and would gain no benefit through their participation."[31]

If the current adversarial fact-finding process will continue to be used, the Commission should require the creation of incentives for customers to participate in these unpleasant expungement proceedings. The Commission could do this by requiring FINRA to undertake rulemaking to provide for attorney fees and incentive awards for customers who participate in expungement proceedings. The Commission should also affirmatively state in any release on this Proposal that the Commission believes that arbitrators conducting these hearings may, in exercising their equitable power, award attorney fees to customers who participate in expungement hearings. As it stands, the Proposal does not do anything to address this fundamental problem.

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[30] JASON R. DOSS & LISA BRAGANÇA, 2019 STUDY ON FINRA EXPUNGEMENTS: A SERIOUSLY FLAWED PROCESS THAT SHOULD BE STOPPED IMMEDIATELY TO PROTECT THE INTEGRITY OF THE PUBLIC RECORD 15 (2019), https://perma.cc/9FSY-GJ6F (PDF) ("Of the 1,078 cases, customers whose complaints are the subject of expungement requests participated and objected to brokers' expungement requests only 141 times – approximately 13% of the time.").

[31] Letter from Karen Tyler, N. Am. Secs. Admins. Ass'n President and N.D. Sec. Comm'r, to Nancy M. Morris, Sec'y, Sec. Exch. Comm'n (Apr. 24, 2008), https://www.sec.gov/comments/sr-finra-2008-010/finra2008010-7.pdf.

A well-functioning expungement process must aim to surface relevant information and customers have essential information. Despite this, the Proposal does not devote significant attention to increasing customer participation. The Commission should require FINRA to reach out to customers who have not participated and attempt to gather information about why they did not participate in expungement hearings. This sort of inquiry would likely yield information enabling FINRA and the Commission to better understand why the current expungement system fails to adequately safeguard the public interest.

V. The Proposal Does Not Provide for Adequate Notice to Customers

The Proposal does not adequately address significant, known problems with how customers receive notice about expungement proceedings.[32] At present, customers often receive inconsistent and confusing notice. The Proposal should be modified to rectify problems with form, content, and timing of the notice.

A. Customer Notices Should Actively Encourage Customer Participation

The Proposal improperly leaves the form of the initial notice in "straight-in" expungement requests up to the person requesting the notice. The Proposal states that the "panel should review all documents that the associated person used to inform the customers about the expungement request as well as any customer responses received."[33] It also indicates that this requirement is aimed at ensuring "that the associated person does not attempt to dissuade a customer from participating in the expungement hearing."[34]

This procedure improperly leaves the power of the pen in the hand of the person seeking an expungement. Given the lack of customer participation, a notice which simply does not actively dissuade a customer from participating will not suffice to increase customer participation or the likelihood that arbitrators will make anything approaching an informed decision when recommending expungement.

Given the problems with the expungement process and the general lack of any opposition to these requests, there is no good reason to believe that arbitrators will be able to effectively supervise initial notice. At the outset, arbitrators will receive these notices only after they have been transmitted. No party with any real incentive to point out a problem with an inadequate, subtly dissuading, or tediously discouraging notice will appear before the arbitrator. Whenever there is any doubt about the adequacy of notice, arbitrators will likely fail to order another form of notice and delay the proceedings. The Proposal does not indicate that arbitrators will have any training on the forms of notice likely to increase customer participation. The Proposal provides no good reason to believe that these notices will increase customer participation.

The Commission should direct substantial attention to the form of the initial notice to customers. It should require FINRA to draft notices which encourage participation and to test which notices actually drive increased participation.

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[32] *Adversarial Failure*, at 138-141.
[33] Proposal, at 50.
[34] *Id.* at 51.

B. Initial Notices Should Address Common Customer Concerns About Participation

The initial notice contemplated by the Proposal appears inadequate because it does not affirmatively address major barriers to participation. Many customers now fear to participate because they have signed settlement agreements with confidentiality and non-disparagement clauses. At the very least, FINRA should require an associated person seeking an expungement to affirmatively state in the initial notice that nothing the customer says in connection with the expungement will be deemed to violate any settlement agreement with the customer or subject the customer to any liability. It should also affirmatively state that the customer may use documents produced in any other action within the expungement hearing, regardless of whether they were subject to any confidentiality order. To the extent such documents have been destroyed pursuant to the conclusion of the underlying case, FINRA should require the member firm or other party which initially produced the documents to produce them again so that the panel may have access to information relevant to deciding any expungement request. To give customers confidence that they will not face retaliation, associated persons seeking expungements should provide customers with a release absolving them of any potential liability related to their participation in an expungement proceeding in the initial notice transmitted to the customer. A binding promise to hold the customer harmless for their participation in an expungement hearing should be required for an associated person to seek an expungement and delivered to the customer with the initial notice.

At present, FINRA Rule 2081 does not go far enough to address these concerns. Although the current rule prohibits conditioning settlement on an express agreement not to oppose expungement, it does not ensure that customers will be able to provide arbitration panels with the information they may know or the documents they may have seen in an arbitration proceeding. It also does not affirmatively remove the fears customers have about participating in these processes.

Participating customers need an express release from liability and protection from retaliation because associated persons have, on multiple occasions, refused to agree to hold customers harmless for their participation in expungement proceedings. On at least one occasion, counsel for a customer seeking to participate in an expungement proceeding had to threaten to seek a declaratory judgment in court that the customer could participate before counsel for the associated person would agree that the customer could participate without fear of retaliation.

C. Customer Notices Should Include All Documents Filed in The Proceeding

The notice contemplated by the Proposal will not provide the customer with sufficient information. Notably, the Proposal simply requires a broker seeking expungement to provide the customer only with a copy of the statement of claim. It does not require the broker to provide the customer with copies of all documents filed in the proceeding, leaving customers at a significant disadvantage and without access to all of the statements which have been made about them in the proceeding. In many straight-in expungement proceedings, the interests of the broker requesting expungement and the respondent are aligned. As the respondent will likely benefit if the arbitrator recommends expungement, a copy of any answer filed by the respondent as well as all other documents should also be provided to a customer.

D. Notice Should Not Be Delayed By Delaying Initial Hearings

The Proposal allows persons seeking expungement to delay notice by not requesting or waiving initial hearings. As drafted, the Proposal only requires notice before the first hearing is held.[35] This odd structure should be modified to require notice to be sent on the same day that the broker files the request. Although the first hearing would ordinarily be a scheduling hearing, parties may, and likely will, delay notice to a customer by submitting a stipulated schedule. This effectively cuts the customer out of participating in any scheduling hearing deciding when the fact-finding hearing will be held because the parties will simply agree to schedule the hearing at a time which is convenient for them without any regard to the customer's schedule. The Proposal should allow customers to participate in all initial scheduling decisions and to communicate with the panel on these scheduling matters.

E. The Proposal Should Define a Notice Period for Customers

The current proposal does not specify how much time customers will have after receiving notice about a straight-in expungement request before they will need to be prepared to respond. A 90 day period should be required to give customers the ability to secure counsel and prepare a response.

VI. FINRA Should Segregate Expungement Arbitrators from Customer Arbitration Pools

The Proposal does improve the process by removing the ability of parties to influence arbitrator selection for expungements. This may remove some incentive for arbitrators to grant expungements in order to continue to be selected for expungement matters.

Yet the Proposal must go further. The current expungement process may taint the arbitration pool and bias arbitrators against customers. In these expungement proceedings, parties tell arbitrators that investors are liars who have made false claims against them. Many arbitrators hear this narrative again and again from broker after broker as they recommend expungement after expungement.

This process likely causes bias against customers. The Proposal does not provide any information about whether arbitrators who recommend expungements are more likely to rule against customers than arbitrators who have not been marinated in "straight-in" expungement hearings. FINRA could determine whether expungement hearings bias its arbitrators by studying the data in its possession. Academics may soon reach this issue as well. In the absence of solid information about how these processes may bias customer arbitrations, the Commission should take steps to limit how expungement processes may influence arbitrators.

The Commission should require FINRA to create a separate pool for expungement proceedings. A small, highly-trained pool would reduce the risk that bias against customers would bleed over to customer cases. It would also enable the arbitrators presiding over these odd

[35] *Id.* at 50.

hearings to more quickly accumulate expertise. It would also allow FINRA to devote targeted resources to training these arbitrator to approach expungement matters in a different way than the ordinary, largely passive arbitrator posture.

VII. The Proposal Must Include Some Standard of Proof Beyond Mere Preponderance

The Commission should require the Proposal to set forth some standard of proof for these expungement proceedings.[36] As it stands, arbitrators do not have sufficient guidance about whether to apply a preponderance of the evidence standard, a clear and convincing standard, or a beyond reasonable doubt standard when deciding whether to recommend expungement. Arbitrators have wrestled with this issue for some time in the absence of guidance. This system generates enormous confusion and inconsistent application of the standards set forth in Rule 2080—something which the Proposal claims to desire to avoid.[37]

In the absence of any standard of proof, outcomes in expungement proceedings may be largely arbitrary or granted at abnormally high rates on the mistaken belief that the arbitrator should simply apply a preponderance of the evidence standard. Consider a recent arbitration award recommending the expungement of twelve different items from the CRD for two brokers. The two brokers brought an arbitration against Geneos Wealth Management, Inc., which "did not appear at the expungement hearing and did not contest the expungement requests."[38] The arbitrator found that "the Customers were served with the Statement of Claim and received notice of the expungement hearing" at some unspecified date before the hearing.[39] At a hearing where only the brokers appeared, the arbitrator found that "preponderance of the evidence adduced at the expungement hearing" supported a series of factual findings.[40] Altogether, the brokers successfully erased "five FINRA arbitration cases, [one] civil court case and two customer complaints" from the CRD. The arbitrator reached this conclusion after just a single hearing session on the expungement requests which lasted four hours or less.[41]

Misplaced application of a preponderance standard to these unopposed proceedings nearly guarantees that arbitrators will recommend expungement. After all, in "straight-in" expungement proceedings, the respondent will normally outright support the claimant, or failing that, not oppose any of the claimant's requests. When the only evidence presented supports an expungement, arbitrators will simply rule on the limited and one-sided evidence before them to recommend expungement. Only in rare circumstances will a customer participate or a party actually oppose an expungement request.

Given the near total absence of adversarial opposition and the need to protect public information, the Commission should require that FINRA modify its rules to require persons

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[36] *See Adversarial Failure*, 141-143 (discussing standard of proof problems).
[37] Proposal, at 111-112 (explaining FINRA's decision to not codify the "no investor protection or regulatory value" standard because codification of the standard might "create confusion among arbitrators and the potential for inconsistent application among different arbitrators and panels").
[38] Arford v. Geneos Wealth Mgmt., Inc., No. 19-00739, 2019 WL 5681728, at *1 (Oct. 24, 2019) (Cutler, Arb.).
[39] *Id.*
[40] *Id.*
[41] *Id.*

seeking expungement prove their case by at least clear and convincing evidence. Absent some official standard, arbitrators will continue to flounder on these issues, reaching inconsistent decisions and recommending expungement whenever scant but uncontested evidence supports it.

VIII. Expungement Recommendations Should Be Unanimous

The Proposal takes the wrong approach by rejecting FINRA's initial release proposing that a three-arbitrator panel render a unanimous decision in order to recommend expungement. Instead, FINRA "determined to allow arbitrators to recommend expungement through a majority decision, consistent with what is required for other decisions in customer and industry arbitrations."[42]

Allowing a simple majority to reach decisions insufficiently protects the public's vital interest in information. It also fails to communicate that expungement should only be recommended in truly extraordinary cases.

I thank you again for the opportunity to comment on the Proposal. Current expungement processes drain valuable public information from public databases and drive enormous harm to the public. States now struggle to identify bad actors because they rely on databases which have had significant information deleted from them. Investors mistakenly rely on BrokerCheck on the misplaced belief that it will tell them if a broker has had problems in the past. The Commission must require more to effectively protect the public's interest.

Sincerely,

Benjamin P. Edwards
Associate Professor of Law
University of Nevada, Las Vegas
William S. Boyd School of Law

[42] Proposal, at 109-110.

Exhibit A

Adversarial Failure

Benjamin P. Edwards*

Abstract

Investors, industry firms, and regulators all rely on vital public records to assess risk and evaluate securities industry personnel. Despite the information's importance, an arbitration-facilitated expungement process now regularly deletes these public records. Often, these arbitrations recommend that public information be deleted without any true adversary ever providing any critical scrutiny to the requests. In essence, poorly informed arbitrators facilitate removing public information out of public databases. Interventions aimed at surfacing information may yield better informed decisions. Although similar problems have emerged in other contexts when adversarial systems break down, the expungement process to purge information about financial professionals provides a unique case study.

Multiple interventions may combine to more effectively surface information and generate better informed decisions. In quasi-ex parte proceedings, traditional attorney ethics rules must yield to a higher duty of candor. Yet adjudicators should not rely on duty alone. Adversarial scrutiny may emerge by designating an advocate to independently and critically engage in circumstances where no party has any real incentive to oppose an outcome. Ultimately, addressing adversarial failures may

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require a shift away from adversarial adjudication to a more regulatory framework.

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I. Introduction

Customer complaints about stockbrokers (brokers), misconduct findings, and other information have long been public record. The public disclosures for Gregory Brian VanWinkle, a broker affiliated with Essex Securities, reveal a history of problems detailed in seven different disclosures.[1] In 2013, Securities America discharged him for violating the firm's policy related to client signatures.[2] Arising from this incident, the Financial Industry Regulatory Authority (FINRA) also brought a disciplinary action against him which culminated in a fine of $5,000 and a twenty-day suspension.[3] The public record includes three customer disputes, two of which resulted in

1. *See Gregory Brian VanWinkle,* BROKERCHECK, https://perma.cc/KXP7-U53R (providing the employment history and public disclosure record of VanWinkle).

2. *See id.* (detailing that VanWinkle was discharged due to an allegation that he "violated firm policy relating to client signatures").

3. *See* Letter of Acceptance, Waiver, and Consent No. 2013038209301 from Gregory Van Winkle to Fin. Indus. Reg. Auth. 2 (June 29, 2015), https://perma.cc/XA38-UTDV (detailing that VanWinkle agreed to "[a twenty] business-day suspension from association with any FINRA firm in any capacity and a $5,000 fine").

settlements.[4] But these public disclosures only tell part of the story.

VanWinkle erased another twenty-four customer disputes and some now unknowable number of settlements from the public record with one weird trick. In 2017, he filed an arbitration claim against a former employer, IFS Securities.[5] IFS never responded to the action and did not file any answer.[6] Importantly, VanWinkle did not seek any damages from IFS Securities.[7] He filed the action to secure an arbitration award declaring that the twenty-four customer complaints should not be on his record because they were either false or that he had nothing to do with the alleged misconduct.[8] He succeeded and obtained the arbitration award after a single fact-finding hearing lasting four hours or less.[9]

A traditional, adversarial fact-finding process may have yielded a substantially different result. With no opposing voice in the room, VanWinkle successfully shifted the blame to a third party who played no role in the arbitration—an insurance company who accurately described its offering in its

4. *See Gregory Brian VanWinkle*, supra note 1 (reporting that one customer dispute was denied and two other customer disputes were settled).

5. *See* VanWinkle v. IFS Sec., Inc., No. 17-02465, 2018 WL 4051277, at *1 (Aug. 13, 2018) (Ver Beek, Arb.) (memorializing VanWinkle's arbitration claim).

6. *See infra* Part II.C.1.d and accompanying text (explaining why brokerages do not oppose these requests). *See also VanWinkle*, 2018 WL 4051277, at *1 (noting that IFS "did not file with FINRA Office of Dispute Resolution a properly executed [s]ubmission [a]greement" and that IFS "did not participate in the expungement hearing").

7. *See VanWinkle*, 2018 WL 4051277, at *1 (stating that VanWinkle's requested relief was only for "expungement of the [u]nderlying [c]laims from his registration records maintained by the [Central Registration Depository]").

8. *See* FIN. INDUS. REG. AUTH., RULE 2080 (2009) (setting out the requirements for expungement awards). *See also VanWinkle*, 2018 WL 4051277, at *2 (supporting VanWinkle's expungement claim on the basis that the underlying issues in the customer's complaints were not VanWinkle's fault but rather the fault of the issuer of the security).

9. *See VanWinkle*, 2018 WL 4051277, at *2 (reporting that the arbitrator found in favor of VanWinkle's expungement argument). Within the FINRA forum, a hearing session lasts for four hours or less. *See Summary of Arbitration Fees*, FIN. INDUS. REG. AUTH., https://perma.cc/9L8N-APY6 ("A hearing session is any meeting between the parties and arbitrator(s) of four hours or less, including a hearing or a prehearing conference.").

prospectus.[10] In granting VanWinkle's request, the arbitrator found that VanWinkle "sold a particular annuity product to many customers" and that he "was familiar with this product from sales meetings and prior sales to several customers."[11] Implicitly acknowledging that VanWinkle did not understand the product he sold, the arbitrator found that "[a]pparently the issuer changed the [d]eath [b]enefit with nothing calling attention to the change except language in a very long prospectus."[12] Ultimately, the arbitrator found that the customer claims were false and that VanWinkle had not been involved with the misconduct because the "fault lies with the issuer, not [VanWinkle], and none of the allegations raised involved actions by [VanWinkle]."[13] The award seemingly acknowledges that VanWinkle either did not understand the product he sold or that he sold it to customers while misrepresenting its true nature. At best, the reasoning might support a finding that VanWinkle repeated the same innocent mistake at least twenty-four times. It does not establish that the customer complaints about him were false.

The arbitrator's ruling appears particularly puzzling because customers work with brokers to help them find financial products that are suitable for their situation.[14] This requires that brokers like VanWinkle understand the products that they sell to customers and not simply push whatever product pays the highest commission.[15] The rules governing

10. *See VanWinkle*, 2018 WL 4051277, at *1 (noting that the parties involved in the arbitration included VanWinkle and IFS Securities, a broker-dealer, but did not include the insurance company who issued the underlying annuity that was at issue in the case).

11. *Id.* at *2.

12. *Id.*

13. *Id.*

14. *See* FIN. INDUS. REG. AUTH., RULE 2111 (2014) (obligating a broker to "have a reasonable basis to believe that a recommended transaction or investment strategy involving a security or securities is suitable for the customer").

15. *Cf.* Ann Lipton, *I Do Not Think It Means What You Think It Means*, BUS. L. PROF BLOG (May 7, 2016), https://perma.cc/N9NV-7USX (describing variable annuities as "a product that might be suitable if you're trying to shelter your assets from a lawsuit, but otherwise one whose chief virtue lies in its capacity to serve as a litmus test for the honesty of your broker").

brokers make clear that a broker must have "an understanding of the potential risks and rewards associated with the recommended security or strategy" and that a broker who lacks "such an understanding when recommending a security or strategy violates the suitability rule."[16] The arbitrator's factual finding about VanWinkle shows that he lacked that understanding.

Many different stakeholders have an interest in these disputes and could have pointed out obvious problems with a broker selling dozens of customers the same variable annuity without understanding its terms. State regulators rely on public records to target their oversight and enforcement efforts. FINRA, which oversees brokers, would likely want to know this information when its staff examines a brokerage. Future investors would likely want to know about these complaints when deciding whether to hire him as a broker. And, presumably, the annuity's issuer might want to point out that the broker and brokerage firm must understand the product it sells. But none of these stakeholders participated in the arbitration hearing.[17]

The required final step of judicial confirmation of arbitration awards provides no real check on the process.[18] Even when regulators have attempted to intervene at this stage, they have not generally succeeded at stopping confirmation. Courts routinely confirm these arbitration awards without any inquiry into whether the arbitrator made a reasonable decision.[19] A confirmed award allowed VanWinkle to have all this information deleted from public records.

16. FIN. INDUS. REG. AUTH., RULE 2111 Supplementary Material .05(a) (2014) .

17. *See* VanWinkle v. IFS Sec., Inc., No. 17-02465, 2018 WL 4051277, at *1 (Aug. 13, 2018) (Ver Beek, Arb.) (listing participating parties).

18. *See id.* at *2 (noting that before arbitration awards may be enforced, they must be confirmed by courts of competent jurisdiction).

19. *See* Stephen J. Ware, *Default Rules from Mandatory Rules: Privatizing Law Through Arbitration*, 83 MINN. L. REV. 703, 711 (1999) ("Courts do not closely review arbitration awards to ensure that arbitrators apply the law. And even if a court discovers that an arbitration award does not apply the law, the court will likely confirm the award."(citation omitted)).

For decades, brokers and financial services industry firms have used private arbitration decisions to strip information from the public record.[20] In theory, this expungement process provides an extraordinary remedy to protect financial professionals from having malicious, false, or entirely baseless complaints taint their records and harm their careers.[21] In reality, significant evidence indicates that the expungement process actually suppresses important public information and tends to increase financial misconduct.[22] This may happen either by allowing bad actors to remain or by emboldening others to take advantage of clients.[23]

Brokers win expungements quite frequently. By one calculation, brokers have requested to expunge around 12% of the allegations of misconduct made by customers and firms in recent years.[24] Brokers making these requests generally succeed at suppressing information and win over 80% of their requests.[25] Notably, brokers who successfully expunge complaints from their record "are 3.3 times as likely to engage in new misconduct as the average broker."[26]

The finding that brokers who have secured expungements pose significantly more risk than the average broker raises real

20. *See* Jill E. Fisch, *Top Cop or Regulatory Flop? The SEC at 75*, 95 VA. L. REV. 785, 800 (2009) (noting that existing arbitration rules "facilitate the concealment of allegations of misconduct").

21. *See* Colleen Honigsberg, *The Case for Individual Audit Partner Accountability*, 72 VAND. L. REV. 1871, 1914 (2019) (explaining that FINRA's "BrokerCheck . . . database includes unverified customer complaints, prompting concerns that certain brokers are unfairly targeted").

22. *See* Colleen Honigsberg & Matthew Jacob*, Deleting Misconduct: The Expungement of BrokerCheck Records*, J. FIN. ECON. (forthcoming 2020) (manuscript at 1) (on file with the Washington and Lee Law Review) [hereinafter Honigsberg & Jacob] (reporting that brokers with past history of successful expungements are more likely that brokers without past expungements to engage in future misconduct).

23. *See id.* at 5 ("Our analysis provides evidence that successful expungements increase recidivism.").

24. *See id.* at 3 (explaining that evidence "suggests that brokers request to expunge 12% of the allegations of misconduct made by customers and firms") (citation omitted) .

25. *See id.* at 15 ("[O]ver 80% of expungements decided on the merits are successful in each year from 2007 to 2016 . . . .").

26. *Id.* at 4.

concerns about the legitimacy of the expungement process itself. Private arbitration proceedings may be particularly poorly suited to resolve questions of great public importance.[27] If the expungement process reliably functioned to remove only false information, a broker who obtains an expungement award would not pose any special danger.[28] Instead, the statistics emerging from the current expungement process reveal that the system likely purges truthful information, or at least information with significant predictive power.

Many stakeholders have strong interests in knowing about a broker's disclosures. The broker's current and future investor clients have an interest in knowing about past customer disputes, as well as bankruptcies and convictions.[29] Similarly, regulators have an interest in the information to effectively police their markets. Future employers also have an interest because a record of past disputes may help a firm decide whether a new hire will generate new liabilities. Yet the current expungement process only requires the participation of a broker and a brokerage firm.[30] Regulators are able to participate at the confirmation stage, but rarely do. Customers whose disputes may have settled years ago may receive notice but have little incentive to participate.[31]

The current broker expungement process exemplifies "adversarial failure." In using the phrase, I mean more than that the system simply does not work well. As Malcom Feeley

27. *Cf.* Jean R. Sternlight, *Mandatory Binding Arbitration Clauses Prevent Consumers from Presenting Procedurally Difficult Claims*, 42 SW. L. REV. 87, 127 (2012) ("[O]ur system often relies heavily and explicitly upon enforcement by private parties to achieve public regulatory objectives.").

28. Theoretically, it might be possible that the brokers most likely to harm the public were also the most likely to draw false allegations. This seems highly unlikely.

29. *See* Benjamin P. Edwards, *The Professional Prospectus: A Call for Effective Professional Disclosure*, 74 WASH. & LEE L. REV. 1457, 1485 (2017) ("For market forces to function effectively, reputation must play a significant role. Yet reputation only plays a weak role in the current markets for professional services because public consumers both struggle to recognize and broadcast information about low quality professionals.").

30. *See infra* Part II.

31. For a description of the limited notice customers receive in many instances, *see infra* Part II.C.3 and accompanying text.

has noted, adversarial systems can fail in ways analogous to market failures.[32] Although writing in the criminal law context, he explains that although we "have theories and well-recognized institutions to prevent or correct for market failure—public finance theory, public utilities, regulatory agencies, and the like—we have no equivalent safeguards for adversarial failure."[33]

Adversarial failure may occur when parties to a dispute have either aligned interests or no real incentive to contest. Accustomed to adjudicating genuinely contested disputes, arbitrators and courts mistakenly expect that the lawyers and parties appearing before them will raise all relevant facts as well as applicable law and rules. They may also expect that, collectively, participating parties have some incentive to bring reasonably pertinent information to the adjudicator's attention. Yet in many securities, shareholder, and mass tort disputes, the named parties have little incentive to generate a complete record.[34] Sometimes, no party to an action has any real interest in focusing a court's attention on a significant issue.[35] Seeing only what parties with aligned interests place before them, adversarial systems chug along—blind to the real picture.

32. *See* Malcolm M. Feeley, *How to Think About Criminal Court Reform*, 98 B.U. L. REV. 673, 704 (2018) ("Just as there is market failure at times, so too there can be adversarial system failure.").

33. *See id.* (describing the criminal law system as using "some crude stop-gap measures, such as chronically underfunded public defender systems" to address the problem).

34. *See* ELIZABETH CHAMBLEE BURCH, MASS TORT DEALS: BACKROOM BARGAINING IN MULTIDISTRICT LITIGATION 107-09 (2019) (discussing how settlement deals may emerge without significant information ever reaching a court). *See also* Elizabeth Chamblee Burch, *Publicly Funded Objectors*, 19 THEORETICAL INQUIRIES L. 47, 48–49 (2018) (citation omitted) ("On paper, things run like clockwork. But practice suggests the need for tune-ups: some judges still approve settlements rife with red flags, and professional objectors may be more concerned with shaking down class counsel than with improving class members' outcomes.").

35. *See* Cathy Hwang & Benjamin P. Edwards, *The Value of Uncertainty*, 110 NW. U. L. REV. 283, 284–85 (2015) (explaining that "despite the fact that some security holders may benefit from raising [a] jurisdictional issue and possibly having the case dismissed, courts and parties have generally not raised it" (citation omitted)).

This article connects with scholarly discussion in the shareholder derivative and securities class action settlement context. For the most part, scholars have highlighted problems in the context of class action settlement approvals.[36] Principal-agent problems often occur when lawyers representing named parties generally have interests which align in favor of settlement approval, often to the detriment of other key stakeholders and class members.[37] Normal adversarial processes break down at this point because all of the parties actually involved desire the same result—approval of the settlement agreement.[38] After agreeing to pay a set price to resolve all liability, defendants have no reason to pay lawyers to point out any defects in the settlement agreement or plan of distribution to the court. With significant fees on the table, plaintiffs' lawyers have little incentive to encourage a court to reduce their fees or carefully scrutinize how the agreement will affect all unrepresented and absent class members. In many instances, significant conflicts and flaws with a settlement deal

36. *See*, *e.g.*, Susan P. Koniak, *Feasting While the Widow Weeps:* Georgine v. Amchem Products, Inc., 80 CORNELL L. REV. 1045, 1126 (1995) (explaining that in settlement approval hearings, "settling parties are aligned, and there may be no objector represented at the fairness hearing. These proceedings are thus analogous to ex parte proceedings, where a lawyer's duty of candor to the court is much greater than in an ordinary adversarial proceeding."); Susan P. Koniak & George M. Cohen, *Under Cloak of Settlement*, 82 VA. L. REV. 1051, 1057–68 (1996) (describing class counsel taking advantage of absent class members in class action settlements).

37. *See* Jonathan R. Macey & Geoffrey P. Miller, *The Plaintiffs' Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. CHI. L. REV. 1, 46 (1991) [hereinafter Macey & Miller] ("[S]ettlement hearings are typically pep rallies jointly orchestrated by plaintiffs' counsel and defense counsel. Because both parties desire that the settlement be approved, they have every incentive to present it as entirely fair.").

38. *See In re* Trulia, Inc. Stockholder Litig., 129 A.3d 884, 893 (Del. Ch. 2016) ("Once an agreement-in-principle is struck to settle for supplemental disclosures, the litigation takes on an entirely different, non-adversarial character. Both sides of the caption then share the same interest in obtaining the Court's approval of the settlement."). *See also supra* note 37 and accompanying text.

may never be brought to a court's attention.[39] Yet little work connects these threads to similar problems within the financial regulatory system.

This Article explores how an adversarial system breaks down and fails to produce informed decisions in a way that hurts the public. It focuses on the process stockbrokers use to delete public information. It begins in Part II by developing a detailed case study about how brokers now leverage a private arbitration process to enlist courts in suppressing public access to information. Courts reviewing these arbitration awards actually exercise little oversight. The Federal Arbitration Act limits judicial review of arbitration awards, and only permits a court to vacate an arbitration award in rare circumstances.[40] In essence, poorly informed arbitration decisions now drain important information from society without any real judicial or adversarial check.[41] As with the problems in securities class actions, skewed incentives, underrepresentation, and conflicts amplify these recurring problems within the process for expunging customer dispute information about stockbrokers.

Channeling disputes through arbitration proceedings only serves to amplify these problems—leaving courts as an ineffective check on arbitration outcomes.[42] In contrast, ordinary judicial dispute resolution systems create some restraint on adversarial failures. Public courts owe duties to the public to correctly state the law and consider how the precedent

39. *See* Benjamin P. Edwards & Anthony Rickey, *Uncovering the Hidden Conflicts in Securities Class Action Litigation: Lessons from the State Street Case*, 75 BUS. LAW 1551, 1552–53 (2020) ("[A]dversarial review of settlements is rare, and no settling party has a reason to bring uncomfortable facts to the attention of a reviewing court.") (citation omitted).

40. *See* 9 U.S.C. § 10 (2018) (setting out circumstances in which a court may vacate an arbitration award).

41. *See* Jean R. Sternlight, *Hurrah for the Consumer Financial Protection Bureau: Consumer Arbitration as a Poster Child for Regulation*, 48 ST. MARY'S L.J. 343, 345 (2016) (explaining that "regulation is desirable . . . when market forces are not sufficient to protect individual or public interests").

42. *Cf.* Jean R. Sternlight, *Mandatory Arbitration Stymies Progress Towards Justice in Employment Law: Where to, #Metoo?*, 54 HARV. C.R.-C.L. L. REV. 155, 159 (2019) ("If companies can continue to use mandatory arbitration to eradicate access to court, where judges are potentially influenced by social movements, social movements will no longer be able to assist the overall progressive trend of our jurisprudence.").

created will shape future cases.[43] In contrast, private arbitrators often look no further than the materials submitted to them by the parties.[44]

To its credit, FINRA has periodically responded to problems and imposed additional requirements.[45] In 2017 it considered additional incremental reforms, including establishing a dedicated arbitrator pool for expungements, requiring unanimous approval from three arbitrators, imposing a one-year time period for seeking expungements, and other changes.[46] In 2019, FINRA's Board of Governors "approved . . . amendments to the Codes of Arbitration Procedure to create, among other things, a roster of arbitrators . . . to decide" expungement requests.[47] Although these proposals have not yet been released, they will not solve the core problems which flow from bad incentives and conducting fact-finding through an arbitration process. At best, they may mitigate the ongoing harm to a degree.

These failures reveal the need for a range of interventions to produce better informed decisions. Part III considers some possibilities. It proposes shifting resolution of these issues to a non-adversarial and more regulatory process. Adjudicators might also mitigate adversarial failures by adopting a more skeptical approach or recruiting assistance when parties lack incentives to develop and present important information. If an

43. *See* Benjamin P. Edwards, *Arbitration's Dark Shadow*, 18 NEV. L.J. 427, 432 (2018) ("Arbitrators and judges adjudicate disputes in different ways. Precedent-creating judges owe a duty to the public to correctly state the law because court judgments are public acts by public officials. This means that judges will not simply regurgitate incorrect statements of law provided by the parties." (citation omitted)).

44. FINRA's training materials for arbitrators instruct that "[a]rbitrators should not make independent factual investigations of a case." FIN. INDUS. REG. AUTH., FINRA DISPUTE RESOLUTION SERVS. ARBITRATOR'S GUIDE 60 (May 2020), https://perma.cc/5W3F-NKXU (PDF).

45. For a discussion of past problems with the process, *see infra* Part II.D and accompanying text.

46. *See* Fin. Indus. Reg. Auth., Regulatory Notice 17-42, Expungement of Customer Dispute Information 5 (Dec. 6, 2017), https://perma.cc/K8U4-Q2WU (PDF) (detailing updates to FINRA expungement rules and related arbitration proceedings).

47. Robert W. Cook, *Update: FINRA Board of Governors Meeting*, FIN. INDUS. REG. AUTH. (Oct. 3, 2019), https://perma.cc/3H3M-UUE8.

adversarial system must be used, it also explores necessary changes to the dominant ethical framework for lawyers presenting information to decision makers. The American Bar Association's Model Rules of Professional Conduct provides the framework and operative text for most state professional ethics rules.[48] Although Model Rule 3.3 generally calls for lawyers to be candid with tribunals, the rules grant lawyers substantial leeway to shape the factual scenarios adjudicators actually see.[49] Changes to attorney ethics rules might cause lawyers to present more balanced pictures.

II. Expungement and Adversarial Failure

For decades, brokers have been able to leverage arbitration proceedings to remove customer complaints from readily accessible public records.[50] Brokers have long supported the process because it gives them a path to challenge unverified customer complaints. Yet the process does not sufficiently protect the public's interest in information. One arbitrator generally criticized the way most expungements occur, pointing out that many arbitration awards recommending expungement "are not much more than conclusory reiterations of the findings and not careful discussions and analyses of the evidence."[51] Ultimately, the arbitrator recognized that many "decisions suggest that the panel did little more than have a mini ex parte trial on the merits," resulting in expungements.[52] State regulators have also panned this expungement process as "a failed system."[53] This case study details the broad context and history surrounding the expungement process before examining

48. *See generally*, MODEL RULES OF PROF'L CONDUCT (AM. BAR ASS'N 2020).

49. *See* MODEL RULES OF PROF'L CONDUCT r. 3.3 (AM. BAR ASS'N 2020) (allowing lawyers to present information they suspect may be false or incomplete).

50. For an explanation of FINRA's role, *see infra* Part II.D and accompanying text.

51. Gilliam v. Sagepoint Fin., Inc., No. 12-03717, 2013 WL 3963949, at *3 (July 22, 2013) (Meyer, Arb.).

52. *Id.*

53. Letter from Christopher Gerold, N. Am. Sec. Admins. Ass'n President, to Vanessa Countryman, Sec'y, U.S. Sec. & Exch. Comm'n 3 (Mar. 18, 2020) (on file with the Washington and Lee Law Review).

the many reasons why this adversarial expungement process fails to generate informed or reliable decisions. At root, much of the harm flows from the reality that this arbitration-facilitated expungement system most substantively resembles an ex parte proceeding cloaked in the form of an ordinary, adversarial arbitration. In the end, the system now functions so poorly that brokers receiving expungements pose over three times as much danger to the public on a statistical basis than the average broker.[54]

Importantly, arbitration-facilitated expungements only partially erase and blur history. Those in the know may find expungement awards buried in FINRA's database of publicly available arbitration awards.[55] Although it is not possible to reconstruct all expunged information, informed observers can identify brokers who have had customer dispute information deleted. Some informed observers may still take the fact of prior expungements into account. Yet most ordinary regulatory, arbitral, and judicial processes will not. After all, a court does confirm an award before the customer dispute information is actually deleted.[56]

A. The Broad Context

When Americans need help allocating funds and saving for retirement, they often turn to financial advisors for assistance.[57] These advisors operate within a variety of regulatory structures and may owe different duties depending on the particular

54. *See* Honigsberg & Jacob, *supra* note 22, at 4 (finding that brokers with expungements pose significantly greater risks than the average broker).

55. *See* Nicole G. Iannarone, *Finding Light in Arbitration's Dark Shadow,* 4 NEV. L.J. F. 1, 7 (2020) ("In the process of removing all information concerning the customer's dispute from her CRD, the broker asserts a claim for expungement in the FINRA arbitration forum, the result of which is then recorded as an award and publicly available . . . ." (citation omitted)).

56. *See supra* note 10 and accompanying text.

57. *See* Benjamin P. Edwards, *Conflicts & Capital Allocation*, 78 OHIO ST. L.J. 181, 213 (2017) (explaining that different "types of financial advisors now play a major role in dispensing personalized investment advice and influencing retail capital allocation").

capacity in which they operate at any time.[58] And many brokers operate in a dual capacity, sometimes acting as a fiduciary investment adviser and a salesperson with the same customer. The actual standards for investment advice continue to evolve, and many financial advisors provide advice subject to significant conflicts which often skew their advice toward more expensive and underperforming options.[59] A financial advisor's prospective clients need accurate information to screen advisors to protect themselves from conflicts of interest. Existing clients need this information to determine whether to stay with a broker or whether to investigate products the broker may have previously sold them. This case study focuses on brokers—commission-compensated salespeople affiliated with brokerage firms. Although many of these brokers wear multiple hats and also operate within other capacities, this case study focuses on them as brokers.

Clients often struggle to monitor their broker's performance because of life cycle, behavioral, and innumeracy-related reasons. Many Americans turn to financial advisers for assistance at a time when they may be less capable of protecting their own interests than ever before. Most ordinary savers accumulate retirement savings within some defined-contribution pension, such as a 401(k). Many savers also have individual retirement accounts or taxable brokerage

58. See Christine Lazaro & Benjamin P. Edwards, *The Fragmented Regulation of Investment Advice: A Call for Harmonization*, 4 MICH. BUS. & ENTREPRENEURIAL L. REV. 47 (2014), and Benjamin P. Edwards, *Fiduciary Duty and Investment Advice: Will a Uniform Fiduciary Duty Make a Material Difference?*, 14 J. BUS. & SEC. L. 105 (2014), for discussions of the divergent standards governing financial advisors. Some have begun to turn to automated investment advice platforms known as "roboadvisers" for assistance. *See* Benjamin P. Edwards, *The Rise of Automated Investment Advice: Can Robo-Advisers Rescue the Retail Market?*, 93 CHI.-KENT L. REV. 97, 98 (2018) ("Consumer interest in automated investment advice continues to grow.").

59. One well-known bias is toward recommending higher-fee, actively managed mutual funds. *See* Jacob Hale Russell, *The Separation of Intelligence and Control: Retirement Savings and the Limits of Soft Paternalism*, 6 WM. & MARY BUS. L. REV. 35, 59 n.102 (2015) (likening the debate over active versus passive investing to the debate over climate change because the debate persists even though the relative underperformance of active management has been conclusively established for decades).

accounts. As a saver approaches and enters retirement, she faces an ever-increasing risk of cognitive decline.[60] In this context, retiring savers stand to suffer enormous losses if they entrust their assets to an unfaithful or inept manager. Detecting mismanagement or exploitation may be especially challenging for many Americans because Americans, as a whole, exhibit low levels of basic financial literacy.[61] Despite this, America's securities law regime assumes that Americans will be able to make sense of our disclosure-based regime for financial products.[62] In reality, Americans generally struggle to understand financial products and the obligations financial services professionals actually owe to them.[63]

The regulatory framework also aims to protect Americans through significant oversight of industry actors. The federal Securities and Exchange Commission (SEC) possesses broad jurisdiction over the securities markets.[64] It also delegates authority to FINRA, which "oversee[s] more than 634,000 brokers across the country," and focuses on "protecting investors and safeguarding market integrity in a manner that facilitates vibrant capital markets." [65]

60. *See* ALZHEIMER'S ASSOCIATION, 2020 REPORT, ALZHEIMER'S DISEASE FACTS AND FIGURES REPORT 18 (2020), https://perma.cc/DM6M-MQDZ (explaining that that 10% of persons over 65, and 32% of persons over 85, suffer from dementia).

61. *See* U.S. SEC. & EXCH. COMM'N, STUDY REGARDING FINANCIAL LITERACY AMONG INVESTORS iii (2012), https://perma.cc/C6WZ-3SYQ [hereinafter SEC FINANCIAL LITERACY STUDY] (documenting extensively widespread financial illiteracy).

62. *See* Lisa M. Fairfax, *The Securities Law Implications of Financial Illiteracy*, 104 VA. L. REV. 1065, 1069 (2018) ("[T]he federal securities law regime is inextricably linked to financial literacy because the regime presumes investors have the capacity to sufficiently understand the information being disclosed to them and thus the capacity to make suitable investment choices for themselves.").

63. *See* Edwards, *supra* note 29, at 1462 (discussing "information asymmetry between professional service providers and the public").

64. *See FINRA*, FIN. INDUS. REG. AUTH., https://perma.cc/2QAA-8Q8E (explaining that FINRA "work[s] under the supervision of the SEC").

65. FINRA was formerly known as the National Association of Securities Dealers. FINRA describes itself as a "government-authorized not-for-profit organization that oversees U.S. broker-dealers." *About FINRA*, FIN. INDUS. REG. AUTH., https://perma.cc/V2M2-BW47.

FINRA plays a unique role and bridges the gap between business and government. As a financial self-regulatory organization, FINRA operates with significant oversight from the SEC.[66] It funds its own operations, primarily from member dues.[67] Its members consist of broker-dealer firms—the same entities it regulates.[68]

FINRA also maintains a dispute resolution forum which captures nearly all brokerage industry disputes. When disputes between investors and brokers arise, mandatory pre-dispute arbitration agreements channel nearly all of those disputes into FINRA's dispute resolution forum.[69] FINRA remains responsive to stakeholder concerns and has changed the rules governing its arbitration process to address many of those concerns.[70]

B. BrokerCheck and the Underlying CRD Database

Investors and regulators may learn about complaints other investors have lodged against brokers by reviewing information

66. *See* 15 U.S.C. § 78o-3 (2018) (prescribing the regulations for "registered securities associations").

67. *See* William A. Birdthistle & M. Todd Henderson, *Becoming A Fifth Branch*, 99 CORNELL L. REV. 1, 20 n.101 (2013) (describing FINRA's funding).

68. *See* Andrew Stoltmann & Benjamin P. Edwards, *FINRA Governance Review: Public Governors Should Protect the Public Interest*, 24 PIABA B.J. 369, 370 (2017) (describing FINRA's governance structure).

69. *See* Jill I. Gross, *The Historical Basis of Securities Arbitration as an Investor Protection Mechanism*, 2016 J. DISP. RESOL. 171, 171–72 (2016) ("Today, in fact, most disputes between customers of broker-dealer firms and the firms and their associated persons must be arbitrated through FINRA Dispute Resolution . . . .").

70. One 2008 study found investors were mostly dissatisfied with their experience in the FINRA arbitration forum. *See* Jill I. Gross & Barbara Black, *When Perception Changes Reality: An Empirical Study of Investors' Views of the Fairness of Securities Arbitration*, 2008 J. DISP. RESOL. 349, 386 (2008) ("An overwhelming 71% of customers disagreed with the positive statement that 'I am satisfied with the outcome,' and only 22% of customers agreed with that statement."). *See also* Teresa J. Verges, *Evolution of the Arbitration Forum as a Response to Mandatory Arbitration*, 18 NEV. L.J. 437, 439 (2018) ("FINRA has made significant changes to its arbitration rules governing customer disputes to better serve investors.").

about a broker on BrokerCheck, a website operated by FINRA.[71] BrokerCheck explains that it "is a free tool to research the background and experience of financial brokers, advisers and firms."[72]

Yet this tool has real limits.[73] Information available on BrokerCheck comes from the Central Registration Depository (CRD) and the Investment Adviser Registration Depository (IARD), databases operated by FINRA and jointly owned by the states.[74] The North American Securities Administrators Association (NASAA) and FINRA developed the CRD to consolidate regulatory processes.[75] It "contains the licensing and disciplinary histories on more than 630,000 securities professionals."[76] Much of this information enters the database when brokers file their licensing forms. NASAA has long held that CRD records are state records because state regulations direct brokerages to file forms with the CRD to register their associated persons.[77] Courts also recognize that the CRD data is "'the joint property of the applicant, [FINRA], and those CRD

71. *See BrokerCheck by FINRA*, FIN. INDUS. REGULATORY AUTH., https://perma.cc/KRN3-245G (noting that BrokerCheck is operated and controlled by FINRA).

72. *Id.*

73. *See* Susan Antilla, *The Unbelievable Story of One Broker and Her Firm Fighting to Clean Her Tarnished Record*, THE STREET (June 21, 2016, 11:14 AM), https://perma.cc/W7DH-8DB4 ("[A]nyone who does business with a securities firm would be insane to assume that the stuff they read on Finra's online BrokerCheck tells the whole story.").

74. *See CRD & IARD Resources,* N. AM. SECS. ADMINS. ASS'N, https://perma.cc/2HCM-DN4G (providing informational resources regarding the CRD and IARD).

75. *See CRD at a Glance*, N. AM. SECS. ADMINS. ASS'N, https://perma.cc/TG43-LTQD ("Developed by NASAA and NASD (now FINRA) and implemented in 1981, CRD consolidated a multiple paper-based state licensing and regulatory process into a single, nationwide computer system.").

76. *Id.*

77. *See* Letter from Joseph Borg, N. Am. Secs. Admins. Ass'n President, to Barbara Sweeney, Sec'y Nat. Ass'n Secs. Dealers Regulation, Inc. (Dec. 31, 2001) (on file with the Washington and Lee Law Review).

[s]tates.'"[78] State public records laws generally apply to information contained in the CRD database.[79]

The Exchange Act requires that some information from the CRD database be freely available to the public and grants FINRA discretion to decide the "type, scope, and presentation of information to be provided" to the public.[80] FINRA exercises discretion to curate BrokerCheck disclosures down to reveal only a portion of the information contained in the full CRD. This sanitization has drawn some criticism for obscuring too much information.[81]

Investors need access to information about brokers to protect themselves.[82] FINRA recognizes that customer complaint disclosures are useful in predicting future misconduct.[83] One study by FINRA staff found "that

78. *E.g.* Karsner v. Lothian, 532 F.3d 876, 885 n.9 (D.C. Cir. 2008) (quoting CRD Agreement Amendment) (emphasis in original removed).

79. *See* Advisory Legal Opinion from Robert A. Butterworth, Attorney Gen. of Fla. to Robert F. Milligan, Comptroller of Fla. (Aug. 28, 1998) ("[A]pplication and disciplinary reports maintained by the National Association of Securities Dealers Central Registration Depository that are used by the Department of Banking and Finance in licensing and regulating securities dealers doing business in this state do constitute public records . . . .").

80. 15 U.S.C. § 78o-3(i)(1)(C) (2018).

81. The Public Investors Advocate Bar Association (PIABA), criticized FINRA in 2014 and in 2016 for providing limited information. *See* JASON R. DOSS, CHRISTINE LAZARO, & BENJAMIN P. EDWARDS, THE INEQUALITY OF INVESTOR ACCESS TO INFORMATION (Mar. 6, 2014), https://perma.cc/VSQ4-9L4T (PDF). *See also* HUGH D. BERKSON & MARNIE C. LAMBERT, BROKERCHECK – THE INEQUALITY OF INVESTOR ACCESS TO INFORMATION REMAINS UNABATED – AN UPDATE TO PIABA'S MARCH 2014 REPORT 26 (2016), https://perma.cc/BC3H-K4CP (PDF).

82. *See* Order Granting Accelerated Approval to Filing Related to Changes to Forms U4, U5, and FINRA Rule 8312, 74 Fed. Reg. 23,750, 23,754 (May 20, 2009) (explaining that investors entrust brokers "with their savings and should have sufficient pertinent information available to enable them to select a registered representative with whose background they are comfortable").

83. *See* Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Amend FINRA Rule 8312 to Allow the Dissemination of IAPD Information Through BrokerCheck, 85 Fed. Reg. 26,502, 26,505 (May 4, 2020) (explaining that an inclusion of customer complaints in the CRD system can help "increas[e] the ability of users to understand the potential risk of misconduct" on the part of their brokers).

BrokerCheck information, including disciplinary records, financial disclosures, and employment history of brokers has significant power to predict investor harm."[84] Since investors cannot get complete information from BrokerCheck, the SEC also encourages investors to seek information from state regulators.[85]

Expungement processes—discussed in greater detail in the next subpart—remove information from the CRD database and, consequently, it also disappears from the more broadly known and accessible BrokerCheck website.[86] Importantly, this record suppression likely harms even those public investors who would have never personally conducted due diligence. Industry firms may hire brokers without knowledge of past problems. Even if they do become aware of past expungements, they have no way to know the true merits of any past expunged complaint. In the same way, deletion also inhibits regulators' ability to protect the public.[87]

Ultimately, a well-functioning expungement process must balance appropriate, competing interests. Although brokers will generally prefer to minimize unflattering information about themselves, they have a legitimate interest in removing provably false and defamatory claims. But this interest must be balanced against the need for regulators to have visibility into past complaints and for diligent investors to be able to gather information before turning their life's savings over to a broker. The current process has drawn criticism for improperly

84. HAMMAD QURESHI & JONATHAN SOKOBIN, DO INVESTORS HAVE VALUABLE INFORMATION ABOUT BROKERS? 1 (2015), https://perma.cc/S8QA-VEHC (PDF).

85. *See* Order Approving a Proposed Rule Change to Amend FINRA Rule 8312 (FINRA BrokerCheck Disclosure), 75 Fed. Reg. 41,254, 41,258 (July 15, 2010) ("The Commission urges the public to utilize all sources of information, particularly the databases of the state regulators . . . .").

86. *See infra* Part II.C.

87. *See* Fin. Indus. Reg. Auth., Reg. Notice 14-31 Expungement of Customer Dispute Information 2 (July 30, 2014) https://perma.cc/49B7-UGZ2 (PDF) ("Once information is expunged from the CRD system, it is permanently deleted and, therefore, no longer available to the investing public or regulators.").

balancing these interests and broadly facilitating the removal of information.[88]

C. Expungement Incentives and Process

Expungement processes have evolved substantially over the years. After the CRD's creation in 1981, FINRA would delete information from the database after either an arbitration award or a court decision called for it.[89] FINRA instituted a moratorium on arbitrator-ordered expungements in 1999 after state regulators expressed concern about the removal of information from the CRD database that regulators contended were state records without any court order directing removal.[90]

To resolve the issue, FINRA created a new process, now codified under Rule 2080.[91] Under Rule 2080, brokers can pursue relief two different ways, either by going directly to court or by having a court confirm an arbitration award which

88. A study by the PIABA Foundation found that FINRA's "current expungement process fails to properly balance the interests of investors, regulators, and the public in the CRD maintaining complete and accurate information about brokers against the interest of brokers in protecting their reputations from false customer complaints." JASON R. DOSS & LISA BRAGANÇA, 2019 STUDY ON FINRA EXPUNGEMENTS: A SERIOUSLY FLAWED PROCESS THAT SHOULD BE STOPPED IMMEDIATELY TO PROTECT THE INTEGRITY OF THE PUBLIC RECORD 7 (2019), https://perma.cc/9FSY-GJ6F (PDF).

89. *See* Nat. Ass'n Secs. Dealers, Notice to Members 01-65 Request for Comment on Proposed Rules Relating to Expungement from the CRD 563 (Oct. 2001), https://perma.cc/CK26-BFZB (PDF) (requesting comment on changing procedures).

90. *See* Nat. Ass'n Secs. Dealers, Notice to Members 99-09 Moratorium on Arbitrator-Ordered Expungements from the CRD 47 (Feb. 1999), https://perma.cc/7FDZ-8569 (PDF)

> NASD Regulation has taken the position that expungement of information from the CRD system that is ordered by an arbitrator and contained in an award should be afforded the same treatment as a court-ordered expungement. NASAA disagrees with this position and has informed NASD Regulation that it does not believe that arbitrator-ordered expungements should be afforded the same treatment as court-ordered expungements.

91. *See* Seth E. Lipner, *The Expungement of Customer Complaint CRD Information Following the Settlement of a FINRA Arbitration*, 19 FORDHAM J. CORP. & FIN. L. 57, 68–76 (2013) (tracing the early history of FINRA Rule 2080).

recommends expungement.[92] Rule 2080 requires brokers seeking judicial assistance with an expungement to "name FINRA as an additional party and serve FINRA with all appropriate documents unless this requirement is waived."[93] FINRA may waive the requirement to name it as a party if the underlying customer claim is: (i) "factually impossible or clearly erroneous;" (ii) the broker had no involvement in the conduct; or (iii) the "claim, allegation or information is false."[94] FINRA also reserves the right to waive the requirement to name it as a party under "extraordinary circumstances."[95]

When the SEC approved Rule 2080, it also contained the requirement to name FINRA as a party to the court action unless FINRA opted to waive the requirement.[96] The SEC approved the framework because it believed "that the potential involvement of [FINRA] at the court confirmation level will provide greater safeguards than simple application of the rule to members."[97] As conceived, the system aimed "to shift final authority on expungement away from arbitrators, and to courts of law."[98]

Yet courts of law are not well-situated to constrain expungements. A court may only vacate an arbitration award in rare circumstances.[99] Both federal statutory law and precedent leave courts unable to conduct any significant review of an

92. *See* FIN. INDUS. REG. AUTH., RULE 2080 (2009) ("Obtaining an Order of Expungement of Customer Dispute Information from the Central Registration Depository (CRD) System.").

93. *Id.*

94. *Id.*

95. *Id.*

96. The SEC first approved a nearly identical, earlier iteration of Rule 2080 issued by the National Association of Securities Dealers (NASD).

97. Order Granting Approval of Proposed Rule Change Relating to Proposed NASD Rule 2130 Concerning the Expungement of Customer Dispute Information from the Central Registration Depository System, 68 Fed. Reg. 74,667, 74,671 (Dec. 24, 2003).

98. Reinking v. Fin. Indus. Reg. Auth., No. A-11-CA-813-SS, 2011 WL 13113323, at *3 (W.D. Tex. Dec. 1, 2011).

99. *See* 9 U.S.C. § 10 (2018) (setting out circumstances where a court may vacate an arbitration award).

arbitrator's decision absent rare circumstances.[100] Absent some indication that the arbitrator was biased or otherwise refused to listen to evidence, it remains extraordinarily difficult to prevent an arbitration award from being confirmed in a court hearing. Courts simply do not get into the weeds when reviewing arbitration awards. Absent extraordinary circumstances, they simply confirm them.[101]

Now, most expungement hearings proceed under a mix of official FINRA rules, guidance, and arbitrator training materials. Because the critical fact-centric expungement hearings occur within an arbitration forum, the public has little or no access to information about the hearings.[102] Only in the rarest circumstances will a court review the evidence considered by an arbitrator before confirming an arbitration award.

Although most brokers pursue expungements through the FINRA arbitration process before having a court confirm the award, a few still attempt to go directly to court proceedings.[103] Courts divide over whether and how to consider these direct-to-court filings. Some courts evaluating these requests have sought to weigh the equities, balancing the public's rights against the broker's interest to reach a decision.[104] Others have

100. *See* Hall St. Assocs., L.L.C. v. Mattel, Inc., 552 U.S. 576, 584 (2008) ("We now hold that §§ 10 and 11 respectively provide the FAA's exclusive grounds for expedited vacatur and modification.").

101. *See, e.g.*, Walker v. Connelly, No. 100681/08, 2008 WL 4754138, at *7 (N.Y. Sup. Ct. Oct. 16, 2008) (confirming arbitration award over opposition).

102. Notably, FINRA itself is not subject to the Freedom of Information Act because it is not a government agency. A quirk in the law also exempts information about the SEC's oversight of FINRA from disclosure. *See* Pub. Invs. Arbitration Bar Ass'n v. U.S. Sec. Exch. Comm'n, 930 F. Supp. 2d 55, 72–73 (D.D.C. 2013), *aff'd*, 771 F.3d 1 (D.C. Cir. 2014) ("[A]ll records relating to the SEC's examination reports—including reports relating to the administrative functions of FINRA—are exempt from disclosure under the FOIA.").

103. *See In re* Lickiss, No. C-11-1986 EMC, 2011 WL 2471022, at *2 (N.D. Cal. June 22, 2011) ("[A]s FINRA conceded at the oral argument herein, its rules do not require a member or associated person to first present a request to expunge to FINRA before going to court under Rule 2080(a).").

104. *See* Lickiss v. Fin. Indus. Reg. Auth., 146 Cal. Rptr. 3d 173, 180 (2012) (instructing lower court to consider the equities in evaluating an expungement request). *See also* Reinking v. Fin. Indus. Reg. Auth., No. A-11-CA-813-SS,

declined jurisdiction on the theory that the broker already has a remedy through the FINRA arbitration process.[105]

1. Incentives

Understanding how the arbitration-facilitated expungement process operates requires a sense about how different incentives influence actors who participate within the arbitration forum. These fundamental incentive problems bias the expungement process toward facilitating the removal of information from public records.

a. Customers Have No Real Incentive to Participate

At the outset, it has long been clear that customers have little incentive to oppose a broker's request to expunge information from public records.[106] Harmed customers have no need to ensure that public information about the broker is accurate once they have settled or otherwise resolved their dispute. These customers already know to avoid the broker who swindled them. Unsurprisingly, customers rarely appear to contest a broker's request for expungement.[107]

At best, harmed customers may feel they have some civic duty to protect the information if they understand the broader

2011 WL 13113323, at *2 (W.D. Tex. Dec. 1, 2011) ("[T]he Court finds (1) it has the power to expunge a CRD record, and (2) the correct guiding standard should be whether the disputed record has any regulatory value . . . .").

105. *See* Aiguier v. Fin. Indus. Reg. Auth., No. SUCV201602491BLS1, 2017 WL 1336579, at *6–7 (Mass. Super. Mar. 11, 2017) (declining equity jurisdiction over FINRA because it would "circumvent the arbitration provisions that govern the resolution of claims that the plaintiff asserts against NYLife. Accordingly, this court holds that it does not have jurisdiction in equity to consider the plaintiff's claim for expungement.").

106. *See* Letter from Karen Tyler, N. Am. Secs. Admins. Ass'n President and N.D. Sec. Comm'r, to Nancy M. Morris, Sec'y, Sec. Exch. Comm'n (Apr. 24, 2008) (on file with the Washington and Lee Law Review) (explaining "the claimant and their counsel have no incentive to participate in the expungement hearing. Quite the opposite is true. Claimants would incur additional costs, in the way of attorney's fees and time, in order to participate and would gain no benefit through their participation.").

107. One study of over a thousand expungement awards found that customers appeared only 13% of the time. *See* DOSS & BRAGANÇA, *supra* note 88, at 4.

systemic ramifications of a broker's attempt to expunge information. Yet aside from the dry pleasure of protecting the integrity of public information, customers receive no real benefits by opposing a broker's expungement request.

Consider a customer's financial interests. One court recognized that "customers have no financial interest in the outcome of [expungement] claims the plaintiff asserts in the [c]omplaint and may well be disinterested in whether BrokerCheck reports their complaints against him or not."[108] Customers do not receive any additional compensation if they successfully oppose a broker's expungement request. In most instances, customers will need the assistance of a lawyer to mount any reasonable opposition to an expungement request— and they should not be compelled to defend an action.[109] Few lawyers will assist customers and oppose expungements on a pro bono basis. Even if the customer could find pro bono assistance, many would likely prefer to spend their time doing other things than participating in arbitration hearings where they will likely be called a liar.

Customers face little downside from spending their time on more enjoyable activities. While customers may theoretically face reputational risk if arbitrators deem their complaint "false" and recommend that it be expunged, this will likely have no real-world effect on them. When the customers are not parties to the arbitration, the expungement awards do not ordinarily even identify them by name.[110]

108. Aiguier v. Fin. Indus. Reg. Auth., Inc., No. 16-02491, 2017 WL 1311986, at *4 (Mass. Super. Ct. Mar. 10, 2017).

109. *See id.*

> [T]he court has grave concerns about naming a person as a defendant in a case in which no claim is asserted against him/her, thereby putting that person to the potential expense of retaining counsel to explain the nature of the proceeding and what if anything he/she must do in response to being served with a summons and complaint.

110. *See, e.g.* Loris v. Sec. Am., Inc., No. 19-02661, 2020 WL 2494752, at *1 (May 7, 2020) (Thompson, Arb.) ("[C]ustomer in Occurrence Number 1933223 (the 'Customer') was served with the [s]tatement of [c]laim").

b. Weak Claimant Attorney Incentives

While the customer receives notice of the expungement hearing, the attorney who represented that customer can only learn of the expungement proceeding if the customer tells her. Even when the attorney learns about a hearing, the attorneys who regularly represent claimants in FINRA arbitration also have little incentive to convince clients to aggressively oppose expungement attempts. Most claimant attorneys take cases on a contingency basis. Representing a client at an expungement hearing usually requires a substantial amount of time and preparation. After expending this effort, the claimant's attorney will not recover any funds if she successfully opposes an expungement. Very few customers are willing to pay an attorney fees to oppose an expungement request.

Still, claimants' attorneys may have some incentive to oppose expungements because they operate as repeat players in FINRA arbitrations. A string of expungement awards finding that they file "false" claims may hurt their reputations. They may also have an interest in preserving information about past claims to assist future clients. A claimant's attorney may desire to ask a broker about past complaints or use the information in the CRD database to identify possible additional witnesses who could testify about a broker's behavior.

Ultimately, claimant attorneys who learn of an expungement proceeding may hesitate to devote significant resources to opposing the expungement request. Although preserving information may benefit future clients, the claimants' bar is not monolithic. A lawyer who expends resources to protect information from expungement may never be positioned to use the information in a later arbitration hearing because some other lawyer may represent future clients who were harmed by the particular broker. In contrast, the broker or brokerage firm will almost certainly benefit from removing the information from the public record.

Securities arbitration clinics affiliated with law schools may contain the only claimant attorneys with a real incentive to

oppose broker requests for expungement.[111] An expungement hearing may provide an opportunity for a law student to both protect the public and gain practical experience. Regrettably, only about a dozen securities clinics exist and they rarely appear in expungement hearings because the hearings may happen on relatively short notice, making it difficult for clients to find the pro bono clinics and for students to prepare.

c. Brokers Have Strong Incentives to Seek Expungement

In contrast, brokers have strong incentives to seek expungements. We know that brokers place substantial value on expunging unflattering information because they regularly pay lawyers to secure expungements. Public customer complaints likely inhibit a broker's ability to drum up new business and continue to make money. Customers who do review a broker's record may pause if they see that other investors have raised complaints.

Brokers may also seek expungement to reduce regulatory pressure and scrutiny. FINRA's enforcement process now prioritizes "high risk" brokers and imposes its harshest penalties on repeat offenders.[112] In particular, FINRA now focuses special oversight on "high-risk brokers."[113] Although it does not disclose the precise method it uses to identify high-risk brokers, FINRA has disclosed that its criteria include settlements, customer complaints, disclosures, and proximity to other high-risk brokers.[114] The expungement process offers a

111. *See* Jill Gross, *The Improbable Birth and Conceivable Death of the Securities Arbitration Clinic*, 15 CARDOZO J. CONFLICT RESOL. 597, 600 (2014) (describing securities arbitration clinics).

112. *See* Honigsberg & Jacob, *supra* note 22, at 4 (explaining that the FINRA disciplinary regime "imposes increasingly severe sanctions on repeat offenders").

113. *See* Melanie Waddell, *Here's How FINRA Defines a 'High-Risk' Broker,* THINK ADVISOR (May 23, 2018, 2:02 PM), https://perma.cc/L8G8-BKQF (describing FINRA's assessment mechanisms to determine if a broker is high-risk).

114. *See id.* (stating that FINRA looks at a broker's "settlements, complaints, disclosures, employment history/termination history, exam attempts, geography . . . [and] individuals who associate with high-risk brokers").

method to purge many of the identifying factors from a broker's record and possibly allow her to sink beneath the radar.[115] If higher-risk brokers use the expungement process to avoid scrutiny, it would explain one finding that brokers who have received "expungements are 3.3 times as likely to engage in new misconduct as the average broker."[116]

Negative information in a broker's CRD creates real risk for a broker facing a FINRA enforcement action. FINRA's guidance for sanctions instructs adjudicators to look for a pattern when reviewing a broker's record.[117] FINRA's guidance explains that adjudicators considering arbitration awards or settlements "should rely on the CRD description of the amount of the award or settlement."[118] Within the disciplinary proceeding at least, "parties are precluded from challenging the arbitration award or contesting the CRD description of arbitration settlements."[119] Expunging information from the CRD may reduce the broker's exposure to recidivism-related enhancements in disciplinary sanctions.[120]

Brokers may also pursue expungements because a clean record may help a broker remain at higher-tier industry firms. Remaining affiliated with a marquee firm grants status and often greater access to more profitable high net-worth investors.[121] One recent economics paper found that brokers with records of misconduct tend to migrate from higher-tier to

115. Although it has not disclosed that it does so, FINRA might keep a log of brokers with expungements for use in identifying higher risk brokers.

116. Honigsberg & Jacob, *supra* note 22, at 4.

117. *See* FIN. INDUS. REG. AUTH., FINRA SANCTION GUIDELINES 3 (Mar. 2019), https://perma.cc/8K49-LYZY (PDF) (**"**Adjudicators should draw on their experience and judgment when evaluating if a respondent's [d]isciplinary and [a]rbitration [h]istory establishes a pattern.").

118. *Id.*

119. *Id.*

120. *See* Honigsberg & Jacob, *supra* note 22, at 4 ("[I]f brokers are abusing the expungement process, . . . removing misconduct from BrokerCheck will . . . hamper the effectiveness of FINRA's disciplinary regime, which imposes increasingly severe sanctions on repeat offenders.").

121. *See* Mark Egan, Gregor Matvos & Amit Seru, *The Market for Financial Adviser Misconduct*, 127 J. POL. ECON. 233, 275 (2019) ("[D]efrauding large investors may be more profitable, since they have more wealth.").

lower-tier industry firms.[122] Higher-tier brokerage firms seemingly care more about their reputations and keep discipline by deciding not to employ brokers with misconduct records.[123] In essence, a broker may be able to enhance her chances of staying at or migrating to a higher-tier firm by securing an expungement.

d. Brokerage Firms Have Little Incentive to Oppose

In expungement-only cases, brokers seeking expungements often name their current or former employers as respondents.[124] Importantly, brokerage firms have little incentive to oppose a broker's expungement request and may actually benefit if the broker secures an expungement.[125] One recent study of over a thousand arbitration awards involving expungements found that brokerage firms "did not object or otherwise oppose the individual broker's expungement request . . . over 98% of the time."[126]

Brokerage firms typically benefit when their current and former brokers secure expungements because it lowers their regulatory profile and reduces their reputation and litigation risk.[127] FINRA imposes additional obligations on firms employing brokers with "a recent history of customer complaints, disciplinary actions involving sales practice abuse

122. *See id.* at 237 (explaining that the firms that hire brokers with misconduct records "are less desirable and offer lower compensation").

123. *See id.* at 236 ("Firms, wanting to protect their reputation for honest dealing, would fire advisers who engage in misconduct. Other firms would have the same reputation concerns and would not hire such advisers.").

124. *See Notice to Arbitrators and Parties on Expanded Expungement Guidance*, FIN. INDUS. REG. AUTH., https://perma.cc/VC8L-5YEV (last updated Sept. 2017) ("In some instances, an associated person will file and arbitration claim against a member firm solely for the purpose of seeking expungement, without naming the customer in the underlying dispute as a respondent.").

125. *See* Lisa Bragança & Jason Doss, *How Expungement-Only Cases Are "Gamed, Exploited and Abused" by Brokers*, FINANCIAL PLANNING (Oct. 29, 2019, 11:48 AM), https://perma.cc/RH4T-EH58 ("Since brokers and their brokerage firms both have an interest in erasing customer complaints from the brokers' records, they are rarely in opposition to each other.").

126. *Id.*

127. *See* Honigsberg & Jacob, *supra* note 22, at 6 (recognizing that brokerage firms care more about public, rather than private, misconduct).

or other customer harm, or adverse arbitration decisions."[128] Implementing heightened supervisory procedures for brokers with checkered pasts costs firms money and may expose them to additional liability if the broker harms another customer or if the firm fails to set up adequate enhanced supervision.[129] FINRA tells its firms that they should consider, among other things, "a pattern of unadjudicated matters, such as unadjudicated customer complaints" in determining whether to implement heightened supervision for a particular broker.[130] Successful expungements may cause a "pattern" to disappear from the regulatory record, removing the need for heightened supervision.

One rare unsuccessful expungement attempt showcases how a brokerage firm's interest generally aligns with a broker's interest. In 2019, Paul Douglas Larson named brokerage firm Larson Financial Securities, LLC as a respondent in an arbitration where he sought an expungement.[131] BrokerCheck reveals that the managing member of Larson Financial Securities, LLC is Larson Financial Holdings, LLC.[132] A disclosure form for an affiliated entity reveals that Paul Douglas Larson is a control person for Larson Financial Holdings.[133] In essence, Paul Douglas Larson filed an arbitration against an entity he controls, and somehow managed to defy the odds and lose.[134] The loss might be attributable to unnamed customers

128. *See* Fin. Indus. Reg. Auth., Regulatory Notice 18-15 Guidance on Implementing Effective Heightened Supervisory Procedures 2 (Apr. 30, 2018), https://perma.cc/UB23-PYRE (PDF) (discussing heightened supervision requirements).

129. *See id.* at 3 ("The failure to assess the adequacy of its supervisory procedures in light of an associated person's history of industry or regulatory-related incidents would be closely evaluated in determining whether the firm itself should be subject to disciplinary action for a failure to supervise.").

130. *Id.*

131. Larson v. Larson Fin. Secs., LLC, No. 19-02660, 2020 WL 2494751, at *1 (May 5, 2020) (Matek, Arb.).

132. *Larson Financial Securities, LLC*, BROKERCHECK, https://perma.cc/R4DX-FWZZ.

133. LARSON FIN. GRP., LLC, FORM ADV, CRD NUMBER: 140599 28–29 (2020), https://perma.cc/79EA-RFGN (PDF).

134. *Larson*, 2020 WL 2494751, at *1.

who "filed submissions in opposition to the request for expungement."[135] Notably, one customer actually "appeared at the expungement hearing" and counsel for the customers "appeared at all of the hearings on expungement and opposed" the request.[136]

e. Arbitrator Selection Pressure

Arbitrators within FINRA's forum also face incentives to facilitate expungement requests. FINRA's arbitrators serve as independent contractors and are paid by the number of hearing sessions they conduct.[137] Although an arbitrator might request additional information and conduct additional, lengthy hearing sessions for expungement requests, the arbitrator would likely only get to do this once.[138] Critically, repeat business for arbitrators depends on being selected to conduct arbitrations and only the named parties have any say in the arbitrator selection process.[139] An arbitrator who denies expungement requests will likely stop receiving expungement cases.

When a broker seeking an expungement files a FINRA arbitration against an employer, both the broker and the employer will participate in FINRA's arbitrator selection process.[140] To reduce costs and trigger a proceeding with a single arbitrator, brokers have been filing these actions with a claim for $1.00 in nominal damages, a practice FINRA recently moved

135. *Id.*

136. *Id.*

137. FIN. INDUS. REG. AUTH., RULE 13214 (2019).

138. *See* Kate Webber Nuñez, *Toxic Cultures Require A Stronger Cure: The Lessons of Fox News for Reforming Sexual Harassment Law*, 122 PENN ST. L. REV. 463, 507–08 (2018) ("Arbitrators also have financial incentives to favor employers who, unlike employees, are in a position to hire the arbitrator again in the future.").

139. *Cf.* Bradley A. Areheart, *Organizational Justice and Antidiscrimination*, 104 MINN. L. REV. 1921, 1945 (2020) ("[E]mployers, as 'repeat players,' can choose arbitrators that have been known to rule in favor of other employers.").

140. FIN. INDUS. REG. AUTH., FINRA'S DISPUTE RESOLUTION PROCESS 3 (2012), https://perma.cc/93BS-29ZT (PDF) ("Both sides are allowed to remove or strike some of the arbitrators on the list of consideration and to rank the remaining names in order of their preference.").

to constrain.[141] To select the single arbitrator who will hear the case, FINRA first provides a list of ten names to the claimant and the respondent.[142] Both the claimant and the respondent may each strike up to four arbitrators from the list and rank the remaining arbitrators.[143] If both the claimant and the respondent favor arbitrators who routinely grant expungements, an arbitrator who occasionally rejects an expungement request may be less likely to be selected.[144]

Some evidence suggests that parties in expungement-only cases prefer arbitrators who routinely grant expungements. A recent study by the PIABA Foundation found that the three arbitrators most frequently selected for expungement-only cases "granted expungement requests over 95% of the time."[145]

f. Weak Institutional Oversight Incentives

FINRA also faces institutional constraints limiting its ability to vigorously protect information contained in the CRD.[146] Critically, reviewing and challenging arbitration

141. *See* Notice of Filing of Proposed Rule Change to Amend the FINRA Code of Arbitration Procedure for Customer Disputes and the FINRA Code of Arbitration Procedure for Industry Disputes to Apply Minimum Fees to Requests for Expungement of Customer Dispute Information, 85 Fed. Reg. 11,165, 11,167 (Feb. 26, 2020) ("FINRA is aware that associated persons who file a straight-in request often add a small monetary claim (typically, one dollar) to the expungement request to reduce the fees assessed against the associated person and qualify for an arbitration heard by a single arbitrator.").

142. *See Arbitrator Selection*, FIN. INDUS. REG. AUTH., https://perma.cc/MF44-TY7M ("For claims of up to $100,000, the parties receive one list of 10 chair-qualified non-public arbitrators . . . . For claims of more than $100,000 for unspecified or non-monetary claims, the parties receive two lists (one including 10 non-public chair-qualified arbitrators, and one including 20 non-public arbitrators).").

143. *Id.*

144. *See* David A. Hoffman & Erik Lampmann, *Hushing Contracts*, 97 WASH. U. L. REV. 165, 217 (2019) ("[A]rbitrators face incentive structures to not depart from the parties' settled expectations, and are not rewarded, reputationally or otherwise, for issuing public-facing rulings.").

145. DOSS & BRAGANÇA, *supra* note 88**Error! Bookmark not defined.**, at 4.

146. *See* Benjamin P. Edwards, *The Dark Side of Self-Regulation*, 85 U. CIN. L. REV. 573, 608 (2017) ("[S]elf-regulatory bodies may be particularly

awards in court would consume substantial time and resources. My search revealed 935 different arbitration awards involving expungement in 2019 alone. Effective review and oversight would likely require substantial independent investigation, something FINRA never committed to do when it agreed to create and manage the CRD database. Although FINRA has responded to criticisms of its expungement process and made significant reforms over the years, it has not generally led efforts to protect information contained in the CRD.[147] Its members may also not push FINRA to lead efforts to preserve the public availability of unflattering information about brokers.[148]

2. Arbitrator Fact-Finding in Expungement Hearings

There are two different routes to an expungement hearing within FINRA's arbitration forum, either at the conclusion of a customer arbitration or in a separate arbitration without naming the complaining customer as a party. Brokers named as parties to a customer arbitration "may request expungement during that arbitration, but [are] not required to do so."[149] In practice, many brokers have waited "years after FINRA closed the Underlying Customer Case" to request expungement.[150] Troublingly, these delays often mean that important evidence and witnesses have been lost to the passage of time.[151]

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lethargic protectors in situations where actions in the public's interest would undercut private profits.").

147. *See* Mason Braswell & Jed Horowitz, *Top Merrill Broker Patrick Dwyer Leaves Amid Accusations*, ADVISORHUB (Aug. 22, 2019), https://perma.cc/7YKF-5GGM (describing FINRA's move to block confirmation of an arbitration award directing expungement as a "rare step").

148. *See, e.g.*, Honigsberg & Jacob, *supra* note 22, at 7 (describing a Human Resources Office's decision to ignore allegations of an employee's misconduct until that misconduct became public).

149. Fin. Indus. Reg. Auth., Regulatory Notice 17-42 Expungement of Customer Dispute Information 5 (Dec. 6, 2017), https://perma.cc/HB2Z-YAV3 (PDF).

150. *Id.*

151. *See id.* ("Given the length of time between case closure and filing of the request, in many of these instances, the customers cannot be located and any documentation that could explain what happened in the case is not available or cannot be located.").

Adversarial failure explains many stale expungements. Under the arbitration forum's rules, brokers should face at least some challenge pursuing an expungement through FINRA arbitration after more than six years from the time the information appeared in the CRD database.[152] FINRA's rules explain that its arbitration forum may only be used within six years of the occurrence or event giving rise to the claim.[153] Despite this, arbitrators regularly expunge information dating back 20 years or more.[154] Arbitrators may not apply—or even consider—the eligibility rule because no party to the arbitration points out that the dispute may no longer be eligible to be heard in the FINRA forum.[155] Of course, arbitrators may interpret the rule in some way allowing access to the forum, but it appears odd that arbitrators do not regularly even consider the issue when presented with stale expungement requests.

Notably, the current rules do not require brokers to make the complaining customer a party.[156] Brokers will frequently file their action against a current or former employer and provide notice to a customer shortly before the final evidentiary

152. *See* FIN. INDUS. REG. AUTH., RULE 13206 (2011) (explaining that in industry disputes "[n]o claim shall be eligible for submission to arbitration under the Code where six years have elapsed from the occurrence or event giving rise to the claim").

153. *See* FIN. INDUS. REG. AUTH., RULE 12206 (2011) (directing that in customer disputes "[n]o claim shall be eligible for submission to arbitration under the Code where six years have elapsed from the occurrence or event giving rise to the claim").

154. *See* Rosenberg v. A. G. Edwards & Sons, Inc., No. 19-02801, 2020 WL 2494754, at *2 (May 8, 2020) (Mintzer, Arb.) (recommending expungement where the underlying information "was received by Respondent on July 17, 2000 and solely alleged 'breach of fiduciary duty' concerning an 'Equity Listed (Common & Preferred Stock).'").

155. *See* FIN. INDUS. REG. AUTH., RULE 12206 (2011) (placing responsibility for determining eligibility on the party who submits the claim, not the arbitrator).

156. FINRA's training materials for its arbitrators note that brokers may "file an arbitration claim against a member firm solely for the purpose of seeking expungement, without naming the customer in the underlying dispute as a respondent." FIN. INDUS. REG. AUTH., FINRA OFFICE OF DISPUTE RESOLUTION EXPUNGEMENT TRAINING 14 (2016), https://perma.cc/NLE2-6657 (PDF) [hereinafter EXPUNGEMENT TRAINING].

hearing.[157] Brokers name their employers on the theory that the employers were the ones who actually reported the information to the CRD.[158] These expungement-only arbitrations have dramatically increased in recent years. The PIABA Foundation found that expungement-only cases increased "924% from 2015 to 2018."[159]

The trend has continued since that time. Consider one recent arbitration award recommending expungement.[160] Steven Phillip Margulin sued his current employer, Centaurus Financial, Inc., "seeking expungement of a customer complaint" and relying on evidence from 2003—seventeen years ago.[161] In responding to Margulin's complaint, "Centaurus stated that it does not oppose" the "expungement request."[162] Margulin provided notice to the estate of the deceased customer on February 21, 2020, and a telephonic hearing was held thirty-three days later on March 25, 2020.[163] The arbitrator granted the request and recommended that the customer dispute information be expunged from the CRD database, finding that the information was "false."[164] Once Margulin confirms the award in court, the information will be deleted from the CRD database. Yet, if asked, an arbitrator might have found this expungement request ineligible for arbitration under FINRA's Rules because the dispute was over six years old.[165]

With limited information and briefing, arbitrators regularly make critical factual findings bearing on whether past customer

157. *See id.* ("[A]rbitrators should order the associated persons to provide a copy of their Statement of Claim to the customer(s) involved in the underlying arbitration.").

158. *See* FIN. INDUS. REG. AUTH., RULE 4530 (2015) (requiring the firm to report broker misconduct).

159. DOSS & BRAGANÇA, *supra* note 88, at 3.

160. *See* Margulin v. Centaurus Fin., Inc., No. 19-01639, 2020 WL 1943589, at *3 (Apr. 17, 2020) (Tindall, Arb.) (recommending "the expungement of all references to the Underlying Complaint").

161. *Id.*

162. *Id.*

163. *Id.*

164. *Id.*

165. *See* FIN. INDUS. REG. AUTH., RULE 13206 (2011) ("No claim shall be eligible for submission to arbitration under the Code where six years have elapsed from the occurrence or event giving rise to the claim.").

complaints should be expunged from the public record. Today, arbitrators must at least hold hearings before granting expungement requests.[166] FINRA explains that arbitrators should only recommend expungement of customer dispute information from the public record "when the expunged information has no meaningful regulatory or investor protection value."[167]

The process has evolved over time as FINRA has implemented change after change to address known problems. When past guidance directing arbitrators to make findings did not generate consistent affirmative findings by arbitrators, FINRA amended its code.[168] Both FINRA Rule 12805 (customer disputes) and Rule 13805 (industry disputes) now "establish specific procedures that arbitrators must follow before ordering expungement of customer dispute information from the CRD system."[169]

Arbitration awards recommending expungement must contain specific findings.[170] Although arbitrators do not ordinarily have to explain any basis for their decisions, FINRA Rule 12805 and 13805 require the arbitrator to "indicate in the arbitration award which of the Rule 2080 grounds for expungement serves as the basis for its expungement order."[171] For example, an arbitrator might find that a broker had no involvement in a customer complaint or that it was false because the broker did not even work at the firm at the time of

166. FIN. INDUS. REG. AUTH., RULE 12805 (2009); FIN. INDUS. REG. AUTH., RULE 13805 (2009).

167. *Frequently Asked Questions about FINRA Rule 2080 (Expungement)*, FIN. INDUS. REG. AUTH., https://perma.cc/D7WW-APB2 [hereinafter *FAQ About FINRA Rule 2080*].

168. *See* Fin. Indus. Reg. Auth., Regulatory Notice 08-79 Expungement 1 (Dec. 2008), https://perma.cc/ZTX7-3QPZ (PDF) (describing changes to FINRA's procedural codes for both customer and industry disputes).

169. *Id.* at 2.

170. *See FAQ About FINRA Rule 2080*, *supra* note 167 ("Arbitrators considering expungement relief are required to complete training provided by FINRA Dispute Resolution regarding . . . the requirement to make specific findings if they decide that expungement is appropriate.").

171. FIN. INDUS. REG. AUTH., RULE 12805(c) (2009); FIN. INDUS. REG. AUTH., RULE 13805(c) (2009).

the alleged misconduct.[172] It also requires arbitrators to "provide a brief written explanation of the reason(s) for its finding that one or more Rule 2080 grounds for expungement applies to the facts of the case."[173] In approving the rule change, the SEC found that "additional procedures, such as the required review of settlement documents, and the written explanation of the regulatory basis and reason for granting expungement, in the proposed rule are designed to help assure that the expungement process is not abused."[174] The SEC also encouraged FINRA to "use its authority to review expungement requests to ensure that expungement is an extraordinary remedy."[175]

FINRA's training materials instruct the arbitrators crafting these findings. They explain that the "written explanation should provide regulators and other interested parties with additional insight into why the arbitrators recommended expungement and any facts and circumstances they found in support of the recommendation."[176] While the goal of the rule change was to ensure that arbitrators were recommending expungement selectively as an "extraordinary remedy," that appears not to have happened.[177] Arbitration awards recommending expungement are more prevalent than before and generally do not show evidence of having considered any evidence against expungement.[178]

172. *See* FIN. INDUS. REG. AUTH., RULE 2080 (2009) ("Upon request, FINRA may waive the obligation to name FINRA as a party if FINRA determines that . . . the registered person was not involved in the alleged investment-related sale practice violation.").

173. FIN. INDUS. REG. AUTH., RULE 12805 (2009).

174. Order Approving a Proposed Rule Change Amending the Codes of Arbitration Procedure to Establish Procedures for Arbitrators to Follow When Considering Requests for Expungement Relief, 73 Fed. Reg. 66,086, 66,089 (Nov. 6, 2008).

175. *Id.* at 15.

176. EXPUNGEMENT TRAINING, *supra* note 156, at 16.

177. *Id.* at 8.

178. *See* DOSS & BRAGANÇA, *supra* note 88 ("But today, the floodgates are wide open and the number of expungement cases filed by brokers against their brokerage firms has risen nearly 1,000% in the last four years.").

3. Customers Receive Inconsistent and Limited Notice

No FINRA Rule now requires a broker to provide notice to a former customer about an expungement hearing.[179] The rules also do not require any notice to the securities regulators in states where the broker holds a license. The "requirement" to provide notice appears in the arbitrator training materials, which explain than an arbitrator must "order the associated persons to provide a copy of their Statement of Claim to the customer(s)."[180] FINRA emphasizes that "without this directive from the arbitrators, the customer(s) may not even be aware that an expungement claim is pending regarding their prior dispute."[181]

a. Arbitrators Do Not Always Require Notice

Despite guidance instructing them to require notice be given to former customers, arbitrators do not always actually require that customers receive notice. In some instances, customers receive no notice before arbitrators hold hearings to determine whether to recommend expungement.[182] This may occur when counsel for a party argues for some idiosyncratic interpretation of FINRA's guidance. For example, in one arbitration, the attorney argued that he did not need to provide notice to three different customers because "it was his position that the notification requirements of an expungement request

179. Although FINRA's Board of Governors approved codifying its expanded expungement guidance in 2018, it has not yet codified the guidance. *See Update: FINRA Board of Governors Meeting*, FIN. INDUS. REG. AUTH. (Dec. 21, 2018), https://perma.cc/9CUE-FVVL ("The Board approved proposed amendments to the Codes of Arbitration Procedure for Customer and Industry Disputes to codify the Notice to Arbitrators and Parties on Expanded Expungement Guidance and modify the fees for small claim expungement.").

180. EXPUNGEMENT TRAINING, *supra* note 156, at 14.

181. *See id.* (elaborating that "notice provides the customer(s) with the opportunity to advise the arbitrators and parties of their position on the expungement request, which may assist arbitrators in making the appropriate finding under Rule 2080").

182. *See, e.g.*, Dwyer v. Merrill Lynch, Pierce, Fenner & Smith, Inc., No. 16-02781, 2017 WL 3189311, at *1 (July 20, 2017) (Ainbinder, Thorpe, & Santillo, Arbs.) (recommending expungement of six customer complaints even though the broker made no attempt to notify three of the customers).

applies to customers who have filed for arbitration."[183] The arbitration panel agreed.[184]

b. Short Notice Windows

Determining actual notice times remains difficult. Arbitration awards do not always reveal the date on which a broker seeking expungement notifies a former customer that a hearing will be held. For example, Mark Kravietz procured an arbitration award recommending that customer information be expunged from public records on May 1, 2020.[185] Although the award does not reveal the date on which notice was sent to the customer, Kravietz provided FINRA with an Affirmation of Service on or about April 9, 2020, before a telephonic hearing was held on April 28, 2020, just 19 days later.[186] Unsurprisingly, the award found that the "underlying customer did not participate in the expungement hearing and did not oppose the request for expungement."[187]

Although arbitrators do not seem to aggressively police notice periods, they may balk at egregiously short periods. In one instance, an arbitrator postponed an expungement hearing on account of inadequate notice.[188] The broker had transmitted notice of the hearing "via priority express mail notice" just three days before the hearing.[189]

FINRA's expungement training materials do not specify that notice must go out any particular number of days before a hearing may be held.[190] While there are FINRA Rules specifying dates for motions and responses in its forum, the time period for

183. *Id.*

184. *Id.*

185. Kravietz v. U.S. Fin. Services, Inc., No. 20-00601, 2020 WL 2235746, at *1 (May 1, 2020) (Lascar, Arb.).

186. *Id.*

187. *Id.*

188. *See* Papadopoulos v. Lasalle Fin. Servs., Inc., No. 17-01201, 2018 WL 1452616, at *2 (Mar. 16, 2018) (Murphy, Arb.) ("The Arbitrator postponed the expungement hearing due to inadequate notice.").

189. *Id.*

190. EXPUNGEMENT TRAINING, *supra* note 156, at 14.

a customer to receive notice remains undefined.[191] This also contrasts with the law for class action settlement approvals which require notice to be sent to important stakeholders both within 10 days after any proposed settlement is filed and at least 90 days before a court can grant approval.[192] Notice norms in expungement cases fall far short of the usual sixty-day period under the federal rules for a defendant to respond to a complaint after waiving service or for a defendant to respond to a statement of claim within the FINRA arbitration forum.[193]

c. Vague and Discouraging Notice Language

Neither FINRA's expungement guidance nor its arbitrator training materials require the notice to be provided in any particular form, leaving self-interested parties free to craft notice language in ways seemingly calculated to suppress customer participation. For example, consider the notice language used in one letter sent to notify a customer of about an expungement hearing.[194] The letter opens with legalese, stating that "[p]ursuant to FINRA's Published Guidance, 'Notice to Arbitrators and Parties on Expanded Expungement Guidance,' we are notifying you that a request for customer dispute expungement relief has been filed in the aforementioned case."[195] The letter seems calculated to discourage, stating that "[y]ou are not a party to this case and are under no duty or obligation to answer, respond, participate or engage in any manner."[196] Although the letter does reveal the date and time of the hearing, it does not tell the recipient where it is or how to

191. *See, e.g.*, FIN., INDUS. REG. AUTH., RULE 13503(a)(3) (2017) ("Written motions must be served at least 20 days before a scheduled hearing, unless the panel decides otherwise.").

192. 28 U.S.C. § 1715(b), (d) (2018).

193. *See* FED. R. CIV. P. 4(d)(3) ("A defendant who, before being served with process, timely returns a waiver need not serve an answer to the complaint until 60 days after the request was sent—or until 90 days after it was sent to the defendant outside any judicial district of the United States.").

194. Letter from Dochtor D. Kennedy, President & Founder, Advisor Law, LLC to Dan Tennent, Dec. 31, 2018 (on file with the Washington and Lee Law Review).

195. *Id.*

196. *Id.*

actually participate in these primarily telephonic hearings.[197] A motivated, proactive customer would have to take additional steps to gather more information in order to participate.

Importantly, customer participation provides extraordinary value to an arbitration panel considering an expungement request. When a customer does not participate, an arbitration panel will often receive no evidence to contradict a broker's testimony.[198] A notice seemingly calculated to discourage their participation increases the likelihood that an arbitrator will later render a poorly informed decision.[199]

4. Unclear Standards of Proof

Identifying how these grounds should be interpreted or what standard of proof an arbitrator should apply in reviewing an expungement request remains difficult. Arbitrator training materials do not contain any reference to common standards of proof such as by a "preponderance" of the evidence, by "clear and convincing" evidence, or "beyond a reasonable doubt."[200] One arbitrator concluded that the standard surely must be higher than a preponderance of the evidence because FINRA does not remove a customer complaint if the customer does not prevail in arbitration under an ordinary preponderance standard of civil proof.[201] The arbitrator recognized that if an "allegation is supported by some reasonable proof, even short of 'preponderance,' it cannot be said to be 'false.' Unfortunately,

197. *Id.*

198. *See, e.g.*, Royal All. Assocs., Inc. v. Liebhaber, 206 Cal. Rptr. 3d 805, 813 (Cal. Ct. App. 2016) ("[N]o evidence was presented or information not disputed [*sic*] because the arbitrators did not allow Ms. Liebhaber to present any evidence at the hearing despite her appearance and multiple requests to do so.").

199. *See id.* (describing how the arbitrators prevented the client from presenting evidence at the hearing).

200. EXPUNGEMENT TRAINING, *supra* note 156.

201. *See* Gilliam v. Sagepoint Fin., Inc., No. 12-03717, 2013 WL 3963949, at *2 (July 22, 2013) (Meyer, Arb.) (reasoning that when a customer claimant loses an ordinary arbitration, the customer "failed to prove his/her case by a preponderance of the evidence . . . the allegations nevertheless appear on the respondents' CRD records . . . . From this it may be inferred that to expunge . . . something more than a preponderance of the evidence is required").

too many decisions improperly label 'false' claims simply because they were not supported by a preponderance of the evidence."[202]

Despite this reasoning, most arbitrators seemingly apply a preponderance standard to recommend expunging significant information after a quick, one-sided hearing where only the broker seeking expungement presents any evidence.[203] Consider a recent arbitration award recommending the expungement of twelve different items from the CRD for two brokers.[204] The two brokers brought an arbitration against Geneos Wealth Management, Inc., which "did not appear at the expungement hearing and did not contest the expungement requests."[205] The arbitrator found that "the Customers were served with the Statement of Claim and received notice of the expungement hearing" at some unspecified date before the hearing.[206] At a hearing where only the brokers appeared, the arbitrator found that "preponderance of the evidence adduced at the expungement hearing" supported a series of factual findings.[207] Altogether, the brokers successfully erased "five FINRA arbitration cases, [one] civil court case and two customer complaints" from the CRD.[208] The arbitrator reached this conclusion after just a single hearing session on the expungement requests which lasted four hours or less.[209]

Importantly, the arbitration systems seem unlikely to ever definitively resolve this standard of proof issue or meaningfully engage with arbitration decisions which do address the issue. Arbitrations do not create any binding precedent and a

202. *Id.* at *3.

203. *See, e.g.*, *Royal All. Assocs., Inc.*, 206 Cal. Rptr. 3d at 813 (discussing the one-sided evidence presented at the hearing).

204. Arford v. Geneos Wealth Mgmt., Inc., No. 19-00739, 2019 WL 5681728, at *1 (Oct. 24, 2019) (Cutler, Arb.).

205. *Id.* at *2.

206. *Id.*

207. *Id.*

208. *Id.*

209. *Id.* at *7. Within FINRA's arbitration system, a "hearing session is any meeting between the parties and arbitrator(s) of four hours or less." *Summary of Arbitration Fees*, FIN. INDUS. REG. AUTH., https://perma.cc/7DA4-7EMY.

thoughtful resolution of the standard of proof issue by one arbitrator will not bind another.[210] Parties to arbitrations do not even need to inform the arbitration panel about arbitration decisions interpreting the grounds because they are not legal authority.[211] Although arbitration remains an "equitable" forum, the arbitrators may only seek to do equity between the named or appearing parties and not to the silent stakeholders who do not appear in the proceeding.[212]

5. Limited Rights for Customers to Participate

FINRA Rules do not contain any provisions explicitly providing for a right for customers to participate in expungement hearings before information about their disputes are erased from the public record. Instead, FINRA provides guidance to arbitrators and instructs them to allow customers to participate in expungement hearings. In guidance, FINRA notifies arbitrators that it is "important to allow customers and their counsel to participate in the expungement hearing in settled cases if they wish to."[213] The guidance instructs arbitrators that they should allow customers to appear with counsel, testify, introduce documents and evidence, cross-examine witnesses, and "present opening and closing arguments if the panel allows any party to present such arguments."[214]

FINRA issued the guidance after arbitrators in its forum declined to allow a customer's counsel to cross-examine a broker

210. *See* Edwards, *supra* note 43, at 434 (pointing out that arbitration "cannot 'answer' these questions in any meaningful way because their decisions do not create precedent").

211. *See* MODEL RULES OF PROF'L CONDUCT r. 3.3 (AM. BAR ASS'N 2020) (requiring a lawyer to inform a tribunal about controlling legal authority).

212. *Cf.* Barbara Black & Jill I. Gross, *Making It Up As They Go Along: The Role of Law in Securities Arbitration*, 23 CARDOZO L. REV. 991, 1029–30 (2002) ("Arbitrators are expected to achieve an equitable resolution of the dispute before them but they may not ignore the law. However, without ample training or legal briefing by the parties on each relevant issue, how can the arbitrators know what the law is or how to apply it?").

213. *Notice to Arbitrators and Parties on Expanded Expungement Guidance*, FIN. INDUS. REG. AUTH. (Sept. 2017), https://perma.cc/542Y-UNSN.

214. *Id.*

who testified in favor of her own expungement request.[215] In this case, the customer claimant had already settled in part because the arbitration panel would not require the brokerage firm to provide discovery or allow her to present any oral argument on motions.[216] In this instance, the customer had clear notice because the expungement hearing occurred within the customer-initiated arbitration and the customer remained a named party to the arbitration.[217] The broker, Kathleen J. Tarr, gave an unsworn monologue that the allegations were "highly offensive and without basis in any fact" and that she was "the daughter and granddaughter of ministers."[218] When counsel for the customer sought to introduce the customer's contrary testimony and to question Tarr, the arbitration panel's chairperson stated that he did not "see that any testimony such as this is necessary."[219] When another arbitrator suggested hearing the customer out to generate a complete record, the chair responded "how can we make sure we're not going to be here for another two hours? That's the problem."[220] Ultimately, the three-arbitrator panel declined to allow the customer or counsel to fully participate and unanimously recommended expungement anyway.[221] Surprisingly, despite the protests of

215. *See* Robert S. Banks, Jr., *Muzzling the Claimant Due Process Denied in FINRA Expungement Hearing*, 21 PIABA B.J. 397, 397 (2014) (describing a FINRA expungement hearing where a customer and counsel were not permitted to fully participate).

216. *Id.* at 397 (describing a client who settled an action after an arbitration panel chair "refused to allow oral argument on any of our motions and refused to refer our motions to the full panel").

217. Notably, brokers do not have to seek an expungement in the same action. Many wait to name their employers in a subsequent action.

218. Banks, *supra* note 215, at 398.

219. *Id.*

220. *Id.*

221. *See* Liebhaber v. Royal Alliance Assocs., Inc., No. 13-01522, 2014 WL 4647001, at *2 (Sept. 10, 2014) (Stall, Jr., McLaughlin, & Aragon, Arbs.) ("Panel recommends the expungement of all references to the above-captioned arbitration from non-party Kathleen Tarr's (CRD #4215307) registration records maintained by the CRD.").

the customer's counsel, not one of the arbitrators dissented from the decision.[222]

With the assistance of pro bono counsel, the customer sought to vacate the arbitration award.[223] In *Royal Alliance Associates, Inc. v. Liebhaber*,[224] the customer explained that she had a real interest in the expungement proceeding "because the award deemed her complaints against Tarr false and therefore found her 'essentially to have been a liar without anyone hearing from her or giving her a right to cross-examine'" Tarr.[225] With FINRA also opposing confirmation, the award was ultimately vacated because the arbitrators refused to hear evidence from a party to the arbitration.[226]

FINRA's current guidance and training materials seem designed to address the specific problems that arose in the *Royal Alliance* arbitration.[227] It instructs arbitrators to permit customers to do the specific things the customer was not allowed to do in *Royal Alliance*, including appearing, presenting testimony, and cross-examining any witnesses.

The guidance fails to address the many instances where a broker brings a separate expungement action to which the customer is not a party. The guidance does not facilitate full participation. Although FINRA's guidance calls for arbitrators to require brokers to provide notice and a copy of their statement of claim when seeking an expungement, it does not generally call for customers to have copies of everything that

222. As discussed below, arbitrators may decline to oppose expungement requests because they fear they will not be selected for future panels if they do. *See supra* Part II.C.1.e.

223. *See* Banks, *supra* note 215, at 400 (explaining that the customer "filed an opposition to the confirmation petition and a request that the Award be vacated, with generous assistance from . . . pro bono counsel").

224. 206 Cal. Rptr. 3d 805 (Cal. Ct. App. 2016).

225. *Id.* at 814.

226. *Id.* at 1110 ("[A]rbitrators gave Royal Alliance an unfettered opportunity to bolster the written record but denied Liebhaber even a limited chance to do the same.").

227. *See Notice to Arbitrators and Parties on Expanded Expungement Guidance*, FIN. INDUS. REG. AUTH., https://perma.cc/PR8L-BDAN (last updated Sept. 2017) ("It is important to allow customers and their counsel to participate in the expungement hearing in settled cases if they wish to.").

has been submitted to the arbitrators.[228] As a result, customers cannot see any answer that has been filed, participate in arbitrator selection, readily view all other documents which have been submitted, or even know what the arbitration panel has been told about them in earlier hearings in the matter. This puts the customers who do participate at a substantial disadvantage in the matter.

Thus, even an unusually savvy customer who opted to participate in expungement hearings where she was not a party will struggle to oppose confirmation of any arbitration award. Even after expending the time and effort necessary to oppose an arbitration award, a customer will not receive notice of any award when FINRA delivers it to the parties.[229] The customer must search FINRA's arbitration database to find out the result.[230]

The customer also receives no notice of the next step—confirmation of the arbitration award in court. As the customer was not a party to the arbitration, the customer will not receive notice when a party seeks to confirm the arbitration award.[231] This makes it practically impossible for customers to block confirmation.

6. No Independent Investigation in Arbitration

Facilitating expungements through arbitrations also largely prevents any independent fact-finding into the underlying disputes. FINRA's training materials for arbitrators instruct that arbitrators "should not make independent factual

228. *See* EXPUNGEMENT TRAINING, *supra* note 156, at 14 ("[N]otice provides the customer(s) with the opportunity to advise the arbitrators and parties of their position on the expungement request, which may assist arbitrators in making the appropriate finding.").

229. *See Decision & Award*, FIN. INDUS. REG. AUTH., https://perma.cc/QEP4-LDAR ("Once the award is signed by a majority of the arbitrators, FINRA will send copies of the award to each party or representative of the party.").

230. *See id.* ("FINRA makes all arbitration awards publicly available for free by posting them on Arbitration Awards Online.").

231. *See id.* (explaining the confirmation process).

investigations of a case."[232] Although FINRA encourages arbitrators to ask questions of the parties and for the parties to provide any briefing requested by the arbitrator, its guidance makes clear that arbitrators "generally should review only those materials presented by the parties."[233]

A rule against any independent investigation makes the most sense when purely private parties with equal resources have contracted for an arbitrator to decide a dispute. It makes less sense when it puts public information at risk and forces arbitrators to refrain from conducting even the most rudimentary of independent investigations.

D. Past Problems

The incentives and processes detailed above have left FINRA continually struggling to manage the arbitration-facilitated expungement process. As explained below, FINRA has moved to address some past problems, yet resolving these concerns has not substantially improved the process.

1. Stipulated Expungements after Settlements

For years, brokers secured expungements through stipulated awards agreed to as part of a settlement process.[234] In explaining the operation of NASD Rule 2130, an earlier version of FINRA Rule 2080, FINRA explained how brokers could procure a stipulated award containing the findings necessary to have information about the dispute expunged from

232. FIN. INDUS. REG. AUTH., FINRA DISPUTE RESOLUTION SERVICES ARBITRATOR'S GUIDE 60 (2020), https://perma.cc/9DR9-49CC (PDF).

233. *Id.*

234. *See* Christine Lazaro, *Has Expungement Broken Brokercheck?*, 14 J. BUS. & SEC. L. 125, 136 (2014) ("[P]arties would place a stipulated award before the arbitrators containing an expungement directive, which the arbitrators would then sign. The broker would then confirm the award in a court of competent jurisdiction either with the consent of the customer or by default if the customer did not appear.").

public records.[235] The process was straightforward. Settling parties simply asked the arbitration panel "for a stipulated award and request[ed] that the panel make affirmative findings and order expungement based on one or more of the standards in Rule 2130."[236] After Rule 2130 came into effect, FINRA noted that arbitrators would still state in the award the basis on which the expungement relief was granted."[237]

Stipulated awards sat in tension with the rule's requirement that an expungement recommendation be "based on affirmative judicial or arbitral findings."[238] FINRA's guidance on stipulated expungement awards did not direct arbitrators to make any searching inquiry to protect the public's interest in the accuracy and reliability of CRD information. After all, an arbitrator ordinarily sits to resolve a private dispute, not to play some public enforcement role. One scholar explained that the "message in the Notice is that the arbitrators' role is to execute the request for expungement rather than conduct an independent, skeptical review."[239] Notably, the SEC never directly addressed stipulated awards in its order approving NASD Rule 2130.[240]

But concerns about stipulated awards and the risk that brokers would force customers to agree to expungement as a settlement condition had been raised. One prescient commenter argued that a "broker should not be allowed to purchase a clean CRD from a destitute customer. This is especially true when the

235. Nat. Ass'n Secs. Dealers, Notice to Members 04-16 Expungement of Customer Dispute Information from the CRD 214 (March 2004), https://perma.cc/E7HJ-5NHW (PDF). FINRA was known as the National Association of Securities Dealers (NASD) until 2007, when it became FINRA.

236. *Id.*

237. *Id.*

238. *Id.*

239. Lipner, *supra* note 91, at 76.

240. *See* Order Granting Approval and Notice of Filing and Order Granting Accelerated Approval Relating to Proposed NASD Rule 2130 Concerning the Expungement of Customer Dispute Information from the Central Registration Depository System, 68 Fed. Reg. 74,667, 74,667 (Dec. 24, 2003) (discussing requirements for obtaining an order of expungement of customer dispute information from the central registration depository).

broker is the reason the customer is destitute."[241] The commenter also panned judicial confirmation as a "phony safeguard" because customers were not likely to appear at confirmation hearings and they would be granted "without independent review unless the NASD objects."[242]

Over time, stipulated awards facilitating the expungement of information likely did real harm to the public by enabling fraud and misconduct to go undetected. Consider the aftermath of one stipulated expungement. Carl Martellaro served as a principal for First Associated Securities Group, a firm FINRA expelled from the securities industry in the year 2000.[243] Years before FINRA discovered wrongdoing and expelled the firm, two investors alleged that Martellaro had run a fraudulent scheme causing them to lose $1.75 million.[244] Martellaro settled the dispute on the condition that the investors would not oppose his subsequent request to expunge information about their complaint from public records.[245] He succeeded and later went on to run a Ponzi scheme causing other investors to suffer $125 million in losses.[246] The attorney who represented the first two investors explained that although his clients "cut a deal, . . . the public got cut out."[247]

These deals left only a faint trace behind. A search of arbitration awards reveals that Martellaro successfully expunged at least two disputes from his record before his Ponzi scheme ultimately collapsed. In 1999, an arbitration award directed that a dispute alleging $1.25 million in damages be

241. Letter from Barry D. Estell to Sec. & Exch. Comm'n (Mar. 28, 2003) (arguing that an "agreement to expunge an arbitration claim is inherently corrupt and contrary to the purpose of the CRD") (on file with the Washington and Lee Law Review).

242. *Id.*

243. *First Associated Securities Group, Inc.*, BROKERCHECK, https://perma.cc/5KYC-Y6F6.

244. Michael Freedman, *The X-ed Out Files*, FORBES (Dec. 25, 2000, 12:00 AM), https://perma.cc/23HN-9D3F.

245. *Id.*

246. *Id.*

247. *Id.*

expunged.[248] In the same year, arbitrators also directed that another claim alleging $500,000 in damages be expunged.[249] On both occasions, the parties secured a stipulated award calling for the information to be expunged.[250]

In Martellaro's case, the expungement of dispute information likely facilitated his ongoing fraud. Investors doing ordinary diligence would not see complaint information on his record. Regulators surveying the CRD records for red flags involving brokers operating within their territory would also not have seen the information.

State regulators eventually intervened to oppose the confirmation of some stipulated awards with mixed success.[251] In 2007, Maryland sought to block the confirmation of a stipulated expungement award, arguing that the Maryland Securities Commissioner "has a substantial interest in ensuring the integrity of her records."[252] The customer had collected a $47,000 settlement on the condition that she stipulate to the expungement of all reference to the dispute.[253] After the district court initially rejected Maryland's request to intervene, the D.C. Circuit found that the state regulator should be allowed to intervene as of right because Maryland had an interest in protecting its records and neither the broker nor the customer

248. Drake v. First Associated Sec. Grp., No. 95-03869, 1999 WL 1253565, at * (Jan. 15, 1999) (Bardack, Krotinger, & Mainardi, Arbs.).

249. *See* Bann v. First Associated Sec. Grp., No. 96-04601, 1999 WL 1253604, at *3 (Jan. 15, 1999) (Gault, Goldberg, & McClaskey, Arbs.) ("The NASD shall expunge from its Central Registration Depository (CRD) records maintained for stipulating Respondents Carl Martellaro, Larry Miller, Jay Dugan and First Securities USA, all references to this claim.").

250. In 2014, FINRA prohibited member firms from conditioning any settlement offer on a customer agreeing not to oppose the expungement of complaint information. Fin. Indus. Reg. Auth., Notice to Members 14-31 Expungement of Customer Dispute Information 4 (July 2014), https://perma.cc/3R5A-B2N9 (PDF).

251. *See* Lazaro, *supra* note 234, at 139–46 (describing state efforts to intervene to stop courts from confirming awards recommending expungement).

252. Karsner v. Lothian, 532 F.3d 876, 879 (D.C. Cir. 2008).

253. *Id.* at 881.

"represents the Commissioner's interest in protecting the integrity of the CRD."[254]

States still struggled to block the confirmation of stipulated awards. Some courts confirmed expungement awards over state opposition.[255] For example, New York unsuccessfully sought to intervene and oppose an expungement arising out of a stipulated award in *Kay v. Abrams*.[256] There, the broker had paid $155,000 to secure a stipulated award providing "for confidentiality and expungement of the matter from CRD records."[257] The court confirmed the award because it felt bound by precedent that it lacked authority to set aside the award because a New York appellate court had reversed a prior trial court for refusing to confirm an expungement.[258] Generally, New York's attempts to intervene were unsuccessful because the New York courts generally "viewed their role in the expungement controversy as highly limited, rejecting the policy arguments made by the Attorney General."[259]

Still, the efforts brought attention to significant concerns with how arbitration rules facilitated expungement. One court highlighted real issues with the stipulated award process by focusing on the award before her.[260] The court explained that

254. *Id.* at 885–86.

255. *See, e.g.*,. Walker v. Connelly, 21 Misc. 3d 1123(A), at *2 (N.Y. Sup. Ct. Oct. 16, 2008) ("The Attorney General opposes confirmation of the stipulated award pursuant to CPLR 7511(b) on the grounds that the panel 'exceeded its authority.'").

256. *See* 853 N.Y.S.2d 862, 867 (Sup. Ct. 2008) ("[S]ince no basis has been alleged to deny confirmation, other than the legal arguments of the Attorney General referred to above, petitioner's motion to confirm the Award is granted. In light of the foregoing, the application of the Attorney General to intervene is denied.").

257. *Id.* at 863.

258. *Id.* at 866–67 (citing Goldstein v. Preisler, 805 N.Y.S.2d 647 (App. Div. 2005)) ("Although the then Attorney General did not seek to intervene in that case, since it is on 'all fours' with the case at bar and there is no contrary First Department decision, the court feels bound by the determination therein.").

259. Lipner, *supra* note 91, at 80.

260. *See In re* Sage, Rutty, & Co. v. Salzberg, No. 2007-01942, slip op. at 4–5 (N.Y. Sup. Ct. June 1, 2007) (order granting partial rehearing) (remarking that "[a] hearing was never conducted, no written settlement agreement was

"there are aspects of the [s]tipulated [a]ward which trouble the [c]ourt. The arbitrators found that (certain) claims were factually impossible or clearly erroneous, but there is not a single fact or circumstance described upon which the arbitrators base this conclusion."[261]

Concerns about an arbitration-facilitated expungement process grew. One review of 200 stipulated or settled arbitration awards in 2006 found arbitrators regularly granted expungement without conducting any affirmative fact finding.[262] On the whole, arbitrators granted expungement requests after settlements 98% of the time.[263] The arbitrators conducted no fact-based hearings 71% of the time.[264] The troubling statistics revealed that decisions to expunge information from public records were being made without fully informed arbitrators. As one law professor noted, arbitrators were not considering "the larger policy implications and considerations associated with an effective CRD system."[265] In many cases, arbitrators were simply ordering "expungement at the request of a party to facilitate settlement of a dispute."[266]

After some negative publicity, FINRA moved in 2008 to make changes to its code. It added Rules 12805 and 13805 to require arbitrators to hold at least one hearing session and

ever drafted, and no other documents were submitted. In that sense, the arbitrators' decision on expungement is irrational because it was made without any evidentiary support").

261. *Id.* at 4.

262. *See* PUB. INV'RS ARB. BAR ASS'N, STUDY OF STIPULATED OR SETTLED NASD CUSTOMER AWARDS, ISSUED IN CALENDAR YEAR 2006, FOR WHICH STATEMENTS OF CLAIM WERE FILED ON, OR SUBSEQUENT TO, APRIL 12, 2004, 14 (2007), https://perma.cc/A7A3-NZNN (PDF) (reviewing these awards).

263. *Id.*

264. *Id.*

265. Letter from Barbara Black, Charles Hartsock Professor of Law, Dir. of Corp. Law Ctr., Univ. of Cincinnati, to Nancy M. Morris, Sec'y, Sec. & Exch. Comm'n 2 (Apr. 24, 2008), https://perma.cc/R734-LLB3 (PDF).

266. Order Approving a Proposed Rule Change Amending the Codes of Arbitration Procedure to Establish Procedures for Arbitrators to Follow When Considering Requests for Expungement Relief, 73 Fed. Reg. 66,086, 66,087 (Nov. 6, 2008).

explain the basis for their expungement recommendations.[267] These new rules effectively ended stipulated awards but left the underlying incentives unchanged.

2. Purchasing Perjury & Silence

Brokers had also found other ways to ensure that arbitration panels would approve requests for expungements. Brokers ensured one-sided expungement hearings and evidence by conditioning settlement offers on a customer either agreeing to support an expungement with a sworn affidavit saying the underlying complaint was false, or at least an agreement not to oppose a broker's request.[268] FINRA took repeated steps to address the issue. In 2004, FINRA warned industry members that "affidavits, attested to in connection with settlements that often are incorporated into stipulated awards, appear to be inconsistent on their face with the initial claim and terms of the settlement."[269] FINRA explained that members may face discipline if they submitted "affidavits in which the content is the product of a bargained-for consideration as opposed to the truth."[270] Obtaining expungements with bargained-for evidence undercut the requirement that arbitrators have some

267. *See* Notice of Filing of Proposed Rule Change Relating to Amendments to the Codes of Arbitration Procedure to Establish New Procedures for Arbitrators to Follow When Considering Requests for Expungement Relief, Fed. Reg. 18,308, 18,308 (Apr. 3, 2008) ("The procedures are designed to: (1) make sure that arbitrators have the opportunity to consider the facts that support or weigh against a decision to grant expungement; and (2) ensure that expungement occurs only when the arbitrators find and document one of the narrow grounds specified in Rule 2130.").

268. *See* Melanie S. Cherdack, *Drafting A Securities Arbitration Claim: The Pen Is (Still) Mightier Than the Market*, 18 PIABA B.J. 333, 342 (2011) (explaining that for claimant's counsel "[n]aming the individual broker may have benefits, too . . . . If, for instance, the broker is a big producer and important to the firm, the firm may have some incentive to settle the action and seek your client's cooperation . . . .").

269. *See* Nat. Ass'n Secs. Dealers, Notice to Members 04-43 Members' Use of Affidavits in Connection with Stipulated Awards and Settlements to Obtain Expungement of Customer Dispute Information 554 (June 2004), https://perma.cc/2H7C-F7M6 (PDF) (warning against procuring false affidavits).

270. *Id.*

affirmative basis for recommending an expungement.[271] In effect, the practice of requiring customers to swear to affidavits attesting that their initial claim was "false" may have amounted to purchasing perjury.

Despite the warning, brokers continued to negotiate for customers to assist with, or at least not oppose, their expungement requests as a settlement condition until 2014 when FINRA updated its rules to prohibit the practice. [272] In adopting the rule, FINRA explained that it believed the new rule would "ensure that information is expunged from the CRD system only when there is an independent judicial or arbitral decision that expungement is appropriate"[273]

As often happens, new problems arise after regulators address old ones.[274] The NASD prohibited the use of affidavits in 2004, ended stipulated awards in 2008, and explicitly prohibited negotiations over nonparticipation in expungements in 2014.[275] In response to these changes, many brokers began to seek expungements in separate arbitrations naming their current or former employers as respondents. A report from the PIABA Foundation found that there has been an "explosive

271. *See* Scott Ilgenfritz, *Expungement Study of the Public Investors Arbitration Bar Association*, 20 PIABA B.J. 339, 349 (2013) ("Bargaining for such an affidavit from a customer claimant could clearly result in the 'buying of a clean record' and would make a mockery of any 'affirmative determination' of one of the three grounds in Rule 2130 by a panel of arbitrators.").

272. *See* FIN. INDUS. REG. AUTH., RULE 2081 (2014) (prohibiting brokers and firms from conditioning "settlement of a dispute with a customer on, or to otherwise compensate the customer for, the customer's agreement to consent to, or not to oppose, the member's or associated person's request to expunge such customer dispute information from the CRD system").

273. Fin. Indus. Reg. Auth., Regulatory Notice 14–31 Expungement of Customer Dispute Information 2 (July 2014), https://perma.cc/Q4MN-2S2Q (PDF).

274. *See* Jeffrey N. Gordon, *The Empty Call for Benefit-Cost Analysis in Financial Regulation*, 43 J. LEGAL STUD. S351, S351 (2014) (explaining that in the "financial sector, however, the system that generates costs and benefits is constructed by financial regulation itself and the subsequent processes of adaptation and regulatory arbitrage. An important new rule will change the system beyond our calculative powers").

275. *See* FIN. INDUS. REG. AUTH., RULE 2081 (2014) ("Rule 2081 removes the ability of parties to a customer arbitration to bargain for expungement relief as part of a settlement negotiation.").

increase" in these "expungement-only" arbitrations, rising 924% from 2015 to 2018.[276]

E. Uninformed Decisions

Ultimately, the current system for arbitration-facilitated expungements reveals that arbitrations now regularly occur where no party has any real incentive to bring pertinent, material information to the attention of arbitrators if that information would diminish the odds that an arbitrator will grant an expungement request. Courts asked to confirm these arbitration awards should not have any confidence that the arbitrators made a well-informed decision. Although the arbitrators may hear all the evidence presented to them, they usually hear no more than what the broker seeking an expungement wants them to hear.

Consider an arbitration award directing expungement obtained by Patrick James Dwyer, a broker who once managed billions of dollars in assets.[277] Dwyer secured an arbitration award recommending the expungement of six different customer complaints in two hearing sessions conducted on the same day. [278] His employer, Merrill Lynch, did not oppose the expungement request and indicated that it "agreed that a finding should be entered by the Panel in favor of" the expungement request.[279] Of the six complaining customers, only three of them received any form of notice.[280] Dwyer's counsel took the position "that the notification requirements of an

276. DOSS & BRAGANÇA, *supra* note 88**Error! Bookmark not defined.**, at 3.

277. *See* Braswell & Horowitz, *supra* note 147 (reporting that Dwyer "led a 12-person team that managed some $3.7 billion and generated over $10 million of annual revenue, left this week while under review").

278. *See In re* Dwyer v. Merrill Lynch, Pierce, Fenner & Smith Inc., No. 16-02781, 2017 WL 3189311, at *6 (July 20, 2017) (Ainbinder, Arb.) (noting that Plaintiff's requested relief was the expungement of all records of these occurrences).

279. *Id.* at *1.

280. *See id.* ("Claimant provided notice of this proceeding to the only customer who filed for arbitration . . . . Claimant also provided notice to two other customers and they or their counsel gave written authority to not oppose nor support Claimant's request for expungement . . . .").

expungement request applies to customers who have filed for arbitration."[281] Because some of the complaining customers had never filed an arbitration complaint against Dwyer, he did not notify them of the expungement hearing at all.[282] Hearing no objections from customers, some of whom had not even been told about the hearing, the arbitration panel agreed.[283] The panel noted as significant the fact that his employer supported the request.[284] The panel trusted Merrill Lynch to faithfully defend the integrity of the CRD because Merrill Lynch, as Dwyer's employer, also had "a duty to protect the investing public and the firm's customers from improper, fraudulent or otherwise culpable conduct."[285]

But the arbitration panel did not hear the complete story. FINRA sought to vacate the award in a Florida state court, contending that Dwyer had fraudulently concealed information from the arbitration panel and exhibited an "extreme lack of candor" in the arbitration proceeding.[286] Dwyer, a Miami-based broker, had previously filed an action against FINRA in a California court seeking to force FINRA to expunge information from the CRD.[287] Although his name eventually emerged as the broker behind the request, Dwyer had filed his California suit under a pseudonym. He may have sought relief in court first under the pseudonym to avoid the publicity that would follow

281. *See id.* ("Claimant's counsel advised the Panel that it was his position that the notification requirements of an expungement request applies to customers who have filed for arbitration. The Panel agrees with Claimant's counsel's position.").

282. *See id.* (noting that despite the fact that only one customer had filed an arbitration, Dwyer's counsel represented that he had secured some written statement of some kind from two other complaining customers that they would not oppose the expungement request).

283. *See id* at *2 (recommending expungement).

284. *See id.* ("Critical facts regarding the Focus 20 Fund were not contradicted by Respondent's representative.").

285. *Id.*

286. Fin. Indus. Reg. Auth., Inc. v. Dwyer, No. 2017-023398-CA-01 (Fla. 11th Cir. Ct. 2017), Dkt. 3., at ¶¶ 9–10.

287. *See id.*, at Exhibit B (filing under the pseudonym John Doe).

when a broker with his multibillion-dollar book of business won an expungement.[288]

Yet once Dwyer named FINRA as a defendant in a court action, FINRA contested the case and won, securing a post-trial decision denying Dwyer's request to have information expunged from the CRD database.[289] After adversarial litigation, the California court found that Dwyer "presented no evidence to show that any of these complaints are false, inaccurate, meritless or frivolous" and that the "disclosure of accurate customer dispute information is most definitely in the public interest."[290] The California court concluded that the "equities weigh heavily against expungement of Plaintiff Dwyer's record."[291] The California court was presented with evidence and information that Dwyer, Dwyer's counsel, and Merrill Lynch declined to provide to the arbitration panel.

Ultimately, the Florida court considering vacating the arbitration award recommending expungement never ruled on the propriety of Dwyer's behavior. On November 15, 2018, the parties presented the court with a joint stipulation of dismissal.[292] It stipulated that Dwyer's Petition to Confirm the Arbitration Award was "dismissed with prejudice."[293] Thus, FINRA succeeded at keeping the customer dispute information on the CRD system.

Dwyer may have failed in his expungement attempt because he went to court first and faced FINRA as an actual adversary. If he had proceeded through arbitration first against his employer, FINRA likely would not have sought to block the confirmation of Dwyer's award—or had a clear ground to do so.

288. *See*, *e.g.*, *Star Merrill PBIG Broker Sweeps His Record Nearly Clean*, ADVISORHUB (July 21, 2017), https://perma.cc/HN22-L722 (reporting on Dwyer's expungement award).

289. *See* Fin. Indus. Reg. Auth., Inc. v. Dwyer, No. 2017-023398-CA-01 (Fla. 11th Cir. Ct. 2017), Exhibit B, at 28 ("This is not a close case. The equities weigh heavily against expungement of Plaintiff Dwyer's record.").

290. *Id.* at 27–28.

291. *Id.* at 28.

292. *See* Fin. Indus. Reg. Auth., Inc. v. Dwyer, No. 2017-023398-CA-01 (Fla. 11th Cir. Ct. 2017), Dkt. 56 (stipulating to a dismissal with prejudice of Dwyer's petition to confirm the arbitration award).

293. *Id.*

Under Rule 2080, FINRA must be named as a defendant in court actions unless FINRA waives the requirements under Rule 2080.[294] If Dwyer had obtained affirmative arbitral findings first, FINRA might have waived the requirement to name it as a party or chosen not to contest the expungement because no strong rationale for opposing the individual arbitration award seems readily apparent. The process effectively leaves it up to the parties and the rare customer to present arbitrators with pertinent, material facts.

III. Interventions

Some interventions may address, or at least mitigate adversarial failure. The best solution, discussed in the next subpart, would be to simply remove expungement and other matters with a high degree of adversarial failure from adversarial systems entirely. Absent that, process-oriented changes and ethics-focused interventions might address the issue to some degree.

Ultimately, adversarial failure occurs whenever the parties to an action have no real incentive to present information to an adjudicator. In these situations, courts, regulators, and legislators should not assume that an adjudicator made an informed decision because no party had any real incentive to present the adjudicator with complete information. Adversarial failure may often be a matter of degree. In some instances, a disparity of resources or advocate skill and diligence may generate the same results.

A. Moving Away from Adversarial Adjudication

In most instances, it may be better to simply abandon adversarial adjudication in favor of some alternative approach. Barbara Black suggested this type of shift in 2008, explaining that "the integrity of the CRD is such an important and integral part of an effective investor education and protection system that only the regulators whose responsibilities include, first and

294. *See* FIN. INDUS. REG. AUTH., RULE 2080 (2009) ("Members or associated persons petitioning a court for expungement relief . . . must name FINRA as an additional party . . . unless this requirement is waived.").

foremost, protection of the investing public should make decisions about removing information from the record."[295] Black also recognized that arbitration may be particularly ill-suited to this task because the "arbitrators' mission . . . does not include consideration of the larger policy implications and considerations associated with an effective CRD system."[296]

For expungement processes, the interests of all stakeholders may be better balanced by removing the entire process from an adversarial system. When the parties to an action do not have real incentives to fully inform an adjudicator, society should not resolve issues by routing them through a phony adversarial process and then roping courts in to confirm the results.

Gaming regulation may provide a rough, workable model for effectively policing the CRD system's integrity. Consider how Nevada approaches gaming licenses. Lawyers and enrolled agents who practice before the Nevada gaming regulators operate within a demanding regulatory framework. When a lawyer appears on a client's behalf before the Nevada Gaming and Control Board, "the person represented [is] deemed to have waived all privileges with respect to any information in the possession of such attorney."[297] The gaming regulators also require attorneys practicing before them to be expansively candid, explaining that they "shall not be intentionally untruthful to the board or commission, nor withhold from the board or commission any information which the board or commission is entitled to receive."[298] These obligations also include a duty to investigate before appearing and instruct that attorneys appearing before gaming regulators "shall exercise due diligence in preparing or assisting in the preparation of documents for submission to the board or commission."[299] The regulations place continuing obligations on attorneys appearing

295. Black, *supra* note 265, at 2.

296. *Id.*

297. NEV. GAMING REG. § 10.080 (2017).

298. *Id.* § 10.090(1).

299. *Id*. § 10.090(2).

before the board to update any information that is "no longer accurate and complete in any material respect."[300]

Gaming regulators make the lawyers appearing before them function as gatekeepers.[301] A lawyer may be banned from practicing before the gaming regulators if she "willfully failed to exercise diligence in the preparation or presentation" materials or "knowingly misrepresented any material fact to the board or commission."[302] In effect, an attorney may lose her right to practice before the regulator if she fails to discover readily available information. Bad faith behavior or simple ineptitude may also result in exclusion.[303]

But the attorneys do not serve as the only gatekeepers. Importantly, gaming regulators do not rely entirely upon these expansive disclosure requirements or expect attorneys and applicants to surface all information on their own. They independently investigate persons who apply for a gaming license and may even bill applicants for the costs incurred in conducting an investigation.[304]

An appropriate gatekeeper model may greatly improve the process. Securities regulators already have substantial familiarity with gatekeeping.[305] The securities laws impose gatekeeping liability on underwriters in an effort to improve the quality of information investors receive.[306] Underwriters put

300. *Id.* § 10.090(3).

301. Professor Coffee defines "gatekeeper" as "a reputational intermediary who provides verification or certification services to investors." John C. Coffee, Jr., *Gatekeeper Failure and Reform: The Challenge of Fashioning Relevant Reforms*, 84 B.U. L. REV. 301, 309 (2004).

302. NEV. GAMING REG. § 10.065(2)(b) (2017).

303. *Id.* § 10.025(2)(d) (allowing exclusion if a person lacks "requisite qualifications or expertise to represent others before the board or commission, lacks character or integrity, or has engaged in unethical or improper conduct").

304. *See id.* § 4.070 ("[T]he Board may require an applicant to pay such supplementary investigative fees and costs as may be determined by the Board.").

305. *See* Frank Partnoy, *Strict Liability for Gatekeepers: A Reply to Professor Coffee*, 84 B.U. L. REV. 365, 367 (2004) ("Professor Coffee and I both support a strict liability regime for gatekeepers, not a negligence regime.").

306. *See* John C. Coffee, Jr., *The Attorney as Gatekeeper: An Agenda for the SEC*, 103 COLUM. L. REV. 1293, 1297 (2003) ("The underwriter in an initial

their capital and reputations on the line when selling securities. In contrast, arbitrators are not well-situated to serve as key gatekeepers here. They face no liability for any failure, and they lack real incentives and tools to gather information necessary to make an informed decision. If anything, a reputation for close scrutiny may reduce the likelihood that an arbitrator will even be selected. Fundamentally, arbitrators should not serve as the key gatekeepers in this context.

A regulatory model for resolving these types of disputes would likely yield better informed decisions. As an independent, self-regulatory organization, FINRA could transition its involvement in the expungement process from passively operating an arbitration forum to a more significant gatekeeping role. Some regulatory process akin to the method Nevada uses to vet applicants for gaming licenses might serve as a rough model for a process through which FINRA could better balance the key interests at stake here, allowing brokers to contest and remove provably false information while protecting the integrity of information within the CRD.

A well-constituted committee could manage this process. A committee could incorporate relevant stakeholders including state securities regulators, investor advocates, and brokerage firms. Channeling all expungement requests through a single committee instead of a rotating cast of arbitrators would allow for a more regularized process to develop. Importantly, the committee would accumulate experience resolving these issues much more rapidly than a broadly dispersed pool of arbitrators. A committee could also hire counsel, investigators, and others to help surface information relevant to the committee's decision. This would allow the committee to avoid total dependence on a requesting party's willingness to provide information.

B. Changes to Attorney Ethics Rules

Professional ethics rules shape how attorneys present information to adjudicators when advocating for their clients. In most states, the ethical rules governing law practice generally

public offering also performs a gatekeeping function, in the sense that its reputation is implicitly pledged and it is expected to perform due diligence services.").

track the ethics rules and policies promulgated by the American Bar Association (ABA).[307] As the lawyers elected to the ABA House of Delegates have obligations to their own clients, the lawyers collaborating to generate these rules "likely have direct financial interest in the rules that they draft."[308]

Our adversarial system of justice implicitly assumes tribunals will reach informed decisions because each side will investigate the matter and bring forward facts relevant to the dispute.[309] In theory, clashing parties will hold each other accountable and point out any errors, allowing adjudicators to reach informed decisions.[310] This idyllic vision does not match reality.[311] As explained below, the current ethics rules grant lawyers broad flexibility to frame factual scenarios in their clients' interest without cluing courts or arbitrators in to all relevant information.

1. Existing Rules Treat Law and Fact Differently

The ABA Model Rules of Professional Conduct treat legal arguments and factual presentations differently, often allowing lawyers to withhold adverse relevant facts from a tribunal as long as they disclose governing law.[312] ABA Model Rule 3.3, which speaks to a lawyer's duty of candor, treats a failure to

307. *See* Renee Newman Knake, *The Legal Monopoly*, 93 WASH. L. REV. 1293, 1298 (2018) ("Most states draw from model ethics rules and policies promulgated by lawyers elected by their peers to the American Bar Association ('ABA') House of Delegates.").

308. *Id.*

309. I use the word "tribunal" here to track the ethics rules and because it also encompasses disputes resolved by an arbitrator.

310. *See* MODEL RULES OF PROF'L CONDUCT preamble [8] (AM. BAR ASS'N 2020) ("When an opposing party is well represented, a lawyer can be a zealous advocate on behalf of a client and at the same time assume that justice is being done.").

311. *See* Daniel Markovits, *Adversary Advocacy and the Authority of Adjudication*, 75 FORDHAM L. REV. 1367, 1369 (2006) (explaining that the general assumption that the adversarial system will on balance generate the best results has "been shown to be not just mistaken but simply implausible. To begin with, its factual predicates do not generally obtain.").

312. *See* RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 111 cmt. c. (AM. LAW. INST. 2000) (pointing out that that "it is sometimes argued that the rule . . . it draws a dubious distinction between legal authority and facts").

disclose pertinent, adverse legal authority differently from a failure to disclose pertinent, adverse facts.[313]

a. Governing Law

ABA Model Rule 3.3(a)(2) prohibits lawyers from knowingly failing to disclose "legal authority in the controlling jurisdiction known to the lawyer to be directly adverse to the position of the client and not disclosed by opposing counsel."[314] The official comment to the rule explains that "[t]he underlying concept is that legal argument is a discussion seeking to determine the legal premises properly applicable to the case."[315] In essence, the ethics rule sometimes requires a lawyer to carry the discussion into legal territory she might prefer to avoid—even if the lawyer on the other side of the case does not raise the precedent.[316]

The expectation that lawyers will not knowingly withhold information about relevant past precedents has long been part of the American legal system.[317] Alabama included requirements to not knowingly cite "as authority an overruled case" or not "knowingly misquoting the language of a decision" in the Alabama Code of Ethics of 1887.[318] The Restatement also embraces this view and makes clear that a lawyer "may not knowingly . . . fail to disclose to the tribunal legal authority in the controlling jurisdiction known to the lawyer to be directly

313. *See* MODEL RULES OF PROF'L CONDUCT r. 3.3 (AM. BAR ASS'N 2020) (distinguishing between the two).

314. *Id.* at (a)(2).

315. *Id.* at cmt. [4].

316. *See* ABA Comm. on Prof'l Ethics & Grievances, Formal Op. 146 (1935) (explaining that a precedent-disclosing lawyer "may, of course, after doing so, challenge the soundness of the decisions or present reasons which he believes would warrant the court in not following them in the pending case").

317. *See* Andrea Pin & Francesca M. Genova, *The Duty to Disclose Adverse Precedents: The Spirit of the Common Law and Its Enemies*, 44 YALE J. INT'L L. 239, 256 (2019) (tracing the origin on the rule).

318. CODE OF ETHICS OF THE ALA. STATE BAR ASS'N r. 5 (1887), *reprinted in* ALA. STATE BAR ASS'N, PROCEEDINGS OF THE FORTY-FIRST ANNUAL MEETING OF THE ALA. STATE BAR ASS'N 336 (1918).

adverse to the position asserted by the client and not disclosed by opposing counsel."[319]

Courts have reacted harshly to lawyers who fail to present relevant, adverse legal authority when arguing for their clients. Most famously, Judge Posner published an opinion directing a stinging rebuke at one lawyer for failing to cite relevant authority.[320] After the lawyer repeatedly failed to address a particular case, the opinion compared the lawyer to an ostrich, explaining that the "ostrich is a noble animal, but not a proper model for an appellate advocate."[321] Capturing additional attention, the opinion includes two photographs, one with an ostrich burying its head in the sand and another with a figure clad in a tan business suit in a similar posture.[322]

b. Factual Presentations

In contrast, the Model Rules and ethical norms do not usually require lawyers to disclose adverse factual information. Instead, the model rule instructs that a lawyer "shall not knowingly . . . make a false statement of fact or law to the tribunal or fail to correct a false statement of material fact or law previously made to the tribunal by the lawyer."[323] The Restatement also follows this approach and prohibits lawyers from offering testimony the lawyers knows to be false.[324]

319. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 111(2) (AM. LAW. INST. 2000).

320. *See* Gonzalez-Servin v. Ford Motor Co., 662 F.3d 931, 934 (7th Cir. 2011) ("When there is apparently dispositive precedent, an appellant may urge its overruling or distinguishing or reserve a challenge to it for a petition for certiorari but may not simply ignore it.").

321. *Id.*

322. *Id.* at 935. Notably, the rebuke itself may have been an ethical breach for Judge Posner. *See* Joseph P. Mastrosimone, *Benchslaps*, 2017 UTAH L. REV. 331, 352 (2017) (criticizing so-called benchslaps because "[i]nstead of meeting the attorney's unprofessional or unethical conduct with dispassionate and professional counseling or sanctions, the judges in these benchslaps . . . use[d] their authority to shame and belittle the lawyers").

323. MODEL RULES OF PROF'L CONDUCT r. 3.3 (AM. BAR ASS'N 2020).

324. *See* RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 120 (AM. LAW. INST. 2000) (prohibiting lawyers from offering false facts or testimony to the tribunal).

c. The Knowledge Qualifier

A lawyer's ethical obligations within this framework shift once the lawyer has *knowledge* that some evidence or factual information is false. The knowledge qualifier grants substantial flexibility and even allows lawyers to present information they believe to be false. The Model Rules define "knowledge" as "actual knowledge of the fact in question," with the addition that "[a] person's knowledge may be inferred from circumstances."[325]

In discussing the ABA's Model Rule, the official comment explains that the "prohibition against offering false evidence only applies if the lawyer knows that the evidence is false. Even a lawyer's reasonable belief that evidence is false does not preclude its presentation to the trier of fact."[326]

Substantial justification undergirds this rule. Lawyers practice with limited information and may not be able to actually know whether a client's account actually transpired or was simply fabricated. If lawyers could not present a client's version of events simply because the lawyer harbored some doubts, it would substantially interfere with a client's ability to obtain assistance.

Doubting lawyers do not always need to investigate dubious factual claims. A comment to the Model Rule instructs lawyers to "resolve doubts about the veracity of testimony or other evidence in favor of the client."[327] The ethics rules do not explicitly require lawyers to make any attempt to put their doubts to rest before offering evidence they believe may be false.[328] Although the comment to the Model Rule indicates that a lawyer may not "ignore an obvious falsehood," in most practice situations, lawyers have no clear ethical obligation to investigate their client's factual claims or search for evidence which would show that a client has given a false factual

325. MODEL RULES OF PROF'L CONDUCT r. 1(f) (AM. BAR ASS'N 2020).

326. MODEL RULES OF PROF'L CONDUCT r. 3.3 cmt. [8] (AM. BAR ASS'N 2020).

327. *Id.*

328. *See* George M. Cohen, *The State of Lawyer Knowledge Under the Model Rules of Professional Conduct*, 3 AM. U. BUS. L. REV. 115, 117 (2014) ("The actual knowledge standard aims to exclude a duty to inquire.").

account.[329] George Cohen characterized the "knowledge" qualifier as a "key marker in a contentious struggle over the scope of a lawyer's duty to investigate."[330] The ethics rules only create clear liability for lawyers issuing reckless statements about "the qualifications or integrity of a judge, adjudicatory officer or public legal officer, or of a candidate for election or appointment to judicial or legal office."[331]

In some instances, lawyers may decide that they would rather not investigate and know the truth because knowing the truth might impair their ability to advocate for a client.[332] George Cohen explains that "a lawyer faced with a suspicious fact" might reason that "investigating would be a bad idea because that would put the lawyer at risk of violating the knowledge-based rule."[333] Of course, for lawyers practicing in federal court, Federal Rules of Civil Procedure (FRCP) provide a limited check. FRCP Rule 11 forces lawyers submitting papers to a court to certify that a lawyer conducted "an inquiry reasonable under the circumstances."[334] The requirement does not force a lawyer to certify that she believes a contention to be true, so much as "the factual contentions have evidentiary support."[335] In some instances, this evidentiary support may simply be a client's doubtful claims.

329. *See id.* at 125 ("Thus, a lawyer faced with a suspicious fact that is not sufficient along with other circumstances to impart actual knowledge need not do anything further.").

330. *Id.* at 124.

331. MODEL RULES OF PROF'L CONDUCT r. 8.2(a) (AM. BAR ASS'N 2020).

332. Duties of inquiry do exist in some practice areas. In transactional securities practice, lawyers and other professionals have long faced a duty to inquire. *See* Cohen, *supra* note 328, at 118 ("Transactional lawyers in particular are familiar with the recklessness standard because it plays an important role in securities fraud and other business crimes and torts."). Lawyers must also make inquiries when preparing opinion letters. *See, e.g.*, Excalibur Oil, Inc. v. Sullivan, 616 F. Supp. 458, 463 (N.D. Ill. 1985) ("Necessarily implicit in any [opinion letter] contract is the lawyer's duty to investigate the title with reasonable diligence and to report his findings accurately.").

333. Cohen, *supra* note 328, at 125.

334. FED. R. CIV. P. 11.

335. *Id.* at (b)(3).

d. A Limited Duty to Correct

Under the ethics rules, lawyers owe only a limited obligation to inform a tribunal when they know that false evidence has been presented to it. The ABA's Model Rules only explicitly require lawyers to take "remedial measures, including, if necessary, disclosure to the tribunal" when a lawyer learns that she, her client, or a witness she called offered material evidence she later came to know was false.[336] The Restatement takes the view that lawyers have "no responsibility to correct false testimony or other evidence offered by an opposing party or witness."[337]

Lawyers do owe an obligation to the tribunal to correct false information when they have had some hand in presenting the information to the tribunal. The Restatement explains that even if it would hurt a client's interests, a lawyer must correct false information she had some role in presenting because "preservation of the integrity of the forum is a superior interest."[338]

e. Undisclosed Vital Factual Evidence

In most situations, ethics rules do not obligate lawyers to provide tribunals or opposing counsel with all, significant, material information in their possession.[339] The ethics rules do not generally require lawyers to volunteer accurate information vital to developing an informed understanding of a dispute.[340]

336. MODEL RULES OF PROF'L CONDUCT r. 3.3(a)(3) (AM. BAR ASS'N 2020).

337. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 120 cmt. d. (2000) ("[A] plaintiff's lawyer, aware that an adverse witness being examined by the defendant's lawyer is giving false evidence favorable to the plaintiff, is not required to correct it . . . .").

338. *Id.* at cmt. b.

339. *See* Nathan M. Crystal, *Limitations on Zealous Representation in an Adversarial System*, 32 WAKE FOREST L. REV. 671, 715 (1997) ("It is a well-established doctrine that lawyers have no obligation to disclose voluntarily . . . to opposing parties or to the tribunal evidence that is material to the case, even if nondisclosure would produce a result that is inconsistent with the truth.").

340. *See* John A. Humbach, *Shifting Paradigms of Lawyer Honesty*, 76 TENN. L. REV. 993, 1013 (2009) ("[I]t is a professional truism of current American legal practice that a lawyer has no general duty to volunteer.").

The ABA has even issued a formal ethics opinion that lawyers may violate the ethics rules if they inform opposing counsel that the statute of limitations has run on a claim because it would violate their duties to their client.[341] At the most, the comment to the ABA ethics rule recognizes that some circumstances exist "where failure to make a disclosure is the equivalent of an affirmative misrepresentation."[342]

Some courts have found "failure to make disclosure of a material fact to a tribunal is the equivalent of affirmative misrepresentation."[343] New Jersey goes further than most states and requires lawyers to disclose unprivileged or otherwise unprotected material facts if a court would otherwise be misled by nondisclosure.[344] These limited requirements leave substantial room for error.

Yet tribunals often fail to receive information vital to developing a well-informed understanding of a dispute—even when the information is known to one or all of the parties to a dispute.[345] Importantly, procedural, ethical, and economic constraints all shape the information tribunals actually receive.[346]

341. *See* ABA Comm. on Ethics & Prof'l Responsibility, Formal Op. 94-387 (1994) ("[W]e conclude that a lawyer has no ethical duty to inform an opposing party that her client's claim is time-barred; to the contrary, it may well be unethical to disclose such information without the client's consent.").

342. MODEL RULES OF PROF'L CONDUCT r. 3.3 cmt. [3] (AM. BAR ASS'N 2020).

343. AIG Haw. Ins. Co. v. Bateman, 923 P.2d 395, 402 (Haw. 1996), *amended on reconsideration in part*, 925 P.2d 373 (1996); *see, e.g.*, *In re* Fee, 898 P.2d 975, 979 (Ariz. 1995) ("The system cannot function as intended if attorneys, sworn officers of the court, can . . . mislead judges in the guise of serving their clients.").

344. *See* N.J. RULES OF PROF'L CONDUCT 3.3(a)(5) (2003) (prohibiting failure "to disclose to the tribunal a material fact knowing that the omission is reasonably certain to mislead the tribunal, except that it shall not be a breach of this rule if the disclosure is protected by a recognized privilege or is otherwise prohibited by law").

345. *See supra* Part II.E.

346. *See* RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 120 cmt. b. (2000) (explaining that an "advocate who knows of the evidence, and who has complied with applicable rules concerning pretrial discovery and other applicable disclosure requirements . . . has no legal obligation to reveal the evidence, even though the proceeding thereby may fail to ascertain the facts as the lawyer knows them").

In some instances, all parties to the litigation might prefer to avoid presenting courts with particular factual information or arguments. Lawyers after all tend to operate in the interests of their clients and not in the interest of helping a tribunal develop the most accurate understanding.[347] This means that tribunals will proceed without important material information when it is not in any party's interest to provide the information and the law does not compel disclosure. Adding to the problem, even when the ethics rules compel disclosure, attorneys will only rarely face any repercussion for failing to disclose.[348]

f. Ex Parte Proceedings

The ethics rules impose an expanded duty of candor on advocates in ex parte proceedings. The ABA's Model Rules instruct that in an ex parte proceeding "a lawyer shall inform the tribunal of all material facts known to the lawyer that will enable the tribunal to make an informed decision, *whether or not the facts are adverse*."[349]

The comment to the Model Rule explains why disclosure is required in ex parte proceedings. In an ordinary situation, "an advocate has the limited responsibility of presenting one side of the matters that a tribunal should consider in reaching a decision."[350] In our adversarial system, "the conflicting position is expected to be presented by the opposing party."[351] Yet in ex parte situations, such as a request for "a temporary restraining order, there is no balance of presentation by opposing advocates."[352] Despite this, the comment instructs that the

347. *See* Humbach, *supra* note 340, at 995 ("Lawyers do not generally view it as part of their professional role to be personally responsible for getting at the truth of the matter but, rather, to persuade others to believe or accept whatever interpretation of the raw evidence is most beneficial to the interests of their own clients.").

348. *See* Edwards, *supra* note 29, at 1491 ("In many instances, state bars do not allocate substantial resources to their enforcement staff to investigate complaints.").

349. MODEL RULES OF PROF'L CONDUCT r. 3.3(d) (AM. BAR ASS'N 2020) (emphasis added).

350. *Id.* at cmt. 14.

351. *Id.*

352. *Id.*

object of the proceeding "is nevertheless to yield a substantially just result."[353] To accomplish this goal, it requires a lawyer for the represented party "to make disclosures of material facts known to the lawyer and that the lawyer reasonably believes are necessary to an informed decision."[354]

In describing a lawyer's ethical obligations in ex parte proceedings, the Restatement goes further and also prohibits lawyers from presenting "evidence the lawyer reasonably believes is false" and instructs lawyers to also comply with "any other applicable special requirements of candor imposed by law."[355] The comment recognizes that the "potential for abuse is inherent in applying to a tribunal in absence of an adversary."[356]

Identifying the situations where a lawyer must operate under an expanded duty of candor remains challenging because the ABA's Model Rules do not define ex parte proceedings.[357] Although technical definition would exclude all cases where some other party appears in the action, this would overly limit the rule's impact. One Idaho court read Idaho's rule as applying when one of the parties, after having received notice, failed to appear in a proceeding.[358] It read the comment as suggesting "that the application of the rule is not meant to hinge on a technical definition of the term ex parte, but is instead intended to ensure that the tribunal is informed of facts necessary to render a just decision."[359] It found that the underlying rationale applied when "'there is no balance of representation by opposing advocates'" applied when one of the parties was simply absent from a proceeding.[360]

353. *Id.*

354. *Id.*

355. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 112 (2000).

356. *Id.* at cmt. b.

357. MODEL RULES OF PROF'L CONDUCT r. 1.0 (AM. BAR ASS'N 2020) (failing to define ex parte).

358. *See In re* Malmin v. Oths, 895 P.2d 1217, 1220 (Idaho 1995) ("The judge has an affirmative responsibility to accord the absent party just consideration.").

359. *Id.*

360. *Id.* (quoting MODEL RULES OF PROF'L CONDUCT r. 3.3 cmt. 14 (AM. BAR ASS'N 2020)).

Policy rationales support extending the requirement beyond purely technical situations. The Restatement recognizes that in some special proceedings, "public policy requires unusual candor from an advocate."[361] It identifies child custody proceedings, involuntary commitment proceedings, and class action settlement proceedings.[362]

Massachusetts also treats class action settlement proceedings as quasi-ex parte proceedings requiring lawyers to be fully candid with the court. The comment to its ethics rule explains that when:

> [A]dversaries present a joint petition to a tribunal, such as a joint petition to approve the settlement of a class action suit or the settlement of a suit involving a minor, the proceeding loses its adversarial character and in some respects takes on the form of an ex parte proceeding.[363]

The Massachusetts rule recently played a significant role in extended litigation arising out of a class action settlement before a Massachusetts federal court.[364] After the court approved a large class action settlement deal, it emerged that "$4,100,000 of the $75,000,000 fee award had been paid to Damon Chargois, a lawyer in Texas who had done no work on the case, and whose name was not disclosed to [the named plaintiff], the class, or the court."[365] Other problems emerged as well. Over 9,000 attorney hours had been double counted.[366] It also appeared that attorneys were billed at rates in excess of what hourly clients ever paid.[367] Troubled by the revelation, the court ultimately reduced class counsel's fee award and explained the need for

361. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 112 cmt. c (2000).

362. *Id.*

363. MASS. RULES OF PROF'L CONDUCT r. 3.3. cmt. 14A (2015).

364. For a more thorough discussion of the case, *see* Edwards & Rickey, *supra* note 39.

365. Ark. Teacher Ret. Sys. v. State St. Bank & Tr. Co., 404 F. Supp. 3d 486, 492 (D. Mass. 2018).

366. *See id.* at 499 ("[D]ouble-counting resulted in inflating the number of hours worked by more than 9,300.").

367. *See id.* ("[S]taff attorneys involved in this case were typically paid $25–$40 an hour . . . . [T]he regular hourly billing rates for the staff attorneys were much higher — for example, $425.").

complete candor in class action settlement hearings because "the adversary process does not operate and have the potential to expose misrepresentations."[368]

2. Expanded Duties

The professional ethics rules governing attorney conduct assume that the attorney plays a defined role within a functioning adversarial system. Yet incentives sometimes align in ways that undercut this assumption within dispute resolution systems. Ethics authorities might address the gap by providing enhanced guidance for attorneys operating in these types of proceedings. A practical expansion may be accomplished by amendments to the ABA's Model Rules or by individualized efforts by states to address the issue. State bar ethics opinions may also operate with some force to shift behavior.

In circumstances where adversarial failure regularly occurs, professional ethics rules should clearly and unambiguously expand an attorney's duties in ways designed to increase the likelihood that a tribunal will render a well-informed decision. An expanded disclosure duty may serve to increase the likelihood that a tribunal will render a reasonably informed decision. Practically, the duty must include two distinct parts, an expanded duty of candor accompanied by an affirmative obligation to investigate.

a. An Expanded Duty of Candor

Ethics authorities could respond to adversarial failure by requiring that attorneys operate under an expanded duty of candor in situations that resemble ex parte proceedings in substance, if not form. Massachusetts, at least, already embraces this premise with its official comment recognizing that when "adversaries present a joint petition to a tribunal, such as a joint petition to approve the settlement of a class action suit or the settlement of a suit involving a minor, the

368. Ark. Teacher Ret. Sys. v. State St. Bank & Tr. Co., No. 11-10230, 2020 WL 949885, at *47 (D. Mass. Feb. 27, 2020).

proceeding loses its adversarial character and in some respects takes on the form of an ex parte proceeding."[369]

The same dynamic may apply whenever an adversary simply opts not to contest an application for relief. Consider the dynamic in expungement-only arbitrations brokers now file against their employers. From an adjudicator's perspective, there may be little difference between a joint application and an uncontested one. In each case, the adjudicator hears no opposition and only views evidence from one party pushing it toward a single outcome.

b. An Expanded Duty to Investigate

Yet an expanded duty of candor alone will not suffice. To avoid speaking any evil, attorneys may simply opt to hear and see little other than what their client tells them. Tribunals should not be deprived of reasonably accessible information simply because a lawyer opts to shut her eyes to obvious lines of inquiry.

A clear duty to conduct a reasonable investigation under the circumstances may address this issue. In instances where attorneys fail to disclose readily obtainable information to a tribunal, protestations that the attorney was not aware of the information should not remove all ethical liability.[370] This obligation might reduce the incentive to seek expungements in cases where readily available public information undercuts a broker's claims.

c. Disclosure's Limits

Changes to attorney ethics rules may do some real good, but they certainly will not entirely solve the problems that flow from attempting to resolve these issues through processes designed for adversarial parties to resolve private disputes. Disclosure-oriented reforms have not always shifted actual

369. MASS. RULES OF PROF'L CONDUCT r. 3.3. cmt. 14A (2015).

370. *Cf.* Cohen, *supra* note 328, at 148 (suggesting that the ABA "add a comment to the definition of knowledge stating that the knowledge requirement does not negate or limit any duty to investigate or communicate that otherwise exists, and that the deliberate breach of these duties can be evidence of willful blindness and therefore knowledge").

conduct in adversarial proceeding.[371] Even substantive disclosure requirements in securities class action litigation, requiring repeat plaintiffs to disclose prior litigation have not always generated expected disclosures.[372] Expanded ethical guidance must be accompanied by some real enforcement pressure to be effective.

Arbitration forums also present real challenges because the reach of attorney ethics rules may depend on the state. New York's federal courts have found that representing a party in arbitration does not qualify as the practice of law.[373] In contrast, California treats arbitration as part of the practice of law.[374]

As an alternative to state-by-state ethics changes, FINRA could make rules applicable to all representative advocates appearing in expungement hearings. It could enforce these rules by suspending or permanently barring violators from pursuing expungement relief for clients within its forum. This might generate a significant incentive to disclose readily available information that would be contrary to an expungement request. As a number of firms specialize in pursuing expungement requests for clients, the threat of losing access to the forum would be significant enough to shift behavior.

371. *See* Edwards & Rickey, *supra* note 39, at 1566 ("Disclosure-based reforms, however, have a limited track record of success and are unlikely to be a panacea on their own.").

372. *See* Jessica Erickson, *The New Professional Plaintiffs in Shareholder Litigation*, 65 FLA. L. REV. 1089, 1135 (2013) (discussing absent disclosures in securities class action litigation).

373. *See* Prudential Equity Grp., LLC v. Ajamie, 538 F. Supp. 2d 605, 608 (S.D.N.Y. 2008) (ruling that under New York law, arbitration does not qualify as the practice of law); *see also* Siegel v. Bridas Sociedad Anonima Petrolera Indus. y Comercial, No. 90 CIV. 6108 (RJW), 1991 WL 167979, at *5 (S.D.N.Y. Aug. 19, 1991) (same).

374. *See* Birbrower, Montalbano, Condon & Frank v. Super. Ct., 949 P.2d 1, 9 (Cal. 1998), *as modified* (Feb. 25, 1998) (declining "to craft an arbitration exception to section 6125's prohibition of the unlicensed practice of law in this state").

C. Adjudicator Responses

1. An Appointed Advocate

Adjudicators may also respond to adversarial failure by taking steps to restore adversarial scrutiny and increase the likelihood of an informed decision. This idea has been raised before. Special masters have been proposed as a response to defects in class action settlement approval processes with one justice suggesting appointing a "devil's advocate" to raise arguments against class action fee arrangements.[375] Delaware's vaunted Chancery Courts have also considered recruiting assistances from an *amicus curiae* to overcome adversarial breakdown.[376] The PIABA Foundation also suggested a reform in this vein, arguing that "FINRA and/or the SEC create an investor protection advocate ("Advocate") that is independent from FINRA to participate in every Expungement-Only case."[377]

These ideas have real merit and may increase the likelihood that an adjudicator considering an expungement request will make a reasonably informed decision. At the very least, regular, experienced, and reasonably competent opposition would likely discourage some of the worst abuses.

2. Greater Control Over Process

Adjudicators could also take steps to mitigate adversarial failure by taking greater control over the process. Consider the benefits which might flow from adjudicators taking greater control over notice processes. At present, advocates enjoy substantial freedom to influence the notice process to increase

375. *See* Laffitte v. Robert Half Int'l Inc., 376 P.3d 672, 691 (Cal. 2016) (Liu, J., concurring); *see also* William B. Rubenstein, *The Fairness Hearing: Adversarial and Regulatory Approaches*, 53 UCLA L. REV. 1435, 1475–77 (2006) (arguing for a devil's advocate to evaluate substantive settlements in class actions).

376. *See In re* Trulia, Inc. S'holder Litig., 129 A.3d 884, 899 (Del. Ch. 2016) ("[I]t may be appropriate for the Court to appoint an amicus curiae to assist the Court in its evaluation of the alleged benefits of the supplemental disclosures, given the challenges posed by the non-adversarial nature of the typical disclosure settlement hearing.").

377. DOSS & BRAGANÇA, *supra* note 88, at 10.

the likelihood that they will receive favorable outcomes.[378] An adjudicator focused on increasing participation and surfacing information would likely provide notice in a different way. Notices would be crafted to encourage participation. They would be distributed repeatedly and with a substantial lead time before any hearing. A notice aimed at increasing customer participation would direct recipients to relevant information about any available pro bono assistance.

Improved processes would also distribute notice about the request more broadly to encompass all relevant stakeholders. State and federal regulators might opt to appear at the fact-finding stage if they were given notice and an invitation to participate. Investors with claims currently pending against a broker seeking an expungement might also opt to provide their perspectives and experiences with the broker. Essentially, adjudicators could shift the processes they use to solicit additional information in ways designed to encourage stakeholder participation.

3. Eliminate Repeat Player Bias Risk

In the expungement context, FINRA might attempt to eliminate the risk that arbitrators will favor industry interests in expungement hearings by removing the ability for parties to rank and strike arbitrators who hear expungement requests. To its credit, FINRA has considered and its board has approved a rule establishing a pool of arbitrators who receive additional trainings for expungements.[379] As the rule proposal has not yet been filed with the SEC, the precise contours of the rule remain uncertain.

A roster with additional training alone seems unlikely to substantially improve the process because selection effects will

378. *See* Humbach, *supra* note 340, at 995 ("While telling lies is definitely out of bounds . . . trying to bend others' perceptions to the client's best advantage is seen to be at the heart of good advocacy.").

379. *See* Fin. Indus. Reg. Auth., Regulatory Notice 17–42 Expungement of Customer Dispute Information 5 (Dec. 6, 2017), https://perma.cc/HB2Z-YAV3 (PDF) (requesting comments on the proposed changes); *see also* FIN. INDUS. REG. AUTH., UPDATE: FINRA BD. OF GOVERNORS MEETING (Oct. 3, 2019), https://perma.cc/ETT5-5S5W (noting that the Board had approved the proposed changes).

remain significant. The arbitrator selection process now allows brokers to cut known skeptics or arbitrators prone to asking too many probing questions from their list. As many expungement-only matters proceed without participation from parties with an interest in a skeptical arbitrator, the selection pressures strongly favor arbitrators who routinely grant expungement requests. Removing the ability to rank and strike arbitrators in expungement matters would substantially mitigate this risk.

Importantly, the arbitrator roster for expungement matters should serve exclusively on expungement matters. Maintaining a limited, exclusive pool would generate real benefits. With a smaller pool, the overall cost of providing significant training would diminish. Setting the expungement roster aside from other customer or industry cases would also mitigate other selection pressures. The financial services industry always participates in customer or industry disputes and remains a repeat player, allowing it to accumulate knowledge about arbitrators. This creates pressure for expungement arbitrators to favor the industry to increase the likelihood they will be selected for other matters. In contrast, customers with disputes generally appear in the forum as single-shot players. Although past arbitration results are disclosed and some customer-claimant-side counsel operate as repeat players, the industry will generally have more knowledge and sophistication. The financial services industry always appears in these arbitrations as a party while customers will only sometimes secure representation from repeat player counsel. Completely insulating an expungement arbitrator roster from these selection pressures may do significant good.

Creating different rules for the expungement arbitrator roster and making it an exclusive body may also shift the way these arbitrators view their roles. In ordinary matters, the parties jointly select an arbitrator to resolve a dispute primarily concerning their interests. In expungement matters, the arbitrators must serve as gatekeepers for the public's interest in maintaining access to information. Although setting them up in this way falls far short of an alternative regulatory process, it would likely do significant good.

IV. Conclusion

Our system of securities laws relies heavily on disclosure to serve as disinfecting sunlight on the theory that when more information comes out, it will enable better decisions. In our dispute resolution systems, we expect adversarial processes, on balance, to surface information and provide adjudicators with the information they need to make informed decisions. Yet these assumptions do not always hold. As this article shows, adversarial failure can leave adjudicators bereft of significant information. When these processes facilitate the deletion of public information, the failures affect society more broadly.

When it occurs, adversarial failure must be addressed to protect the integrity of decisions affecting significant groups of stakeholders. Although an ethics-oriented approach may shift behavior to a degree, it cannot entirely solve the problem. Ultimately, whenever adversarial failure occurs, society should consider alternative methods for deciding issues which better balance the interests at stake.

Exhibit B

Deleting Misconduct: The Expungement of BrokerCheck Records

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ABSTRACT

We examine a controversial process, known as expungement, which allows brokers to remove evidence of financial misconduct from public records. From 2007-2016, we identify 6,660 expungement requests, suggesting that brokers attempt to expunge 12% of the allegations of misconduct reported by customers and firms. When these requests are adjudicated on the merits, arbitrators approve expungement 84% of the time. We show that expungements significantly predict future misconduct; brokers with prior expungements are 3.3 times as likely to engage in new misconduct as the average broker. Further, using an instrumental variable based on the random assignment of arbitrators, we present evidence that brokers who receive expungement are more likely to reoffend than brokers denied expungement. We also show that successful expungements improve long-term career prospects.

Keywords: FINRA Rule 2080, expungement, broker misconduct, recidivism, BrokerCheck

JEL Classification: D18, K20, K22, K23, G24, G28

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1. Introduction

BrokerCheck, a public-facing website maintained by financial regulators, provides employment and disciplinary history for all US-registered securities brokers in an easy-to-search format. There are many indications that the website is well-utilized and provides important information. For example, as of September 1st, 2018, Amazon's Alexa estimated there were 263,478 unique visitors to BrokerCheck over the past 30 days, and that these visitors were older, more educated, and wealthier than the internet average—characteristics of consumers we might expect to research a broker prior to hiring him or her.[1] In addition, brokerage firms are well-known to use the information in hiring decisions. Regulators, too, use the information; they rely on the disciplinary history in BrokerCheck when deciding which brokerage firms to inspect, as not all brokerage firms are inspected annually (FINRA, 2017).[2] Academics have also recently begun to explore the data. For example, Egan, Matvos, and Seru. (2019a) found that prior offenders are more than five times as likely to engage in new misconduct as the average broker, and Qureshi and Sokobin (2015) found that the 20% of brokers with the highest ex-ante predicted harm probability are associated with more than 55% of total harm cases.

Given the relevance of this database to a variety of users, it is important to understand not only what is presented in the database, but also what information has been removed. Information is removed through a controversial practice, known as "expungement," which allows brokers to remove select allegations of misconduct through an arbitration process. The expungement process has been the subject of significant policy debate (Warren, 2019; Lipner, 2013; Edwards, 2017ab; Berkson and Lambert, 2016). State regulators and investor advocates have argued that expungement removes legitimate allegations of misconduct, therefore harming the ability for state regulators to monitor brokers effectively and for investors to protect themselves (Lipner, 2013). In response, broker advocates have pointed out that the allegations of misconduct in BrokerCheck are frequently unverified, and have praised the expungement process as an avenue for brokers to remove meritless allegations (Kennedy, 2016).

[1] Please see Exhibit 1 in the Online Appendix for information provided by Amazon's Alexa.

[2] Although FINRA and other regulators rely on Central Registration Depository (CRD) (the database underlying BrokerCheck), expungements remove the information from CRD as well.

Journalists and the Public Investors Arbitration Bar Association (PIABA) have previously collected subsets of the BrokerCheck expungement awards (e.g., PIABA, 2013, 2015, Weinberg, 2018).[3] These prior studies often demonstrate success rates of over 90%, leading to vigorous policy debate and congressional action proposing reform (e.g., Grassley and Reid, 2013). To our knowledge, however, none of the prior work has attempted to collect the full set of expungements; nor has it examined the effect of BrokerCheck expungement on future misconduct or career outcomes. We provide this analysis.

Our study begins by scraping data on arbitration awards from FINRA's Arbitration Awards database, allowing us to identify 6,660 broker requests for expungement filed from 2007 to 2016. For comparison, there were just over 53,000 new allegations of misconduct made by firms or customers over the same period (brokers cannot expunge civil, criminal, or regulatory disclosures through this process, so we limit the comparison to allegations made by firms or customers). This suggests that brokers request to expunge 12% of the allegations of misconduct made by customers and firms.[4] Of the expungement requests that are adjudicated on the merits, over 80% are successful.

On the one hand, if the process functions as intended—meaning that the expunged information is inaccurate or otherwise does not reflect the broker's conduct—removing the information has many benefits. It should (1) improve the accuracy of the BrokerCheck database, (2) incentivize brokers to maintain a clean record by sharpening the signal between "clean" and "misconduct" brokers (Mungan, 2017; Png, 1986; Polinsky and Shavell, 1989), and (3) allow

[3] PIABA has performed the most systematic study of the awards, but their collection process is limited to expungement cases involving stipulated awards or settled customer claims rather than the full set of expungement awards. Further, their coding reflects whether any expungement request in the award was successful, not whether each request was successful (there are frequently multiple requests in the same award, and outcomes may differ for each request). This choice leads to a mechanically higher success rate.

[4] Under the conservative assumption that all expunged misconduct was incurred during our sample period and should be included in the denominator, we have 6,660 expungement attempts relative to 58,100 new allegations of misconduct by customers and firms (53,525 allegations remaining in BrokerCheck and 4,575 successfully expunged allegations). Of course, this estimate is imperfect as there is a time-lag between when the infraction occurs and when it is expunged, meaning that expungements in the beginning of our sample likely relate to misconduct that occurred prior to 2007, and that misconduct in recent years would not show up in our expungement sample. For this reason, our inclusion of all successfully expunged allegations in the denominator is over-inclusive as some of these infractions occurred prior to 2007, but we take this approach to be conservative.

regulators, firms, and consumers to perform more effective monitoring, as they can better predict the brokers likely to commit misconduct.

On the other hand, if brokers are abusing the expungement process, as some have alleged, removing misconduct from BrokerCheck will reduce the utility of BrokerCheck and monitoring based on this information—and hamper the effectiveness of FINRA's disciplinary regime, which imposes increasingly severe sanctions on repeat offenders (FINRA, 2019). Moreover, if the expungement process is abused, behavioral literature suggests that it could lead to an increase in socially undesirable behavior, as studies have found that a higher incidence of unethical behavior is likely to occur if prior unethical decision making is rewarded (Hegarty and Sims, 1978). Moreover, success can breed overconfidence and, in the investment context, excessive risk-taking (e.g., Laming, 1968; Rabbitt and Phillips, 1967; Rabbitt and Rodgers, 1977; Mizruchi, 1991; Gino and Pisano, 2011; Odean, 1998; Camerer and Lovallo, 1999).

Therefore, a key issue in understanding the impact of expungement is the relationship between expungement and broker recidivism. At a descriptive level, successful expungements predict future misconduct; brokers with prior expungements are 3.3 times as likely to engage in new misconduct as the average broker. This suggests that expungements may provide value to BrokerCheck users insofar as these awards contain some predictive information. However, this simple OLS regression does not address whether expungement affects recidivism, as many of the characteristics associated with successful expungements are also likely to be associated with a lower likelihood of recidivism.

To answer the causal question of whether expungement affects recidivism, we use an instrumental variable analysis where our instrument is based on the randomized list of arbitrators assigned to the case. The arbitrators on this list are chosen by an algorithm, and FINRA states explicitly—and has undergone an audit to confirm—that the algorithm selects the initial list of arbitrators randomly (subject only to geographic limitations) (FINRA, 2016). The arbitrators on this list are not publicly available, but FINRA provided us with this information for the purposes of this study. Conceptually, our instrument is the relative leniency of this randomly generated list. Empirically, we define two instruments: the relative leniency of the (1) mean and (2) median arbitrator on FINRA's randomly generated list of potential arbitrators, where "relative" is determined in comparison with other arbitrators in the same year and region. To determine each

arbitrator's leniency, we compute the number of expungements awarded relative to the total number of expungements over which the arbitrator has presided (excluding the current case).

Although the parties can endogenously select their arbitrators from this randomly generated list, we do not expect this potential endogenous selection to affect the validity of our IV as we rely solely on the randomly generated list. Moreover, our tests confirm that the leniency of the arbitrators on the randomly generated list is significantly correlated with expungement success (i.e., the first-stage results are highly significant). However, we do not expect FINRA's random draw of arbitrators to affect recidivism except through its effect on the expungement process (i.e., we theorize that the exclusion restriction holds).

Our analysis provides evidence that successful expungements increase recidivism. The 2SLS results, which exploit plausibly exogenous variation in expungement from the random assignment of FINRA's arbitrator list, show that expunged brokers are more likely to reoffend. With full controls, the 2SLS result using the median arbitrator on the randomly generated list of potential arbitrators shows that the marginal expunged broker has 0.31 more years with allegations of misconduct (or expunged misconduct) than brokers who are denied expungement. Notably, this result appears to be driven by repeat expungements—in other words, successful expungements cause an increase in future expungements. With full controls, the 2SLS results show that the marginal expunged broker has 0.16 to 0.20 more years with successful expungements than brokers who are denied expungement. Additional robustness tests provide evidence that the increase in successful expungements is jointly driven by an increase in expungement requests and a greater likelihood of success.

There are several explanations for why successful expungements would increase recidivism. First, as noted previously, predictions based on behavioral literature are consistent with this finding. Relative to a broker denied expungement, a broker granted expungement might increase recidivism and expungement requests due to increased risk-taking with client assets, overconfidence that he can obtain another expungement, and/or more frequent incidences of unethical behavior, as the broker has received external signals that his initial behavior was appropriate. Second, the findings are consistent with the incentives created by FINRA's accelerating sanctions regime. The brokers denied expungement face increasing costs of misconduct for each additional infraction, but the brokers granted expungement are reset to a lower baseline as expunged misconduct will not be considered when penalizing additional misconduct.

Thus, a marginal broker granted expungement is presumably more likely to engage in future misconduct because the cost of such misconduct is likely to be lower than for a marginal broker denied expungement.

Finally, it is possible that expungement increases recidivism because it improves career outcomes, allowing expunged brokers to remain in the industry for longer periods and thus have more opportunity to commit misconduct. Prior literature on financial advisors supports this possibility, as brokers are more likely to depart the firm after misconduct, and are less likely to be rehired going forward (Egan, Matvos, and Seru, 2019a). Although we are not aware of any prior work that has examined the effect of removing evidence of misconduct on brokers' career prospects, there are intuitive explanations for why it would provide similar career benefits. For example, even if an employer knows of an expunged infraction, firms may be more comfortable with a broker who has "private" allegations of misconduct rather than a broker with "public" allegations of misconduct.

Therefore, we examine the career consequences of expungement. Our descriptive analysis suggests that brokers who receive a successful expungement are more likely to remain with their firm, and conditional on leaving the firm, to be rehired by another brokerage firm. Similarly, the results from our instrumental variable analysis using the leniency of the mean arbitrator show that, relative to those denied expungement, marginal expunged brokers are 21 percentage points less likely to separate from their firm (with full controls). Marginal expunged brokers also remain in the BrokerCheck database for a greater number of years (meaning they remain employed as registered brokers). Therefore, there is evidence that expungement improves career outcomes, plausibly providing expunged brokers with greater opportunity to commit misconduct and driving our results on recidivism. Although additional robustness tests suggest that the beneficial career consequences of expungement are unlikely to be the primary mechanism driving our results showing that expungement increases recidivism, they are likely a contributing factor.

Our paper contributes to several areas of literature. First, we contribute to prior work on personal brands as a regulatory tool. Personal brands are a crucial component of the regulatory regime for different financial professionals, including registered broker-dealers, investment advisers, and National Futures Association members. Regulators require these individuals to disclose substantial personal information to the regulator, much of which is then made available online in accordance with a market-based theory of deterrence: public disclosure will allow

markets to weed out the "bad actors". Regulators frequently post allegations with relatively limited verification, such as customer complaints, because these allegations have predictive power (e.g., Dimmock and Gerken, 2012; Egan, Matvos, and Seru, 2019a; Qureshi and Sokobin, 2015; McCann, Qin, and Yan, 2017). But, although these allegations have predictive power on average, there are false positives as well. Thus, one tension with this approach is the degree to which regulators should verify disciplinary information ex ante versus allowing individuals to remove information ex post through expungement. Our study suggests that, at least at present, regulators should rely more heavily on ex ante verification rather than ex post expungement.

Second, our paper contributes more generally to literature on reputation. Prior work has shown that firms punish bad actors, but it is unclear whether firms penalize bad actors because they care about misconduct or because they do not want to be publicly associated with bad actors. A simple example illustrates the difference. Human Resources at the Wynn Las Vegas had received allegations that Steve Wynn sexually assaulted female employees for over a decade, but it was only when the allegations became public that Steve Wynn was forced to step down from his position as CEO and Chairman of Wynn Resorts (Astor and Creswell, 2018). Similarly, there may be a difference in how brokerage firms view public and private misconduct, and our setting allows us to better understand this distinction. If these firms care equally about public and private misconduct, we might expect expungement to have little impact on career outcomes. However, we find that expungement significantly improves career prospects, and that many firms' applications do not ask about expunged misconduct, implying that firms care more about public misconduct.

Third, we contribute to work on the removal of information from consumer databases. Prior work examines the career consequences of publicly known misconduct, but we are unaware of any prior empirical work that examines the effect of removing that misconduct. The closest area of literature examines the removal of adverse credit market indicators such as bankruptcy flags (e.g., Dobbie, Keys, and Mahoney, 2017; Dobbie, Goldsmith-Pinkham, Mahoney, Song, 2019). However, our setting differs from these papers in crucial ways. First, the parties in our setting remove allegations of misconduct rather than financial mishaps. Second, the parties here apply for expungement, whereas credit flags disappear after a certain number of years.

Finally, we contribute to the ongoing policy debate over expungement. FINRA has recently proposed updated rules to govern the process, and our analysis suggests several avenues for

reform. The period to comment on FINRA's proposals closed in early 2018, so FINRA may formally propose rule changes for SEC approval in the near future.

2. Institutional Background

In the United States, many investor allegations involving financial-advisor misconduct—anywhere from 3,000 to 9,000 complaints each year—are adjudicated through FINRA's arbitration process (FINRA, 2020). Arbitrations are conducted either by a single factfinder or a panel comprised of three adjudicators. In each case, the arbitrators are drawn from a group of more than 7,800 arbitrators maintained by FINRA nationwide (FINRA, 2020).

FINRA identifies a potential set of arbitrators using the Neutral List Selection System, a computer algorithm that ensures conditional random selection (subject only to minimization of arbitrator travel). According to FINRA, "[t]he randomized process [used in NLSS] has been verified by an Ernst & Young audit in a report that confirmed that a 'random pool management algorithm [is] used to ensure that each arbitrator in the pool has the same opportunity to appear on a list as all other arbitrators in that pool'" (FINRA, 2016). After the list is determined, each party to an arbitration is allocated a certain number of strikes to eliminate undesirable candidates. Theoretically, if both parties select the arbitrator with equal diligence, they will end up with the average arbitrator on the initial list of randomly assigned arbitrators.[5] In investor cases with claims of up to $100,000, the general rule is that a single arbitrator will adjudicate the claim. The parties receive one list of ten qualified public arbitrators, and each party has the right to strike up to four arbitrators from the list and rank the remaining six (FINRA, 2016). Investor cases involving claims of more than $100,000 are typically adjudicated by a panel of three arbitrators. In these cases, the

[5] For example, assume the following scenario: A broker attempts to expunge an infraction from his record, and he has a single-arbitrator panel. FINRA will provide a list of ten randomly generated potential arbitrators, along with detailed Arbitrator Disclosure Statements describing their professional qualifications, to the respondent and claimant. After completing the research process, each party may strike up to four arbitrators—presumably those perceived as most hostile—and is asked to rank those remaining. FINRA then assigns as arbitrator the candidate who has been ranked most favorably by both parties (and who has not been eliminated). If the claimant strikes arbitrators 1 through 4 and the respondent strikes arbitrators 7 through 10, FINRA will assign either arbitrator 5 or 6, depending on which one was ranked more highly by the participants. However, it is not clear that both parties select the arbitrator with equal diligence. For example, Egan, Matvos, and Seru (2019b) examines 9,000 FINRA arbitrations and find that industry-friendly arbitrators are more likely to be selected. They attribute this result to firms' informational advantage in selecting arbitrators. In our sample, we find that regressing the leave-out success rate of the average arbitrator on the randomly generated list of potential arbitrators on the arbitrator selected yields a coefficient that slightly below 1 (0.929 and 0.657 for mean and median, respectively), and a positive constant (0.071 and 0.255 for mean and median, respectively).

parties receive three lists of potential arbitrators, and again strike the least desirable options from each list and rank those remaining (FINRA, 2016).

After a customer complaint is settled or adjudicated, the firm or broker that was the subject of the complaint has an obligation to report that outcome to FINRA's Central Registration Depository (CRD), typically no more than 30 days after learning that a filing is required. Firms or individuals who fail to file required updates are subject to regulatory action by FINRA. FINRA then releases some, but not all, of the information in each firm and broker's CRD file to the public on FINRA's BrokerCheck website (Qureshi and Sokobin, 2015).

BrokerCheck displays information on all brokers and firms registered with FINRA. Subject to limited exceptions, financial professionals who buy or sell securities on behalf of their customers or their own account are required to register with FINRA. As such, the scope of BrokerCheck extends beyond traditional retail-facing brokers to include sell-side advisors such as investment bankers. BrokerCheck is meant to provide individuals with a free and easy way to research an investment professional, and the database includes information about licenses, employment history, and disciplinary history. The disciplinary history—in FINRA parlance, "dispute information"—includes written complaints, criminal conduct, arbitrations in which the broker is named as a party, litigation in which the broker is named as a party, arbitration awards, and civil judgments. An example of a BrokerCheck webpage is provided in Exhibit 2 of the Online Appendix. In this instance, the broker appeared to have a disclosure-free record until December 2012. However, this particular individual had expunged an infraction in 2011. After the expungement, he received three more disclosures and was later barred from the industry due to misconduct.

One concern with the disciplinary history provided on BrokerCheck is that much of it has not been independently verified. Although some complaints are confirmed, such as criminal or regulatory actions against the broker, the allegations made by private parties such as customers or employers are frequently unverified. For example, a written customer complaint against a broker can show up in BrokerCheck without third-party verification. The process leads to concerns that a completely erroneous allegation—such as a dispute against the wrong broker—may be recorded in BrokerCheck.

For this reason, there are concerns that the disciplinary information in BrokerCheck is over-inclusive and may penalize brokers unfairly. To address these concerns, FINRA allows brokers to

expunge their records. The rules governing expungement have been the subject of a great deal of controversy and have changed extensively over time (Lipner, 2013). Since April 2004, however, expungement of customer-related information has been governed by Rule 2080 (former NASD Rule 2130). This rule provides arbitrators with guidance on addressing expungement requests and specifies that expungement may only be awarded in cases where the initial case either (1) involved a claim that was "factually impossible or clearly erroneous," (2) involved a complaint where the registered person was not involved in the alleged conduct, or (3) the information in the claim is "false." To our knowledge, there is no FINRA rule governing expungement of non-customer related disputes that may arise, such as disputes between a broker and her firm.

An important question in this debate is why all brokers do not attempt to expunge their records. To answer this question, we cold-called 554 brokers in our sample. Of these, one hundred had successfully expunged an infraction and the remainder had non-expunged misconduct on their public records. Of these 554 brokers, only 19 agreed to speak with us—the remainder immediately hung up, did not return our calls, or hung up after comments such as "I don't know what an expungement is." However, these 19 provided consistent explanations for why brokers do not expunge. First, many brokers stated they were unaware of the process, or even that allegations of misconduct could be viewed publicly. Several were very surprised to receive our call, responding with comments such as "your call is the first time I've ever heard this" (referring to the expungement process). Second, of the brokers familiar with the process, many thought it was too costly. The cost mentioned ranged from $12,500 to $300,000, with most putting the cost around $25,000-$50,000 before settlement payments.[6] Finally, many of the brokers estimated their likelihood of success to be low, noting that FINRA considers expungement an exceptional remedy.

3. Methodology and Descriptive Statistics

Our analysis uses two datasets: (1) the BrokerCheck data, and (2) the Expungement data. The BrokerCheck data include an unbalanced panel of 1.23 million brokers available in FINRA's BrokerCheck database from 2007 to 2017. The Expungement data include 4,817 cases initiated from 2007 to 2016 requesting expungement for 6,660 offenses (some cases request expungement

[6] At the extreme, one broker estimated the cost to be $700K for an expungement. However, this same broker mentioned that he had prior difficulty over a "traffic stop" that we later determined to be assault on a police officer, so we question his credibility.

for multiple brokers or multiple offenses). After eliminating requests for which we could not locate the broker's CRD number, and those related to brokers no longer remaining in BrokerCheck, we have a total of 6,433 requests. Of these requests, 5,282 were resolved on the merits (in the remaining actions, the underlying claim was typically withdrawn or dismissed prior to when the arbitrator would have ruled on expungement, making the request for expungement moot).

When creating the Expungement data, we focused on requests filed from 2007 to 2016 for three reasons. First, FINRA was created through regulatory consolidation in July 2007, so recordkeeping becomes more consistent at this point. Second, many expungement cases brought after 2016 are yet to conclude. Third, BrokerCheck is meant to display records for a period of ten years, meaning that data over a decade old becomes subject to an increasingly severe selection bias. We provide detailed information on these two datasets below.

3.1. BrokerCheck Data

We scraped BrokerCheck in May 2018, so our BrokerCheck data contain information on all brokers and firms with records available on BrokerCheck in May 2018. This yields an unbalanced panel of 1.23 million brokers spanning the period between 2007 and 2017 (the data only include brokers in the year(s) they are actively registered broker-dealers). In total, there are roughly 7.7 million broker-year observations. If a broker switched firms midway through the year, he was assigned to the firm that he spent the most time at in any given year. If a broker was registered at two firms for an entire year, we randomly selected one firm for the year.

For each broker identified in BrokerCheck, we pulled the individual-level variables shown in Panel A of Table 1. The table presents characteristics of brokers who have applied for expungement, brokers who have not applied for expungement, and t-statistics comparing the two populations. There are clear differences between the populations. Brokers who apply for expungement have more years of experience, far more disciplinary history, and are more likely to be retail brokers (following Qureshi and Sokobin (2015), we define retail brokers as those who hold more than three state registrations). These brokers have also passed more exams, likely because they are retail brokers and must pass the exams required for the state(s) in which they operate. Notably, 85% of the brokers who have applied for expungement are dually registered as broker-dealers and investment advisers—significantly higher than the general population in

BrokerCheck. Generally speaking, investment advisers make investment decisions on behalf of their clients, whereas brokers execute trades they are told to execute. Therefore, investment advisers typically have greater opportunity to harm their clients.

Following Egan, Matvos, and Seru (2018, 2019a), we consider 6 of the 23 disclosure categories on BrokerCheck to be "misconduct." These six categories are as follows: Customer Dispute-Settled, Regulatory-Final, Employment Separation After Allegations, Customer Dispute - Award/Judgment, Criminal - Final Disposition, and Civil-Final. The number of allegations in each of the disclosure categories, including those categories we do not consider misconduct, is presented in Exhibit 3 of the Online Appendix. Many of the other disclosure categories do not necessarily relate to misconduct but may reflect personal history such as liens or bankruptcies. Further, by limiting to these six categories, we have greater confidence in the accuracy of the underlying complaint. For example, for an oral complaint to be included in the Customer Dispute – Settled category, the settlement must have exceeded $15,000.[7]

After completing the scrape of brokers, we generated a unique list of employers and scraped BrokerCheck for information on these firms. As shown in Panel B of Table 1, we identified 7,481 unique firms (roughly one-third were available in all years). The majority of firms in BrokerCheck do not employ expunged brokers, but those that do tend to be larger, more established, and more retail facing. This seems intuitive, as larger firms with more brokers—especially retail brokers—and longer lifespans have more opportunity for the brokers they employ to commit misconduct and expunge that misconduct.

3.2. Expungement Data

Our expungement data contain, as best possible, the complete set of all requests to expunge broker CRD information initiated from 2007 through 2016. We identified the expungement cases using FINRA's Arbitration Awards online database. First, we conducted a search of the Arbitration Awards online database using the following keywords: 'expungement,' '2080,' or '2130' (as discussed previously, Rules 2080 and 2130 govern FINRA's expungement procedures for

[7] Amendments in 2009 increased the reporting threshold to $15,000 from $10,000. However, this threshold only applies to oral complaints. Written complaints are included if the claim amount (not settlement amount) exceeds $5000.

customer-initiated disputes). This search yielded over 10,000 arbitration awards, each uniquely indexed by a FINRA Award ID. We scraped this list of FINRA Award IDs and the links to the relevant arbitration award PDFs. Second, using this list of Award ID numbers and PDF links, we downloaded the PDFs. As a first cut, we identified the 3,500 cases that contained '2080' or '2130' in the award section of the PDF. For the remaining PDFs, we identified those containing 'expungement' in the text of the award and hand-coded these PDFs to confirm they were actually related to expungement proceedings. After removing duplicates, we had 6,100 expungement arbitration awards in total.

To gain confidence in our sample and identify further expungements, we reached out to PIABA, an international bar association whose members represent investors in disputes with the securities industry. PIABA tracks expungements and shared with us data from 2007 to 2014 for the purposes of this study. Our initial data included 92% of the cases in the PIABA data, and we added the missing 227 observations.[8]

After restricting attention to cases initiated from 2007 through 2016, our search parameters yielded 4,817 arbitration awards corresponding to 6,660 unique (broker-offense) expungement requests. For each arbitration award, we identified the following variables: Date of award, date of claim, all brokers who applied for expungement, the justification for the expungement under Rule 2080 (False, Erroneous, or Not Involved), whether the case was heard by a panel or sole arbitrator, whether the expungement was successful, whether the case was settled, the hearing site of the case, whether the expungement was unopposed, settlement amounts (when disclosed), who initiated the case (broker, firm, or customer), and the date and type of the underlying infraction. (Detailed descriptions of these variables are provided in Exhibit 4 of the Online Appendix.) We scraped the variables initially, but hand-checked the coding. To categorize the underlying infraction, we used the categories provided in Table 3(a) of Egan, Matvos, and Seru (2019a) for customer-initiated cases and created similar categories for cases initiated by firms or brokers. The number of expungement requests by category is provided in Exhibit 5 of the Online Appendix. Particularly for the customer-initiated infractions, most instances of misconduct are those typically associated with an investment adviser rather than a broker-dealer (e.g., breach of fiduciary duty).

[8] Our sample included an additional 1,233 cases that were not included in the PIABA data. This discrepancy is largely because PIABA restricts attention to expungement cases involving stipulated awards or settled customer claims.

We identified additional detail about the broker using his or her name. First, as in Egan et al. (2018), we match the broker's name with the GenderChecker.com database to identify the broker's gender. If the broker's first name was not in the database or was unisex, we matched the middle name (or any other name excluding the broker's last name). Second, we ran the broker's name through NamePrism, an ethnicity classification tool (Junting et al., 2017). The tool classifies brokers into six categories: White, Black, API (Asian and Pacific Islander), AIAN (American Indian and Alaska Native), Multiple Race (more than two races), and Hispanic.

3.2.1. *Summary Information on Expunged Brokers*

Descriptive statistics for the Expungement data are presented in Tables 2 and 3, which contain additional information from the BrokerCheck data. To merge these datasets, we use the broker's CRD and the year that the arbitration award was adjudicated. Roughly 12% of the brokers who sought expungement were not employed at a FINRA-registered firm when the arbitration is decided, and we omit these brokers from our merged dataset. This reduces the sample to 5,578 expungement requests made by actively registered brokers. Of these, 4,011 were successful, 621 were unsuccessful, and the remainder were not decided on the merits (i.e., moot).

Panel A of Table 2 includes only brokers with expungable misconduct and examines which brokers file for expungement. The first set of columns reflects all brokers with expungable misconduct,[9] and the next set of columns compares the brokers by whether they filed for expungement. Some trends are evident. Retail-facing brokers and those with a prior successful expungement are more likely to file for expungement. Brokers from firms with more expungements are also more likely to apply, as are brokers from disciplined/taping firms. Disciplined firms are those that have been expelled from FINRA membership or have had their broker-dealer licenses revoked. Taping firms are those that, roughly stated, are required to tape conversations with customers because they have a significant association with a disciplined firm.

Panel B of Table 2 examines the brokers who succeeded on expungement requests. As in Panel A, we show the mean, median, and standard deviation for each relevant variable, and present

[9] Of the six categories of "misconduct," three can be expunged: Customer Dispute - Settled, Employment Separation After Allegations, and Customer Dispute - Award / Judgment. See Frequently Asked Questions about FINRA Rule 2080 (Expungement), available at https://www.finra.org/registration-exams-ce/classic-crd/faq/finra-rule-2080-frequently-asked-questions (last accessed on January 17, 2020).

these statistics conditional on whether the expungement was successful. Certain characteristics are associated with success. Brokers are more likely to succeed if the case is not opposed, the broker has settled with the aggrieved party, and the broker has a prior successful expungement. Brokers from larger firms—and firms without disciplinary history—are also more likely to succeed. In sum, Table 2 shows there are significant selection issues with regard to brokers who request and receive expungement that need to be addressed to estimate the causal effect of expungement.

Table 3 presents information on the brokerage houses with the most expunged brokers (only firms with one hundred or more brokers are included, but over 98% of brokers who file for expungement are from firms with one hundred or more brokers). Column (1) presents the firms with the greatest absolute number of expungements. Column (2) presents the firms with the greatest number of expungements relative to total misconducts. Column (3) presents the firms with the highest percentage of expungements relative to total brokers. Column (4) presents the firms with the highest percentage of expungements relative to retail brokers (as discussed previously, retail brokers are more likely to have misconduct on their records).

The most notable finding is that 12 of the 36 unique firms in Table 3 are no longer operating. Four firms, Blackbook Capital, LLC, NSM Securities, RW Towt, and iTRADEdirect.com, have been expelled from FINRA membership. And FINRA has terminated the registrations for another two of these firms, Lighthouse Capital Corporation and Rockwell Global Capital LLC. Finally, another six are no longer registered (Accelerated Capital Group, Calvert Investment Distributors, Inc., Jefferies Bache Securities, LLC, Newbury Street Capital, RP Capital LLC, and The Delta Company). One explanation is that firms facing severe disciplinary action or a lapse in registration encourage their brokers to expunge their records to present a better image. Another possibility is that brokers at these firms want to clean their records because they expect to soon look for other employment.

3.2.2. *Summary Information on the Expungement Process*

Further descriptive statistics are presented in Figures 1 through 3. Figure 1 presents the number of moot, successful, and unsuccessful expungement awards by year and shows that over 80% of expungements decided on the merits are successful in each year from 2007 to 2016 (including the moot requests as part of the denominator, roughly 70% of requests are successful). Figure 2 presents the number of brokers who sought multiple expungements during our sample

period and shows that roughly 6% of brokers (among those who requested expungement at least once in our sample) sought two expungements, and 4% sought three or more expungements (at the extreme, one broker requested expungement 39 times during our sample period). Further restricting to the set of brokers whose first expungement attempt is successful, we find that 10% request expungement again. Finally, Figure 3 shows the mean and median net settlement for all non-zero, customer-related arbitrations requesting an expungement by year (the net settlement value reflects the difference between what the customer was due to receive minus what she was required to pay, in the few rare instances where the customer was required to compensate the broker for infractions committed by the customer). Although the figure should be interpreted cautiously as we were only able to identify the settlement amount in roughly one-quarter of cases, the settlement values are notable. In all years, the mean settlement exceeded $200K, suggesting that the underlying claims had some validity. If we include the additional cases where we identified a $0 settlement, the mean settlement continues to exceed $68K in all years.

4. Empirical Analysis

This section presents our evidence on the effect of expungement on recidivism and career outcomes. Both the descriptive regressions and our IV analysis are based on an unbalanced panel of BrokerCheck data that is merged with the Expungement data. We keep only one observation per broker per year, meaning that we include only one expungement per year if a broker has multiple expungements in the same year. The expungement included is randomly chosen.

4.1. Descriptive Analysis on Expungement and Recidivism

As a preliminary inquiry, we provide descriptive analysis on the relationship between expungement and future misconduct. Figure 4 plots the conditional probabilities of future misconduct and shows that brokers who are granted expungement have an elevated probability of misconduct throughout their careers. Concretely, we estimate what fraction of brokers with a misconduct or expungement at time $t=0$ record a future misconduct at $t=1,2,3...8$ (future misconduct includes misconduct in BrokerCheck and expunged misconduct). We limit this analysis to eight years (spanning 2009-2017) because we only observe expungements claimed from 2007 onward, and cases typically take 1.5 years to resolve. We also drop observations where a broker records both an expungement and an unrelated misconduct in the same year.

Figure 4 illustrates these conditional probabilities relative to the baseline (unconditional) misconduct rate (0.70%). After one year, 5.81% brokers with a successful expungement record a misconduct—more than eight times the baseline rate. Notably, these elevated misconduct rates are persistent. In the sixth year following an expungement, 3% of brokers with a successful expungement re-offend. This is 4.3 times the baseline rate and comparable to the conditional probabilities for those with a prior misconduct (3.15%). These long-term "effects" suggest that the association between expungement and recidivism is not driven by short-term idiosyncrasies (e.g., same underlying offense recorded as multiple misconducts in different years).

Table 4 formalizes this descriptive analysis in a regression setting. Consider the probability that broker *i*, at firm *j*, in county *c* is reprimanded for misconduct at time *t*. We estimate the following linear probability model:

$$
\begin{aligned}
(1)\ Misconduct_{ijct} &= \beta_0 + \beta_1 Prior\ S.Expungement_{ijct} + \beta_2 Prior\ Misconduct_{ijct} \\
&+ \beta_3 Prior\ S.Expungement_{ijct} \times Prior\ Misconduct_{ijct} \\
&+ \beta_4 Prior\ U.Expungement_{ijct} \times Prior\ Misconduct_{ijct} \\
&+ \beta_5 Prior\ S.Expungement_{ijct} \times Prior\ U.Expungement_{ijct} \\
&\times Prior\ Misconduct_{ijct} + \beta X_{it} + \mu_{jct} + \epsilon_{ijct}
\end{aligned}
$$

The dependent variable $Misconduct_{ijct}$ is a dummy variable that reflects whether the broker received one or more allegations of misconduct (including successfully expunged misconduct) at time *t.* $Prior\ S.Expungement_{ijct}$, the main independent variable of interest, is a dummy variable indicating whether the broker had a successful expungement prior to time *t*. The other independent variable $Prior\ Misconduct_{ijct}$ analogously captures whether the broker had a misconduct prior to time *t* (please note that the this variable captures brokers with prior unsuccessful expungements ***and*** those with prior misconduct that they did not attempt to expunge). The inclusion of interaction terms (including with $Prior\ U.Expungement_{ijct}$) means that β_1 is identified using brokers with no prior misconduct or prior unsuccessful expungement at time *t* and thus reflects the pure "effect" of a successful expungement (it is of course possible for the same broker to have both a prior expungement and a prior misconduct). Some specifications include controls for the broker's gender, years of experience, and qualifications X_{it}, and/or firm-year-county fixed effects μ_{jct}. Standard error are clustered by firm in all columns.

On paper, brokers with a prior successful expungement and no other prior misconduct (or prior unsuccessful expungement) look like "clean" brokers with no misconduct. And if they were no more likely to offend than brokers without misconduct, we would expect to find $\beta_1 = 0$. Instead, the coefficient in column (1) is 2.3 percentage points.[10] Given a baseline misconduct rate of 0.70 percentage points, this implies that brokers with a prior successful expungement are 3.3 times (2.3 + 0.70 / 0.70) as likely to engage in future misconduct as the average broker in any given year. These elevated misconduct probabilities remain when comparing successfully expunged brokers to "clean" brokers within a specific branch of a firm in any year. Table 4 also shows that the recidivism rates of brokers with prior unsuccessful expungements are not significantly different from those with prior misconducts, who re-offend at 6.2 (5.2 + 0.70 / 0.70) times the rate of the average broker.

Simply noting a positive association between expungement and recidivism is not sufficient to conclude that the expungement system is not working as intended. For example, a well-functioning expungement process could generate a positive association because of the successful expungement of marginal misconduct. Imagine that bad behavior is ranked from 0 to 10. Anything over 5 should be classified as misconduct, whereas anything below 5 should be expunged. Under a well-functioning process, a 4 would be expunged—but that broker would be more likely to reoffend than a 0 (assuming that past malfeasance predicts future malfeasance). However, taken together, the magnitude and persistence of the descriptive analyses presented in Figure 4 and Table 4 cast doubt on whether arbitrators are striking the right balance between incorrectly classifying someone as "crooked" versus erasing a prior instance of misconduct.

4.2. Descriptive Analysis on Expungement and Career Outcomes

We next examine expungement and long-term career outcomes in Table 5. Panel A provides summary statistics, and Panels B, C, and D present regressions. The first two columns of Panel A use the full sample of brokers and show that brokers with successful expungements are more likely to maintain their current employment in the following year relative to brokers with unsuccessful expungements (88% vs. 81%). Further, if these brokers do leave their current firm,

[10] Without the interaction terms, the coefficient on prior successful expungement is 2.9 percentage points. This combines the "pure" expungement effect on recidivism with the effect of having both a prior misconduct and prior expungement.

they are more likely to join a different firm as a registered broker-dealer within the next year (71% vs. 48%)—and they are more likely to join a firm with a lower misconduct rate, where the misconduct rate is defined as the average number of misconducts (including expunged misconducts) per retail broker per year. The final two columns include only the subset of "one-misconduct" brokers (i.e., the subset of brokers who would appear "clean" after an expungement). We separately examine this subset because the effects of expungement—and incentives to apply for expungement—are likely to be greatest for this subsample. Indeed, the trends are generally similar, but the successfully expunged one-misconduct brokers are far more likely to join a larger firm.

$$(2)\ Employment\ Outcome_{ijt} = \beta_o + \beta_1 Successful\ Expungement_{t-1} + \beta X_{it} + \epsilon_{ijt}$$

Using equation (2), Panel B of Table 5 formalizes the analysis in Panel A and presents a regression controlling for observable broker characteristics. All control variables are defined in the Appendix, and standard errors are clustered by firm in this panel and the subsequent panels. The analysis shows that brokers who receive a successful expungement are 7 percentage points less likely to leave their firm the following year, and 21 percentage points more likely to re-register with a new firm conditional on leaving. Panel C of Table 5 repeats this analysis, but restricts the sample to the subset of brokers with one misconduct. Interestingly, the brokers who receive successful expungements are no more likely to leave the firm or to be rehired (although the null result may be due to a lack of power). However, conditional on leaving, the successfully expunged one-misconduct brokers are significantly more likely to be hired by a larger firm. Finally, Panel D restricts the set of successful expungements to only those classified by as "erroneous" under FINRA Rule 2080 (i.e., the arbitrator determined that the initial infraction was clearly erroneous). These expungements theoretically represent the weakest claims of misconduct. Panel D shows that the positive career consequences are stronger for this subset of expungements, suggesting the benefits of expungement may be greater for those who remove the weakest claims (in unreported tests, we compare the coefficients from Panel D to those in Panel B and find that the difference is significant at the 10% level).

Using the sample of one-misconduct brokers, Figure 5 provides further evidence that brokers with successful expungements have better career outcomes than those with unsuccessful

expungements—and that there is likely significant selection in the brokers who apply for expungement, as they appear to be those who want to remain in the industry. The figure shows the non-parametric out of industry survival curves for all separations preceded by an expungement award in the previous year. It suggests that successful expungement reduces the length of time spent out of the industry after leaving one's firm. Brokers who do not attempt expungement experience the longest out-of-industry spells. Interestingly, however, brokers with unsuccessful expungements have shorter out-of-industry spells than those who do not apply for expungement. In sum, the figure suggests that expungement improves career prospects, but also highlights selection in the brokers who apply for expungement.

Although our preliminary analysis suggests that successful expungement improves long-term career outcomes, there are two obvious concerns with this analysis. First, the trends only describe careers of brokers who remain registered brokers. It is unclear what happens to the brokers who exit the BrokerCheck database. Second, as highlighted by Table 2 and Figure 5, there is significant selection in the brokers who request—and receive—expungement. We address these questions as best possible in Table 6 and, later, using our instrumental variable analysis.

Table 6 presents descriptive data on brokers who exit the BrokerCheck database by reviewing employment history for 1,515 randomly selected brokers who applied for expungement and experienced at least one employment separation. For the observations with missing employment information, we hand-collect the information as best possible. The table summarizes the post-separation outcomes for this sample of brokers and shows several trends. First, exiting the BrokerCheck database is often a negative career signal. In many instances, especially when brokers exited the database after expungements, we could find no employment records for these individuals and categorized them as "unknown". Presumably, they are not employed in a professional capacity. Second, brokers who cease employment as registered brokers often continue to work in finance—especially those brokers who exit BrokerCheck after an expungement. These brokers tend to fall into two groups. Some continue to work for FINRA-registered firms, despite that the individual is no longer a registered broker (individuals employed at registered brokerages may be exempt from FINRA registration if their tasks do not require that they be actively engaged in the investment banking or securities business). Others work solely as investment advisers rather than dually registered broker-dealer investment advisers (registered investment advisers are regulated primarily by the SEC rather than FINRA and do not appear in BrokerCheck unless they

have been dually registered). As one such example, consider Kimon P. Daifotis—the individual who applied for expungement 39 times. He eventually dropped the broker-dealer title and worked as an investment adviser (he was the Chief Investment Officer for Fixed Income at Charles Schwab Investment Management) until he was barred from the industry by the SEC. Thus, although exits are a negative signal, many brokers who exit the database remain in the financial industry.

4.3. Instrumental Variable Analysis

Studying the effect of a successful expungement is inherently difficult. Brokers with successful expungements are presumably "less bad" than those with unsuccessful expungements, and the variables that predict a successful expungement are likely correlated with outcomes such as recidivism that we would like to test. A simple OLS regression will lead to biased estimates of the effect of expungement success even with the inclusion of fixed effects for broker and firm characteristics. Moreover, as noted in the preceding analysis on recidivism, a positive association between expungement and recidivism could be consistent with a well-functioning expungement process due to the successful expungement of marginal misconducts. A Bayesian would infer that a broker with an expunged misconduct has a higher propensity to reoffend than a broker with no expungement or misconduct history.

4.3.1. *Instrument Calculation*

To overcome these obstacles and identify the causal impact of expungement on broker outcomes, we use the randomly generated list of potential arbitrators as an instrumental variable that predicts the likelihood that the broker will succeed on his request for expungement. As stated earlier, FINRA assigns the initial list of potential arbitrators randomly, subject only to geographic restrictions. Although the list of potential arbitrators is not public information—only the arbitrator(s) selected are publicly known—FINRA provided us with this information for the expungement awards in our sample.[11] The use of randomized arbitrators as an instrument follows prior literature using randomized judges or investigators as an instrument, such as Kling (2006);

[11] FINRA provided us with anonymous IDs for each of the arbitrators selected for the panel as well as an indicator for whether the arbitrator was selected. We back out the arbitrators selected for the cases in our sample using this information, but we are unable to identify arbitrators who have not served on an expungement case in our sample.

Chang and Schoar (2013); Doyle (2007, 2008); Dobbie and Song (2015); Cheng, Severino, and Townsend (2019); Sampat and Williams (2019); and Dobbie, Goldin, and Yang (2018). The key identification assumption is that the randomly generated list of arbitrators will significantly affect the broker's likelihood of success but will not affect recidivism—except through the decision whether to grant the expungement.

We use this randomized list to create two instruments: the relative leniency of the (1) mean and (2) median arbitrator on the list, where "relative" is determined in comparison with other arbitrators in the same year and region. First, we calculate the leave-out success rate for each arbitrator in our sample. The leave-out success rate is the number of times each arbitrator has successfully awarded expungement relative to the number of expungement requests over which she has presided (excluding that particular award). The success rate is highly autocorrelated within arbitrators and ranges from 0% to 100% for arbitrators with five or more awards—that is, some arbitrators in our sample have denied every expungement and others have approved every expungement.[12] Moot expungement requests are not included in this calculation. Further, if the arbitrator has not presided over any expungement cases, we set the missing arbitrator history equal to the mean success rate in the region in that year.

Second, we merge the leave-out success rate for each arbitrator with the FINRA data identifying the potential arbitrators selected for the randomly assigned panel. Using those data, we calculate the mean (or median) success rate of the panel and subtract the annual mean leave-out success rate in the geographic region (region is defined as the hearing site of the arbitration).[13] This process allows us to generate *List Leniency (Mean)* and *List Leniency (Median),* our two instruments. Figure 6 plots the distribution of these instruments. Panel A plots *List Leniency (Mean)* and Panel B plots *List Leniency (Median)*.

[12] The variability in expungement rates across arbitrators suggests that they are swayed by their preferences—an intuition consistent with Choi, Fisch, and Pritchard (2010, 2014).

[13] FINRA determines the location of the arbitration, and we have 83 hearing sites in our sample. For cases involving investors, FINRA typically selects the location closest to the investor's residence at the time of the events giving rise to the dispute. See FINRA Rule 12213, available at https://www.finra.org/rules-guidance/rulebooks/finra-rules/12213 (last accessed on January 17, 2020).

4.3.2. *First Stage Regression*

Our first-stage regression is presented below as equation (3). S_{it} reflects whether the broker *i* successfully obtained an expungement, X_{it} is a set of control variables, and μ_{rt} is a region by award year fixed effect which addresses region-specific time variation. The variable Z_{jrt} is the instrument (i.e., the average leave-out success rate of the initial list of randomly assigned arbitrators *j* relative to the year *t* mean leave-out rate in region *r*).

$$(3)\ S_{it} = \beta_1 Z_{jrt} + \beta X_{it} + \mu_{rt} + \epsilon_{it}$$

The results of the first-stage regressions are shown in Panel A of Table 7. The first two columns show the results using *List Leniency (Mean)*, and the final two columns show the results using *List Leniency (Median)*. The results show that our calculated success rate is strongly positively correlated with the likelihood of success, and that this relationship is robust to the inclusion of control variables and to fixed effects.[14] To put the results in perspective, the table indicates that, for a 10 percentage point increase in the relative leniency of the arbitrator panel, the broker's likelihood of success increases by 9 to 14 percentage points.

Panels B and C of Table 7 provide additional tests of the strength of the instruments. Panel B provides comfort that panel assignment is random by showing that brokers who receive low success-rate panels are not systematically different from those who receive high success-rate panels. Both columns use the same specification to test whether our observable broker and firm characteristics are predictive of each instrument and show that arbitrators of different leniencies are assigned similar cases; F-tests of joint significance are not statistically significant.[15] Panel C

[14] There are fewer observations than in Table 2 because we restrict to expungement requests adjudicated on the merits (i.e., moot requests are omitted). Further, FINRA was unable to locate the deanonymized arbitrators for all awards in our sample. This leaves us with 4,031 observations, which is further reduced to 3,918 observations with full control variables. For the first-stage results, this is reduced to 3,793 observations (125 singletons). Although we include all non-moot expungements in the first stage (i.e., if a broker has multiple expungements in the same year, all such expungements are included), the results are very similar if we randomly select one expungement per broker. For the recidivism and career consequences tests, where we can have only one expungement award per year per broker, the sample is reduced to 3,561 observations. This is reduced to 3,266 observations after we restrict to brokers with expungements prior to 2017 (the sample for which we can observe consequences). From there, we have 3,135 observations in the regressions (131 singletons).

[15] Although the prior successful expungement variable is correlated with our IV variables, other authors using our same test for random assignment have also found that one or more variables is significantly correlated with the IV

provides an analysis of one testable implication of the monotonicity assumption—that the first-stage results should be positive for different subsets of brokers. Panel C divides brokers by gender, race, and employment characteristics. The coefficient on the list leniency variable remains positive across these subsamples.

A visual representation of the first-stage results in Panel A of Table 7 is provided in Figure 7. The figure plots the relationship between the residualized success rate and each instrument. To construct the binned scatter plots, we first regress an indicator for successful expungement on the year-region fixed effects. We then group observations into 20 bins and plot mean values of the x and y variables within each bin. To aid visual interpretation of the plot, we also show the best-fit line from an OLS regression. We note that the probability of successful expungement does not increase one-for-one with our measure of list leniency. This is likely driven by measurement error, which attenuates the effect toward zero, and cases where the parties do not select the mean (or median) arbitrator.

4.4. Effect of Expungement on Recidivism and Career Outcomes

The empirical strategy described above is implemented in Tables 8 and 9, which study the effect of expungement on recidivism and career outcomes, respectively. The generic second stage model is shown below in equation (4). $y_{i,T>t}$ is the outcome variable for broker *i* at time *T* after their expungement decision at time *t*, $\hat{S}_{it}$ is the predicted likelihood of success for each expungement award estimated from the first-stage model, X_{it} is the set of controls, and μ_{rt} is a region by award year fixed effect. In effect, β_1 represents the causal effect of expungement success on outcome $y_{i,T>t}$ (recidivism in Table 8 and career outcomes in Table 9).

$$(4)\ y_{i,T>t} = \beta_1 \widehat{S_{it}} + \beta X_{it} + \mu_{rt} + \epsilon_{it}$$

(see, e.g., Doyle (2008); Dobbie and Song (2015); Dobbie, Grönqvist, Niknami, Palme, and Priks (2019)—but have reported confidence in random assignment based on the F-test. Panel B contains more observations than Panel A because we examine the assignment of all expungement cases in our sample, including those later not resolved on the merits—i.e. "moot" cases. Further, we omit the case characteristics variables (e.g., settlement) as these are plausibly determined by the arbitrator. Following Dobbie, Goldin, and Yang (2018), standard errors in this panel are clustered by broker and lead arbitrator.

In Tables 8 and 9, columns (1) and (2) reflect the results using OLS, columns (3) and (4) reflect the 2SLS results using *List Leniency (Mean),* and columns (5) and (6) reflect the 2SLS results using *List Leniency (Median)*. The odd-numbered columns include only fixed effects and the even-numbered columns include full controls. All models include region-year fixed effects, and standard errors are clustered by firm.

Two conditions are required to interpret the 2SLS results as the local average treatment effect (LATE). First, the exclusion principle must hold, meaning that the arbitrator panel assignment only impacts broker recidivism and career outcomes through the probability of expungement. Although we think this assumption is reasonable, this condition is fundamentally untestable. Our results should be interpreted with this caveat in mind. Second, the monotonicity assumption must hold, meaning that the brokers expunged by a strict arbitrator would also be expunged by a lenient arbitrator, and brokers denied by a lenient arbitrator would also be denied by a strict arbitrator (as discussed earlier, Panel C of Table 7 provides an analysis of a testable prediction of this assumption). If the monotonicity assumption is violated, the 2SLS assumption would be a weighted average of marginal treatment effects, but the weights would not sum to one (Angrist, Imbens, and Rubin, 1996; Heckman and Vytlacil, 2005). Under these two conditions, we are able to identify the causal effect of successful expungement on the subset of brokers who are on the margin of expungement (the "compliers"). However, it is plausible that the causal effect of successful expungement differs for brokers who are always granted or always denied expungement by the arbitrators in our sample.

4.4.1. *Expungement and Recidivism*

Assuming the exclusion and monotonicity assumptions are met, Table 8 provides evidence that the LATE of successful expungement on recidivism is economically meaningful—and that this result is driven by repeat expungements. In Panel A, the dependent variable reflects the number of future years with allegations of misconduct (or expunged misconduct) after the initial expungement request. In Panel B, the dependent variable reflects the number of future years with successfully expunged misconduct. Both panels are restricted to brokers with expungements adjudicated prior to 2017 so that we can monitor at least one year of future outcomes.

In Panel A, the OLS results show a negative relationship between successful expungements and future recidivism, but the results flip in the 2SLS models. The coefficient on the predicted success variable is positive in all models and statistically significant in two models, indicating that marginal expunged brokers are significantly more likely to reoffend that those denied expungement. Using full controls, column (6) shows that the marginal expunged broker has 0.31 more years with misconduct than a broker denied expungement.

Panel B examines the effect of a successful expungement on future expungements (i.e., the dependent variable reflects only expunged misconduct rather than all misconduct). All six models are positive and statistically significant, heavily suggesting that the relationship between successful expungements and recidivism is driven by future expungements. With full controls, Panel B shows that the marginal expunged broker has 0.16 to 0.20 more years with misconduct than a broker denied expungement.

In additional analyses, we tested whether the increase in future expungements is driven by an increase in expungement requests, an increase in the likelihood of success, or both. These tests are presented in Exhibits 6 and 7 of the Online Appendix. Exhibit 6 replicates Table 8, but the dependent variable reflects the number of years with expungement requests (i.e., the dependent variables includes all expungement requests, as opposed to only those that were successful). Exhibit 7 examines the likelihood of future success conditional on (1) the outcome of the broker's initial expungement request, and (2) the relative leniency of the list of randomly assigned arbitrators. The results provide evidence that the increase in expunged misconduct in Panel B of Table 8 is driven by both factors.

As noted previously, there are several explanations for the finding that expungements increase recidivism—and, specifically, lead to future expungements. The first comes from behavioral economics literature. After non-desirable outcomes, people typically become more cautious (e.g., Laming, 1968; Rabbitt and Phillips, 1967; Rabbitt and Rodgers, 1977). By contrast, success arguably breeds overconfidence (Mizruchi, 1991; Gino and Pisano, 2011), which can lead to excessive risk-taking (e.g., Odean, 1998; Camerer and Lovallo, 1999). Moreover, psychologists have found that a higher incidence of unethical behavior is likely to occur if unethical decision-making is rewarded (Hegarty and Sims, 1978).

As applied to our setting, these behavioral findings suggest results consistent with what we find. Relative to those brokers denied expungement, brokers granted expungement may have

increased incidences of recidivism (and corresponding expungement requests) due to the following: (1) greater risk-taking with client assets, (2) overconfidence that the broker can obtain another expungement; and/or (3) more frequent incidences of unethical behavior, as the broker has received external signals that his initial behavior was appropriate. Finally, the literature on repeat players in litigation suggests that an expunged broker will be more likely to succeed on future expungement requests, as he will have learned from the process during the earlier case (Epstein, Landes, and Posner, 2013).

Second, these results are consistent with the incentives created by FINRA's accelerating sanctions regime. As noted previously, FINRA suggests that its adjudicators impose more severe sanctions when the broker in question has similar past misconduct and/or a pattern of causing investor harm (FINRA, 2019). This disciplinary regime could drive our results for two interconnected reasons. First, brokers denied expungement are on a shorter leash because they face increasing costs of misconduct. Second, brokers granted expungement are reset to a lower baseline, meaning they can expect the costs of engaging in misconduct to be lower. Presumably, this regime increases (reduces) the attractiveness of misconduct for those granted (denied) expungement.[16]

Finally, it is possible that expungement improves career outcomes, thus providing marginal expunged brokers with greater opportunity to commit misconduct because they are more likely to remain in the industry. Although we are not aware of any literature studying the removal of broker misconduct on career consequences, much literature finds that the addition of misconduct negatively affects career outcomes (e.g., Srinivasan, 2005; Fich and Shivdasani, 2007; Karpoff, Lee, and Martin, 2008; Egan, Matvos, and Seru, 2019a) and leads to "assortative mating" (e.g., Cook, Johnstone, Kowaleski, Minnis, and Sutherland, 2019). Therefore, we study whether successful expungements affect long-term career prospects in Table 9.

[16] To attempt to distinguish the "accelerating sanctions" and "behavioral" explanations, we limit the analysis in Table 8 to only the first expungement for each broker. In theory, the behavioral explanation implies that the likelihood of bad behavior grows exponentially with each expungement. By contrast, the accelerating sanctions argument seems to suggest that, after brokers are restored to the same baseline in terms of misconduct, the likelihood of bad behavior similarly returns to the same baseline—i.e., a broker who is granted expungement will have the same likelihood of misconduct as she did before the initial misconduct that was expunged. The results are reported in Exhibit 8 to the Online Appendix and show that the findings are directionally consistent but notably weaker in terms of magnitude and statistical significance. These results suggest that repeat expungements have an outsize effect on our results, which seems more consistent with the behavioral explanation—although it does not rule out the accelerating sanctions theory.

4.4.2. *Expungement and Career Outcomes*

Table 9 uses two proxies for career outcomes. Panel A studies whether successfully expunged brokers are more likely to separate from their employer at any point following the expungement. Panel B studies whether successfully expunged brokers are more likely to remain in the industry. As before, both panels are restricted to brokers with expungements adjudicated prior to 2017 so that we can monitor at least one year of future outcomes.

Panel A shows that successfully expunged brokers are more likely to remain employed at their current position, indicating that expungement has positive career outcomes for marginal expunged brokers. The dependent variable is set to 1 if the broker separated from his employer in any year after the award, either by registering with another firm or by exiting the database. The coefficients of interest are statistically significant at standard levels in four of the six models. Using full controls, column (4) indicates that, at the margin, a successfully expunged broker is 21 percentage points less likely to separate from her employer than a broker denied expungement.

Similarly, Panel B provides evidence that expungement increases the likelihood that a broker will remain in the industry. The dependent variable reflects the number of years the broker remains a FINRA-registered broker following the initial expungement. The coefficients of interest are statistically significant in four of the six models, and indicate that, at the margin, a successfully expunged broker enjoys 0.61 more years as a registered broker (with full controls).

On the whole, the results in Table 9 are consistent with our descriptive statistics and indicate that successful expungements improve career outcomes. On the one hand, the results are perhaps surprising. Current employers presumably know about the expungement, and future potential employers can ask about prior expungements during the application process.[17] Even if expungement removes information from regulators and consumers, it is not clear that expungement removes information from employers. Thus, it is not clear that expungement should affect employment outcomes.

On the other hand, there are explanations for why successful expungements would improve career prospects. First, at least some anecdotal evidence indicates that firms have different levels

[17] For example, a recent JP Morgan job application asked candidates the following question. "Are you currently or have you ever been, a named defendant/respondent in any civil lawsuits or arbitrations involving allegations of misconduct related to financial services?" This phrasing is broad enough that a broker with expunged misconduct should answer in the affirmative.

of tolerance for private misconduct (known only within the firm) and publicly known misconduct. A firm may be unwilling to employ a broker with a publicly tarnished reputation, but may be happy to employ a broker who committed the same infractions but has a "clean" public reputation.[18] Second, firms may learn from the expungement award itself. Indeed, in prior conversations with firms, some have indicated that think the expungement award provides additional information on the underlying infraction. If an expungement was denied, some firms view the underlying infraction as more severe than if it was granted (and vice versa).[19]

4.5. Robustness Tests

In Tables 10 and 11, we present the reduced form regressions of our outcome variables on our instruments. The generic model is presented below in equation (5). $y_{i,T>t}$ is the outcome variable for broker *i* at time *T* after their expungement decision at time *t*, Z_{jrt} is the instrument (i.e., the average leave-out success rate of the initial list of randomly assigned arbitrators j relative to the year *t* mean leave-out rate in region *r*), X_{it} is the set of controls, and μ_{rt} is a region by award year fixed effect. In effect, β_1 represents the causal effect of being randomly assigned a relatively more lenient list of arbitrators on outcome $y_{i,T>t}$. Table 10 presents the reduced form regressions with respect to recidivism, and Table 11 presents the reduced form regressions with respect to career outcomes. All models use OLS. As before, the results are presented using both *List Leniency (Mean)* and *List Leniency (Median)*.

[18] Exhibits 9 and 10 in the Online Appendix attempt to test this possibility empirically. In particular, Exhibit 9 splits the sample between firms with higher/lower than average misconduct rates. Assuming that firms with lower misconduct rates will be more concerned with their public reputation, we should see more severe career consequences for brokers at firms with lower misconduct rates. Following a similar intuition, Exhibit 10 examines the effect of expungement on separation, but splits the sample into one-misconduct brokers and multiple-misconduct brokers. Assuming the reputational effect of public misconduct will be greater for the one-misconduct brokers, we should see more severe career consequences for one-misconduct brokers. The results are presented first using OLS and followed by both IVs. To summarize, we do not find evidence that public reputation drives our results on the effect of expungement on separation, but we are hesitant to form definitive conclusions based on null results (particularly given the low number of observations).

[19] Exhibit 11 of the Online Appendix attempts to test this intuition. This Exhibit presents IV analysis on the effect of expungement on separation using (1) "erroneous" expungements, and (2) non-erroneous expungements (under Rule 2080, "erroneous" expungements theoretically represent the weakest claims of misconduct). Thus, if firms learn from the award, "erroneous" expungements should theoretically lead to lower rates of separation than expungements granted under other standards. The results are presented first using OLS and followed by both IVs. To summarize, although the magnitudes are consistent with this intuition, neither the F-tests nor the coefficients of interest are consistently significant (however, this may be due to a lack of power).

$$(5)\ y_{i,T>t} = \beta_1 Z_{jrt} + \beta X_{it} + \mu_{rt} + \epsilon_{it}$$

The results in Table 10 are consistent with those in Table 8. Columns (1) – (4) use the number of following years with an allegation of misconduct (or successfully expunged misconduct) as the dependent variable, and columns (5) – (8) use the number of following years with a successfully expunged misconduct as the dependent variable. The coefficient of interest is statistically significant in six of the eight models.

Similarly, the results in Table 11 are consistent with those in Table 9. Columns (1) – (3) show that brokers who happen to draw a relatively lenient list of arbitrators are less likely to separate from their employer (the coefficients of interest in columns (3) – (4) are negative but not statistically significant). The results indicate that, for a ten percentage point increase in the relative leniency of the arbitrator list, the broker is 1.01 to 3.42 percentage points less likely to separate from her employer. Similarly, the results in columns (5) – (8) are consistent with the 2SLS models in Panel B of Table 9 and show that brokers assigned to a lenient list of arbitrators are more likely to remain in the industry for longer periods.

5. Conclusion

We provide the most thorough analysis of the BrokerCheck expungement process, which allows brokers to remove allegations of misconduct from FINRA's public records. We show that brokers with prior expungements are 3.3 times as likely to engage in new misconduct as the average broker. This is consistent with the concerns of state regulators, who have argued that expungements impair their ability to monitor effectively by making it more difficult to identify potential bad actors. Further, using an instrumental variable based on FINRA's randomly generated list of potential arbitrators, we provide causal evidence on the effect of expungement. In particular, we show that expungement increases recidivism (measured as future allegations of misconduct or expunged misconduct). Further tests show that the increase in recidivism is driven by successfully expunged misconduct—in other words, successful expungements cause an increase in future expungements. Robustness tests indicate that the increase in future expungements is caused by an increase in expungement requests and a greater likelihood of success. Finally, we provide evidence that expungements improve career outcomes. Our descriptive analysis shows that brokers with successful expungements are more likely to remain

with their firm, and conditional on leaving the firm, to be rehired by another brokerage firm. The evidence from our IV analysis is consistent with the descriptive results, and shows that marginal expunged brokers are less likely to separate from their firm and more likely to remain FINRA-registered brokers going forward.

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Appendix. Variable Definitions.

Broker Characteristics	
Prior Successful Expungement	Dummy =1 if broker has a prior successful expungement
Prior Unsuccessful Expungement	Dummy =1 if broker has a prior unsuccessful expungement
Female	Dummy =1 if broker name is female (as matched to GenderChecker database)
Non-White	Dummy =1 if broker name is Black, API (Asian and Pacific Islander), AIAN (American Indian and Alaska Native), Multiple Race (more than two races), and Hispanic according to NamePrism (Junting et al., 2017)
Experience	Number of years since the broker first appeared in BrokerCheck as a registered broker dealer (divided by ten)
Total Qualifications	Number of exams passed among six specific qualifications (S63, S7, S6, S66, S65 and S24). These are the six most popular qualification exams taken by investment professionals (scraped from BrokerCheck)
Case Characteristics	
Settlement	Dollar value of net settlement amount disclosed in arbitration award (frequently unavailable)
Opposed	Dummy =1 if the arbitration award states that the customer was opposed to the expungement request
Intra Industry	Dummy =1 if a customer was involved in the case
Customer Initiated	Dummy =1 if the customer filed the complaint and was listed as the claimant on the FINRA award
Firm Characteristics	
Taping and/or Disciplined Firm	Dummy =1 if the firm has been disciplined by FINRA and/or is subject to taping rules under FINRA Rule 3170
Num. Brokers	Number of broker-dealers registered with the firm in each year
Total Expungements per Year	Number of expungement requests made by broker-dealers registered with the firm in each year
Total Misconducts per Year	Number of misconducts recorded by broker-dealers registered with the firm in each year
Arbitrator Characteristics	
Female	Dummy =1 if arbitrator name is female (as matched to GenderChecker database)
Panel of Arbitrators	Dummy =1 if the case was heard by a panel of arbitrators as opposed to a single arbitrator

Table 1 Summary statistics.

This table provides summary statistics on FINRA's BrokerCheck database from 2007 to 2017. Panel A provides summary statistics on the 1.23 million brokers available in the data, and Panel B provides summary statistics on the firms. In Panel A, observations are broker by year, and brokers are divided into two groups: Non-Expungement Brokers and Expungement Brokers. Expungement Brokers are those who filed a request for expungement at least once from 2007 to 2016. Non-Expungement brokers are analogously defined. In Panel B, observations are firm by year, and firms are divided into two groups according to whether any FINRA-registered brokers employed by the firm filed a request for expungement from 2007 to 2016. Firms dually registered as investment advisers were matched to Form ADV data spanning from 2007 to 2015. All firm and broker characteristics are defined in the appendix. The final column corresponds to a t-test for equality of means between the two groups. Statistical significance of 10%, 5%, and 1% is represented by *, **, and ***, respectively.

Panel A

	Non-Expungement Brokers						Expungement Brokers						t-test
	Obs.	Mean	Std. Dev.	Median	25th Pctl.	75th Pctl.	Obs.	Mean	Std. Dev.	Median	25th Pctl.	75th Pctl.	t
Broker Characteristics													
Experience (Years)	7,736,093	15.16	10.13	14.00	7.00	21.00	42,873	23.68	9.25	23.00	17.00	30.00	-190.12***
Retail Brokers	7,736,093	0.36	0.48	0.00	0.00	1.00	42,873	0.72	0.45	1.00	0.00	1.00	-161.23***
Non-White	7,736,093	0.10	0.30	0.00	0.00	0.00	42,873	0.07	0.25	0.00	0.00	0.00	31.40***
Registration													
Investment Adviser	7,736,093	0.48	0.50	0.00	0.00	1.00	42,873	0.85	0.36	1.00	1.00	1.00	-215.81***
Barred	7,736,093	0.00	0.05	0.00	0.00	0.00	42,873	0.01	0.10	0.00	0.00	0.00	-15.99***
Disclosures													
Disclosure (flow in one year)	7,736,093	0.02	0.13	0.00	0.00	0.00	42,873	0.09	0.28	0.00	0.00	0.00	-51.42***
Misconduct (flow in one year)	7,736,093	0.01	0.08	0.00	0.00	0.00	42,873	0.05	0.23	0.00	0.00	0.00	-43.76***
Expungement (flow in one year)	7,736,093	0.00	0.00	0.00	0.00	0.00	42,873	0.10	0.30	0.00	0.00	0.00	-67.98***
Disclosure (stock)	7,736,093	0.12	0.32	0.00	0.00	0.00	42,873	0.48	0.50	0.00	0.00	1.00	-151.22***
Misconduct (stock)	7,736,093	0.05	0.21	0.00	0.00	0.00	42,873	0.35	0.48	0.00	0.00	1.00	-132.11***
Expungements between 2007-2017	7,736,093	0.00	0.00	0.00	0.00	0.00	42,873	1.00	0.04	1.00	1.00	1.00	-5674.83***
Disclosure (stock - including pre-2007)	7,736,093	0.17	0.38	0.00	0.00	0.00	42,873	0.59	0.49	1.00	0.00	1.00	-177.75***
Misconduct (stock - including pre-2007)	7,736,093	0.09	0.29	0.00	0.00	0.00	42,873	0.45	0.50	0.00	0.00	1.00	-148.38***
Exams and Qulifications													
Num. Qualifications	7,736,093	2.95	1.38	3.00	2.00	4.00	42,873	4.01	1.55	4.00	3.00	5.00	-141.10***
Uniform Sec. Agent St. Law (63)	7,736,093	0.76	0.43	1.00	1.00	1.00	42,873	0.86	0.35	1.00	1.00	1.00	-55.32***
General Sec. Rep (7)	7,736,093	0.69	0.46	1.00	0.00	1.00	42,873	0.93	0.25	1.00	1.00	1.00	-195.39***
Inv. Co. Products (Rep). (6)	7,736,093	0.39	0.49	0.00	0.00	1.00	42,873	0.16	0.36	0.00	0.00	0.00	132.96***
Uniform Combined St. Law (66)	7,736,093	0.24	0.43	0.00	0.00	0.00	42,873	0.28	0.45	0.00	0.00	1.00	-19.70***
Uniform Inv. Adviser Law (65)	7,736,093	0.21	0.41	0.00	0.00	0.00	42,873	0.50	0.50	0.00	0.00	1.00	-119.37***
General Sec. Principal (24)	7,736,093	0.16	0.37	0.00	0.00	0.00	42,873	0.25	0.43	0.00	0.00	1.00	-43.53***
Observations	7,736,093						42,873						7,778,966

Panel B

	Firms without Expungement Attempts					Firms with Expungement Attempts					t-test
	Obs.	Num. Firms	Mean	Std. Dev.	Median	Obs.	Num. Firms	Mean	Std. Dev.	Median	t
BrokerCheck Data											
Investment Adviser	52,134	7,122	0.20	0.40	0.00	679	359	0.64	0.48	1.00	-24.15***
Affiliated w/ Fin. Inst.	52,134	7,122	0.39	0.49	0.00	679	359	0.68	0.47	1.00	-16.33***
Firm Age	52,092	7,105	21.33	12.89	18.00	679	359	29.80	20.08	25.00	-10.96***
Num. Business Lines	52,130	7,120	3.85	4.53	2.00	679	359	11.28	7.88	13.00	-24.51***
Num. Advisers	52,134	7,122	101.68	698.81	9.00	679	359	3649.15	7113.28	543.00	-12.99***
Firm Employee Misconduct (flow in one year)	52,134	7,122	0.01	0.05	0.00	679	359	0.04	0.08	0.01	-9.93***
Firm Employee Misconduct (stock - including pre-2007)	52,134	7,122	0.13	0.20	0.04	679	359	0.23	0.16	0.17	-15.15***
Active	52,134	7,122	0.67	0.47	1.00	679	359	0.75	0.43	1.00	-4.94***
Num. States	52,130	7,120	15.76	20.34	3.00	679	359	37.48	23.05	52.00	-24.43***
Expelled Firm	52,134	7,122	0.02	0.15	0.00	679	359	0.07	0.26	0.00	-4.79***
Form ADV Data											
Retail Brokers	3,894	727	0.83	0.37	1.00	342	149	0.97	0.17	1.00	-12.54***
Number of Accounts	3,660	686	5687.23	32331.93	603.00	329	142	173014.98	352116.59	15309.00	-8.62***
Assets Under Management ($ millions)	3,660	686	2678.11	11319.26	258.08	329	142	42217.62	89555.25	4092.58	-8.00***
Compensation/ Fee Structure											
Hourly	3,894	727	0.45	0.50	0.00	342	149	0.61	0.49	1.00	-5.73***
Fixed Fee	3,894	727	0.58	0.49	1.00	342	149	0.84	0.37	1.00	-12.20***
Commission	3,894	727	0.43	0.50	0.00	342	149	0.64	0.48	1.00	-7.45***
Performance	3,894	727	0.11	0.31	0.00	342	149	0.12	0.32	0.00	-0.52
Observations	52,134					679					52,813

Table 2 Summary statistics.

This table provides summary statistics on the brokers who apply for expungement. Panel A uses the full set of brokers with expungement-eligible misconduct. Observations are broker by year, and brokers are divided into two groups: (1) those who requested expungement at least once, and (2) those who never requested expungement. Panel B includes only brokers who applied for expungement. Observations are broker by request, and the final columns divide these requests by whether they are successful or unsuccessful (i.e., the expungement is approved or denied). The final column corresponds to a t-test for equality of means between the two groups. The number of successful and unsuccessful expungements does not sum to the number of total expungements because there are 946 moot expungement requests (i.e., expungement requests that were not resolved on the merits). All broker characteristics are defined in the appendix. Statistical significance of 10%, 5%, and 1% is represented by *, **, and ***, respectively.

Panel A

	Brokers with Expungement-Eligible Misconducts				Attempted Expungement				Did Not Attempt Expungement				t-test
	Obs.	Mean	Std. Dev.	Median	Obs.	Mean	Std. Dev.	Median	Obs.	Mean	Std. Dev.	Median	t
Broker Characteristics													
Experience (Years)	334,398	20.612	10.49	20.000	42,851	23.683	9.25	23.000	291,547	20.160	10.59	19.000	65.30***
Retail Brokers	334,398	0.523	0.50	1.000	42,851	0.717	0.45	1.000	291,547	0.494	0.50	0.000	86.95***
Investment Adviser	334,398	0.763	0.43	1.000	42,851	0.851	0.36	1.000	291,547	0.750	0.43	1.000	46.10***
Barred	334,398	0.045	0.21	0.000	42,851	0.011	0.10	0.000	291,547	0.050	0.22	0.000	-36.99***
Prior Successful Expungement	334,398	0.038	0.19	0.000	42,851	0.298	0.46	0.000	291,547	0.000	0.01	0.000	351.27***
Gender													
Female	321,779	0.137	0.34	0.000	41,656	0.129	0.34	0.000	280,123	0.139	0.35	0.000	-5.31***
Ethnicity													
White	334,398	0.907	0.29	1.000	42,851	0.935	0.25	1.000	291,547	0.903	0.30	1.000	21.21***
Black	334,398	0.003	0.05	0.000	42,851	0.002	0.04	0.000	291,547	0.003	0.06	0.000	-3.79***
Asian Pacific Islander	334,398	0.038	0.19	0.000	42,851	0.020	0.14	0.000	291,547	0.040	0.20	0.000	-20.94***
Hispanic	334,398	0.050	0.22	0.000	42,851	0.044	0.20	0.000	291,547	0.051	0.22	0.000	-6.60***
Firm Characteristics													
Num. Brokers	334,398	10678.773	11119.57	5967.000	42,851	12354.543	11906.24	9062.000	291,547	10432.472	10977.68	5815.000	33.47***
Num. Retail Brokers	334,398	5575.346	6838.23	1995.000	42,851	7250.230	7538.22	3488.000	291,547	5329.175	6694.00	1876.000	54.54***
Taping and/or Disciplined Firm	334,398	0.004	0.06	0.000	42,851	0.007	0.08	0.000	291,547	0.004	0.06	0.000	8.29***
Investment Adviser	334,398	0.806	0.40	1.000	42,851	0.809	0.39	1.000	291,547	0.806	0.40	1.000	1.28
Total Expungements per Year (at this Firm)	334,398	117.688	171.43	15.000	42,851	167.204	189.27	58.000	291,547	110.411	167.42	14.000	64.43***
Total Misconducts per Year (at this Firm)	334,398	114.471	149.46	44.000	42,851	132.146	158.41	64.000	291,547	111.873	147.92	42.000	26.24***
Observations	334,398				42,851				291,547				334,398

Panel B

	All Expungements				Successful				Unsuccessful				t-test
	Obs.	Mean	Std. Dev.	Median	Obs.	Mean	Std. Dev.	Median	Obs.	Mean	Std. Dev.	Median	t
Broker Characteristics													
Barred	5,578	0.013	0.11	0.000	4,011	0.006	0.08	0.000	621	0.052	0.22	0.000	-8.90***
Prior Successful Expungement	5,578	0.073	0.26	0.000	4,011	0.077	0.27	0.000	621	0.076	0.26	0.000	-0.31
Female	5,440	0.125	0.33	0.000	3,904	0.129	0.34	0.000	608	0.107	0.31	0.000	1.40
Ethnicity													
White	5,578	0.933	0.25	1.000	4,011	0.936	0.24	1.000	621	0.928	0.26	1.000	0.63
Black	5,578	0.002	0.04	0.000	4,011	0.002	0.04	0.000	621	0.002	0.04	0.000	0.22
Asian Pacific Islander	5,578	0.018	0.13	0.000	4,011	0.014	0.12	0.000	621	0.034	0.18	0.000	-3.17**
Hispanic	5,578	0.047	0.21	0.000	4,011	0.048	0.21	0.000	621	0.037	0.19	0.000	1.20
Arbitration Characteristics													
Num. Brokers Per Case	5,578	1.905	2.14	1.000	4,011	1.895	2.32	1.000	621	1.705	1.35	1.000	2.48*
Panel of Arbitrators	5,576	0.770	0.42	1.000	4,011	0.772	0.42	1.000	621	0.773	0.42	1.000	-0.21
Opposed	5,578	0.429	0.50	0.000	4,011	0.277	0.45	0.000	621	0.749	0.43	1.000	-17.53***
Duration from Infraction to Claim (years)	335	5.779	4.38	5.000	304	5.822	4.45	5.000	9	5.222	2.68	4.000	0.39
Duration from Claim to Award (years)	5,555	1.389	0.81	1.000	3,988	1.383	0.79	1.000	621	1.435	0.89	1.000	-1.49
Justification for Expungement													
False	5,578	0.390	0.49	0.000	4,011	0.542	0.50	1.000	621	0.000	0.00	0.000	22.03***
Involved	5,578	0.287	0.45	0.000	4,011	0.399	0.49	0.000	621	0.000	0.00	0.000	17.19***
Erroneous	5,578	0.301	0.46	0.000	4,011	0.418	0.49	0.000	621	0.000	0.00	0.000	17.82***
Truly Erroneous	5,578	0.052	0.22	0.000	4,011	0.071	0.26	0.000	621	0.003	0.06	0.000	5.81***
Settlement Characteristics													
Broker Contributes to Settlement	5,578	0.032	0.17	0.000	4,011	0.016	0.12	0.000	621	0.145	0.35	0.000	-17.61***
Firm Contributes	5,578	0.151	0.36	0.000	4,011	0.155	0.36	0.000	621	0.048	0.21	0.000	7.65***
Both Contribute	5,578	0.063	0.24	0.000	4,011	0.025	0.16	0.000	621	0.341	0.47	0.000	-33.32***
Settlement	5,573	0.683	0.47	1.000	4,006	0.778	0.42	1.000	621	0.538	0.50	1.000	8.32***
Settlement Amount	2,444	264647.242	2343418.55	0.000	1,381	83106.513	408436.77	0.000	373	606721.984	2713015.16	60000.000	-3.07**
Firm Characteristics													
Num. Brokers	5,578	11752.977	12119.90	6039.000	4,011	12745.540	12212.48	10342.000	621	8810.644	11507.56	1682.000	6.44***
Num. Retail Brokers	5,578	7223.038	7906.72	2749.000	4,011	7879.272	8030.50	4005.000	621	5342.813	7356.43	757.000	6.31***
Taping and/or Disciplined Firm	5,578	0.006	0.08	0.000	4,011	0.002	0.05	0.000	621	0.026	0.16	0.000	-6.71***
Total Expungements per Year (at this Firm)	5,578	171.288	192.27	60.000	4,011	185.713	193.53	80.000	621	130.691	184.25	15.000	5.60***
Total Misconducts per Year (at this Firm)	5,578	116.973	136.47	50.000	4,011	123.666	135.67	61.000	621	95.137	135.90	20.000	4.24***
Complaint Characteristics: Initiated By													
Customer Initiated	5,578	0.766	0.42	1.000	4,011	0.738	0.44	1.000	621	0.757	0.43	1.000	0.57
Broker Initiated	5,578	0.202	0.40	0.000	4,011	0.234	0.42	0.000	621	0.156	0.36	0.000	3.01**
Type of Violation - Customer Initiated													
Unsuitable	5,578	0.370	0.48	0.000	4,011	0.353	0.48	0.000	621	0.385	0.49	0.000	-0.83
Misrepresentation	5,578	0.424	0.49	0.000	4,011	0.413	0.49	0.000	621	0.414	0.49	0.000	0.56
Unauthorized	5,578	0.100	0.30	0.000	4,011	0.088	0.28	0.000	621	0.108	0.31	0.000	-0.69
Omission	5,578	0.215	0.41	0.000	4,011	0.215	0.41	0.000	621	0.185	0.39	0.000	1.90
Fee/Commision	5,578	0.024	0.15	0.000	4,011	0.023	0.15	0.000	621	0.016	0.13	0.000	1.42
Fraud	5,578	0.394	0.49	0.000	4,011	0.390	0.49	0.000	621	0.380	0.49	0.000	0.75
Fiduciary_duty	5,578	0.628	0.48	1.000	4,011	0.605	0.49	1.000	621	0.634	0.48	1.000	-0.37
Negligence	5,578	0.586	0.49	1.000	4,011	0.574	0.49	1.000	621	0.580	0.49	1.000	0.35
Risky	5,578	0.055	0.23	0.000	4,011	0.061	0.24	0.000	621	0.031	0.17	0.000	2.85**
Churning/Excessive Trading	5,578	0.061	0.24	0.000	4,011	0.046	0.21	0.000	621	0.092	0.29	0.000	-3.43***
Type of Violation - Firm/Broker Initiated													
Slander/Libel/Defamation	5,578	0.051	0.22	0.000	4,011	0.050	0.22	0.000	621	0.045	0.21	0.000	0.70
Interference	5,578	0.032	0.18	0.000	4,011	0.031	0.17	0.000	621	0.035	0.19	0.000	-0.44
Unfair Practices	5,578	0.015	0.12	0.000	4,011	0.012	0.11	0.000	621	0.035	0.19	0.000	-4.63***
Wrongful Termination	5,578	0.023	0.15	0.000	4,011	0.017	0.13	0.000	621	0.045	0.21	0.000	-3.91***
Other Employment Related	5,578	0.205	0.40	0.000	4,011	0.230	0.42	0.000	621	0.221	0.41	0.000	-1.00
Observations	5,578				4,011				621				5,578

Table 3 Brokerages with the greatest frequency of expungement.
This table ranks firms by the frequency of expungement after restricting to firms with more than 100 registered brokers. Column (1) ranks firms based on the number of expungement requests. Column (2) ranks firms by the ratio of expungement requests to total misconduct disclosures. Column (3) ranks firms by the ratio of expungement requests to the total number of registered brokers. Column (4) ranks firms by the ratio of expungement requests to the total number of registered retail brokers.

Greatest Number of Expungements	N	Highest % of Expungements Relative to Misconducts	p	Highest % of Expungements Relative to Total Brokers	p	Highest % of Expungements Relative to Retail Brokers	p
Morgan Stanley	572	Peachcap	100%	UBS Financial Services Incorporated Of Puerto Rico	6%	Ace Diversified Capital, Inc	100%
Wells Fargo Clearing Services, LLC	522	Candlewood Securities, LLC	100%	Rockwell Global Capital LLC	6%	RP Capital LLC	67%
Merrill Lynch, Pierce, Fenner & Smith Inc	437	Willis Securities, Inc	100%	RP Capital LLC	5%	Kensington Capital Corp	27%
UBS Financial Services Inc	404	Newbury Street Capital LP	100%	NSM Securities, Inc	4%	iTRADEdirect.com Corp	25%
Ameriprise Financial Services, Inc	175	Swedbank Securities US, LLC	100%	Portfolio Advisors Alliance, LLC	3%	The Delta Company	25%
LPL Financial LLC	151	Metropolitan Capital Investment Banc, Inc	100%	Network 1 Financial Securities Inc	3%	Accelerated Capital Group	23%
Edward Jones	115	Calvert Investment Distributors, Inc	100%	Accelerated Capital Group	3%	Lighthouse Capital Corporation	18%
Charles Schwab & Co, Inc	107	SC Distributors, LLC	50%	Peachcap	3%	MSC - BD, LLC	17%
Securities America, Inc	90	Jefferies Bache Securities, LLC	50%	iTRADEdirect.com Corp	3%	Blackbook Capital, LLC	17%
Stifel, Nicolaus & Company, Incorporated	80	Presidio Merchant Partners LLC	50%	First Standard Financial Company LLC	3%	RW Towt & Associates	17%

Table 4 Estimates of the relationship between successful expungements and future misconduct.
This table examines the relationship between expungement and recidivism through the linear probability model outlined in Eq 1. The dependent variable is a dummy variable set to 1 if the broker received one or more misconduct disclosures or successful expungements at time t. The independent variables capture whether the broker had an expungement and/or misconduct prior to time t. Observations are at the broker by year level. Columns 2 and 3 control for the broker's years of experience, gender, race, total qualifications. Column 3 also includes year-firm-county fixed effects. Standard errors are clustered by firm, and standard errors are in parentheses. Statistical significance of 10%, 5%, and 1% is represented by *, **, and ***, respectively.

	(1) Misconducts/Expungements this Year	(2) Misconducts/Expungements this Year	(3) Misconducts/Expungements this Year
Prior Successful Expungement=1	0.023***	0.020***	0.018***
	(0.002)	(0.002)	(0.002)
Prior Misconduct=1	0.052***	0.050***	0.042***
	(0.003)	(0.003)	(0.002)
Prior Successful Expungement=1 × Prior Misconduct=1	0.025**	0.025**	0.016**
	(0.012)	(0.012)	(0.008)
Prior Misconduct=1 × Prior Unsuccessful Expungement=1	0.014*	0.013	0.007
	(0.008)	(0.008)	(0.007)
Prior Misconduct=1 × Prior Unsuccessful Expungement=1 × Prior Successful Expungement=1	0.034	0.036	0.028
	(0.036)	(0.036)	(0.027)
Other Broker Characteristics			
Female		-0.003***	-0.003***
		(0.000)	(0.000)
Non-White		0.002***	0.000***
		(0.000)	(0.000)
Experience		0.001***	0.001***
		(0.000)	(0.000)
Total Qualifications		0.001***	0.001***
		(0.000)	(0.000)
Controls		Yes	Yes
Year × Region × Firm FE			Yes
Observations	7,778,966	7,420,784	6,920,583
Adj. R-Squared	0.008	0.009	0.058

Table 5 Estimates of the relationship between successful expungements and future career outcomes.
This table presents cross-sectional results on career outcomes for brokers in the year following an expungement award. Panel A presents descriptive statistics, and Panels B, C, and D present OLS regression results using the specification in Eq 2. The summary statistics in Panel A are presented first (in columns (1) and (2)) using the full sample of brokers, and second (in columns (3) and (4)) using brokers with only one misconduct in total (i.e., brokers who would appear "clean" after an expungement request). Within each category, statistics are presented separately for two categories of brokers: (1) those with successful expungements and (2) those with unsuccessful expungements. A broker remains with her firm if she is registered with the same firm in the year following her expungement award. A broker leaves his firm if he registers with a new firm ("Join a New Firm") or becomes unregistered ("Leave the Industry"). A broker joins a larger (smaller) firm if, conditional on joining a new firm, the new firm has more (fewer) brokers than his previous firm. If the new firm has more (fewer) than 100 brokers, the broker moved to a big (small) firm. Finally, the average firm misconduct rate is defined as the average number of allegations of misconduct (including expunged misconduct) per retail broker registered to a firm in a given year. Panels B-D present OLS regressions of these career outcomes controlling for observable broker characteristics. Panel B uses the full sample of brokers with expungement requests resolved on the merits, but restricts to one randomly selected expungement in a given year if there are multiple expungement requests. Panel C replicates the analysis in Panel B, but restricts the analysis to only the brokers with one misconduct. Panel D replicates the analysis in Panel B, but restricts the analysis to only the brokers with successful expungements classified as "erroneous" under FINRA Rule 2080. These "erroneous" expungements should reflect the weakest claims of misconduct. In Panels B, C and D, the control variables are the same as Table 4 and standard errors are clustered by firm and included in parentheses. Statistical significance of 10%, 5%, and 1% is represented by *, **, and ***, respectively.

Panel A

	All Misconduct		One Misconduct Sample	
	Unsuccessful Expungement	Successful Expungement	Unsuccessful Expungement	Successful Expungement
Remain with the Firm	81%	88%	87%	90%
Leave the Firm	19%	12%	13%	10%
Conditional on Leaving the Firm:				
Join a New Firm (within 1 year)	48%	71%	60%	73%
Leave the Industry	52%	29%	40%	27%
Conditional on Joining a Different Firm:				
Join a Larger Firm	47%	52%	27%	53%
Join a Smaller Firm	53%	48%	73%	47%
Join a Big Firm (>= 100 brokers)	81%	82%	87%	85%
Join a Small Firm (<100 brokers)	19%	18%	13%	15%
New Firms Properties:				
Avg. Misconduct Rate (misconducts plus expungements per retail broker per year)	0.10	0.06	0.06	0.04

Panel B

	(1) Leave Firm	(2) Join New Firm	(3) Larger Firm	(4) Big Firm	(5) Firm Avg. Misconduct Rate
Successful Expungement	-0.072***	0.211***	0.050	0.002	-0.034
	(0.020)	(0.060)	(0.081)	(0.066)	(0.021)
Female	0.002	-0.119*	0.152*	0.077	-0.013
	(0.016)	(0.065)	(0.078)	(0.062)	(0.026)
Non-White	0.008	0.004	-0.037	0.012	-0.007
	(0.026)	(0.082)	(0.119)	(0.090)	(0.020)
Experience	-0.042***	0.102***	-0.048	0.045*	-0.011
	(0.009)	(0.034)	(0.037)	(0.026)	(0.007)
Total Qualifications	-0.014*	-0.011	0.004	0.018	-0.005
	(0.008)	(0.030)	(0.038)	(0.034)	(0.010)
Constant	0.325***	0.321***	0.560***	0.658***	0.135***
	(0.047)	(0.105)	(0.137)	(0.131)	(0.043)
Observations	3,674	458	302	302	300
Adj. R-Squared	0.019	0.082	0.002	-0.001	0.005

Panel C

	(1) Leave Firm	(2) Join New Firm	(3) Larger Firm	(4) Big Firm	(5) Firm Avg. Misconduct Rate
Successful Expungement	-0.037	0.092	0.275**	-0.031	-0.022
	(0.026)	(0.101)	(0.137)	(0.091)	(0.017)
Female	0.013	-0.149*	0.253***	0.064	-0.013
	(0.019)	(0.081)	(0.090)	(0.076)	(0.011)
Non-White	-0.014	0.091	-0.137	0.207***	-0.014
	(0.036)	(0.150)	(0.169)	(0.053)	(0.010)
Experience	-0.033***	0.124***	-0.085*	0.055*	-0.005
	(0.011)	(0.035)	(0.047)	(0.030)	(0.004)
Total Qualifications	-0.025**	0.026	-0.044	-0.007	0.004
	(0.010)	(0.037)	(0.048)	(0.047)	(0.008)
Constant	0.279***	0.336**	0.536***	0.750***	0.064*
	(0.056)	(0.144)	(0.202)	(0.173)	(0.036)
Observations	1,927	197	141	141	139
Adj. R-Squared	0.013	0.081	0.061	-0.004	-0.013

Panel D

	(1) Leave Firm	(2) Join New Firm	(3) Larger Firm	(4) Big Firm	(5) Firm Avg. Misconduct Rate
Erroneous Success	-0.085***	0.214***	-0.027	0.027	-0.044**
	(0.022)	(0.069)	(0.098)	(0.072)	(0.020)
Female	-0.008	-0.218*	-0.099	0.012	-0.036
	(0.021)	(0.117)	(0.163)	(0.120)	(0.022)
Non-White	0.022	-0.015	0.002	-0.077	-0.000
	(0.039)	(0.106)	(0.168)	(0.140)	(0.031)
Experience	-0.047***	0.050	0.005	0.064*	-0.018***
	(0.012)	(0.042)	(0.058)	(0.034)	(0.006)
Total Qualifications	-0.015	-0.032	0.050	0.025	-0.011
	(0.011)	(0.047)	(0.060)	(0.050)	(0.010)
Constant	0.344***	0.504***	0.343*	0.609***	0.167***
	(0.055)	(0.146)	(0.181)	(0.178)	(0.044)
Observations	1,814	224	138	138	137
Adj. R-Squared	0.031	0.067	-0.028	0.000	0.081

Table 6 Career outcomes for brokers who exit the BrokerCheck database.
This table examines employment outcomes for a random sample of 1,515 brokers who applied for expungement and experienced at least one employment separation. Column (1) records the most popular destinations for brokers who switched roles prior to the expungement award. Column (2) records the most popular destinations for brokers who switched roles after a successful expungement award. Column (3) records the most popular destinations for brokers who switched roles after an unsuccessful expungement award.

	Career Switches Before Expungement Award		Career Switches After Successful Expungement Award		Career Switches After Unsuccessful Expungement Award	
	N	p	N	p	N	p
FINRA-Registered Firm in Registered Capacity	1,264	86%	411	67%	79	50%
FINRA-Registered Firm in Unregistered Capacity	30	2%	29	5%	7	4%
Non-Financial Company	19	1%	32	5%	8	5%
Non-Finra-Registered Financial Firm	38	3%	32	5%	16	10%
Non-Profit/Government	3	0%	4	1%	1	1%
Prison	2	0%	0	0%	0	0%
Retired	5	0%	1	0%	0	0%
Self-Employed	1	0%	3	0%	0	0%
Unemployed	1	0%	3	0%	0	0%
University	2	0%	3	0%	0	0%
Unknown	98	7%	89	15%	46	29%
Deceased	0	0%	2	0%	0	0%
Number of Unique Brokers	866		398		102	
Total Switches	1,463		609		157	

Table 7 Tests of instrument quality.

This table presents the first-stage results and robustness checks. Panel A presents the first-stage results for the two instruments: List Leniency (Mean) and List Leniency (Median). The instruments reflects the relative leniency of the randomly assigned list of potential arbitrators. The relative leniency of the arbitrator list is calculated as the mean (or median) leave-out success rate of all arbitrators on the list minus the mean annual success rate in the FINRA geographic region. Success rate is the number of successful expungement awards divided by the total number of expungement awards over which the arbitrator has presided. The dependent variable is equal to 1 if the expungement was successful. Standard errors are clustered by firm and included in parentheses. Panel B presents reduced form results testing the random assignment of arbitration panels. This panel (Panel B) contains more observations than Panel A because we examine the assignment of all expungement cases in our sample, including those later not resolved on the merits—i.e. "moot" cases. Columns (1) and (2) report estimates from an OLS regression of the two instruments on the set of broker and firm characteristics from Panel A. The p-value from an F-test of the joint significance of the variables listed in the rows is reported at the bottom of the table. All control variables are defined in the appendix, and standard errors are double-clustered by broker and lead arbitrator. All models include year-region fixed effects. Panel C presents the first-stage results separately by the following broker characteristics: gender, race, retail broker, years of experience, and number of qualifications. In line with the monotonicity assumption, we find that the coefficients are consistently positive and sizable in all subsamples. Statistical significance of 10%, 5%, and 1% is represented by *, **, and ***, respectively.

Panel A

	(1) Successful Expungement	(2) Successful Expungement	(3) Successful Expungement	(4) Successful Expungement
List Leniency, Mean	1.420***	1.308***		
	(0.107)	(0.089)		
List Leniency, Median			0.954***	0.924***
			(0.089)	(0.071)
Broker Characteristics				
Prior Successful Expungement		-0.030		-0.036*
		(0.021)		(0.021)
Prior Unsuccessful Expungement		-0.030		-0.026
		(0.052)		(0.050)
Female		0.027*		0.026*
		(0.015)		(0.015)
Non-White		-0.005		-0.007
		(0.028)		(0.029)
Experience		-0.001		-0.004
		(0.007)		(0.007)
Total Qualifications		-0.005		-0.005
		(0.008)		(0.008)
Settlement		0.038**		0.039**
		(0.018)		(0.019)
Opposed		-0.187***		-0.192***
		(0.017)		(0.017)
Intra Industry		-0.007		-0.016
		(0.027)		(0.027)
Customer Initiated		-0.016		-0.023
		(0.022)		(0.021)
Firm Characteristics				
Taping and/or Disciplined Firm		-0.204		-0.225
		(0.136)		(0.140)
Num. Brokers		0.000**		0.000***
		(0.000)		(0.000)
Total Expungements per Year		-0.000		-0.000
		(0.000)		(0.000)
Total Misconducts per Year		-0.000		-0.000
		(0.000)		(0.000)
Arbitrator Characteristics				
Female		0.001		-0.001
		(0.010)		(0.011)
Panel of Arbitrators		-0.055***		-0.074***
		(0.015)		(0.016)
Controls		Yes		Yes
Year × Region FE	Yes	Yes	Yes	Yes
Observations	3,793	3,793	3,793	3,793

Panel B

	(1) List Leniency, Mean	(2) List Leniency, Median
Broker Characteristics		
Prior Successful Expungement	0.009*	0.017***
	(0.005)	(0.005)
Prior Unsuccessful Expungement	-0.004	-0.006
	(0.008)	(0.011)
Female	0.004	0.004
	(0.004)	(0.005)
Non-White	-0.007	-0.008
	(0.005)	(0.006)
Experience	-0.002	0.001
	(0.001)	(0.002)
Total Qualifications	-0.000	-0.001
	(0.002)	(0.002)
Firm Characteristics		
Taping and/or Disciplined Firm	0.001	0.020
	(0.025)	(0.021)
Num. Brokers	0.000*	0.000
	(0.000)	(0.000)
Total Expungements per Year	-0.000	0.000
	(0.000)	(0.000)
Total Misconducts per Year	-0.000	-0.000
	(0.000)	(0.000)
Year × Region FE	Yes	Yes
Joint F-Test	0.176	0.143
Observations	4,564	4,564

Panel C

Sample Restriction	List Leniency, Mean		List Leniency, Median	
	(1)	(2)	(3)	(4)
Full Sample	1.576***	1.342***	1.066***	0.904***
	(0.109)	(0.103)	(0.096)	(0.090)
Male	1.580***	1.333***	1.095***	0.911***
	(0.122)	(0.116)	(0.109)	(0.102)
Female	1.774***	1.609***	1.106***	1.073***
	(0.363)	(0.351)	(0.356)	(0.322)
White	1.582***	1.350***	1.070***	0.911***
	(0.111)	(0.105)	(0.099)	(0.092)
Non-White	0.414	0.393	0.275	0.535
	(0.480)	(0.511)	(0.492)	(0.541)
>10 Years' Experience	1.547***	1.312***	1.058***	0.902***
	(0.114)	(0.106)	(0.103)	(0.095)
<= 10 Years' Experience	1.452*	1.253	0.902	0.694
	(0.753)	(0.795)	(0.602)	(0.584)
>3 Qualifications	1.963***	1.683***	1.209***	0.875**
	(0.388)	(0.392)	(0.390)	(0.379)
<= 3 Qualifications	1.550***	1.308***	1.111***	0.954***
	(0.112)	(0.102)	(0.101)	(0.091)
Controls		Yes		Yes
Year × Region FE	Yes	Yes	Yes	Yes

Table 8 IV estimates of the effect of expungement on recidivism.
This table shows the effect of a successful expungement on recidivism. In Panel A, the dependent variable reflects the number of future years with allegations of misconduct (including expunged misconduct) after the initial expungement request. In Panel B, the dependent variable reflects the number future years with successful expungements after the initial expungement request. Only brokers who applied for expungement prior to 2017 are included. Columns (1) and (2) reflect the OLS results. Columns (3)–(6) use 2SLS, where the instrument is the relative leniency of the randomly assigned list of potential arbitrators. The relative leniency of the arbitrator list is calculated as the mean (or median) leave-out success rate of all arbitrators on the list minus the mean annual success rate in the FINRA geographic region. Success rate is the number of successful expungement awards divided by the total number of expungement awards over which the arbitrator has presided. Columns (3) and (4) reflect the results using the first instrument: List Leniency (Mean) (the relative leniency of the mean arbitrator on the initial list). Columns (5) and (6) reflect the results using the second instrument: List Leniency (Median) (the relative leniency of the median arbitrator on the initial list). All control variables are defined in the appendix, and all models include region-year fixed effects. Standard errors are clustered by firm. Statistical significance of 10%, 5%, and 1% is represented by *, **, and ***, respectively.

Panel A

	OLS	OLS	2SLS	2SLS	2SLS	2SLS
	(1)	(2)	(3)	(4)	(5)	(6)
	Num. Yrs. w/ Misc.	Num. Yrs. w/ Misc.	Num. Yrs. w/ Misc.	Num. Yrs. w/ Misc.	Num. Yrs. w/ Misc.	Num. Yrs. w/ Misc.
Successful Expungement	-0.142**	-0.107**				
	(0.056)	(0.050)				
Predicted Success (using List Leniency, Mean)			0.048	0.042		
			(0.112)	(0.101)		
Predicted Success (using List Leniency, Median)					0.332**	0.307**
					(0.134)	(0.123)
Broker Characteristics						
Prior Successful Expungement		1.429***		1.434***		1.444***
		(0.112)		(0.111)		(0.109)
Prior Unsuccessful Expungement		1.320***		1.330***		1.349***
		(0.205)		(0.202)		(0.196)
Female		-0.030		-0.036		-0.046
		(0.049)		(0.050)		(0.050)
Non-White		0.126*		0.129*		0.135*
		(0.067)		(0.068)		(0.070)
Experience		0.028*		0.028*		0.029*
		(0.017)		(0.017)		(0.017)
Total Qualifications		0.006		0.006		0.008
		(0.020)		(0.020)		(0.020)
Case Characteristics						
Settlement		0.052		0.046		0.037
		(0.036)		(0.037)		(0.039)
Opposed		-0.017		0.013		0.065
		(0.034)		(0.039)		(0.040)
Intra Industry		-0.191*		-0.186*		-0.178
		(0.112)		(0.112)		(0.110)
Customer Initiated		-0.196*		-0.193*		-0.187*
		(0.108)		(0.107)		(0.105)
Firm Characteristics						
Taping and/or Disciplined Firm		1.001***		1.025***		1.067***
		(0.289)		(0.287)		(0.289)
Num. Brokers		-0.000***		-0.000***		-0.000***
		(0.000)		(0.000)		(0.000)
Total Expungements per Year		0.001		0.001		0.001
		(0.001)		(0.001)		(0.001)
Total Misconducts per Year		0.000		0.000		0.000
		(0.000)		(0.000)		(0.000)
Arbitrator Characteristics						
Female		0.024		0.023		0.021
		(0.018)		(0.018)		(0.018)
Panel of Arbitrators		-0.035		-0.033		-0.031
		(0.037)		(0.038)		(0.039)
Controls		Yes		Yes		Yes
Year × Region FE	Yes	Yes	Yes	Yes	Yes	Yes
Observations	3,135	3,135	3,135	3,135	3,135	3,135

Panel B

	OLS	OLS	2SLS	2SLS	2SLS	2SLS
	(1)	(2)	(3)	(4)	(5)	(6)
	Num. Yrs. w/ Exp.	Num. Yrs. w/ Exp.	Num. Yrs. w/ Exp.	Num. Yrs. w/ Exp.	Num. Yrs. w/ Exp.	Num. Yrs. w/ Exp.
Successful Expungement	0.103***	0.114***				
	(0.024)	(0.024)				
Predicted Success (using List Leniency, Mean)			0.201***	0.163***		
			(0.053)	(0.061)		
Predicted Success (using List Leniency, Median)					0.248***	0.198**
					(0.087)	(0.097)
Broker Characteristics						
Prior Successful Expungement		1.156***		1.157***		1.159***
		(0.098)		(0.098)		(0.098)
Prior Unsuccessful Expungement		0.663***		0.667***		0.669***
		(0.140)		(0.139)		(0.138)
Female		0.048		0.046		0.044
		(0.043)		(0.043)		(0.042)
Non-White		-0.038		-0.037		-0.036
		(0.026)		(0.026)		(0.026)
Experience		0.008		0.008		0.008
		(0.008)		(0.008)		(0.008)
Total Qualifications		0.018*		0.018*		0.018*
		(0.010)		(0.010)		(0.010)
Case Characteristics						
Settlement		0.008		0.006		0.005
		(0.023)		(0.023)		(0.024)
Opposed		-0.021		-0.012		-0.005
		(0.021)		(0.024)		(0.023)
Intra Industry		-0.095		-0.094		-0.093
		(0.092)		(0.092)		(0.092)
Customer Initiated		-0.121		-0.120		-0.119
		(0.095)		(0.095)		(0.095)
Firm Characteristics						
Taping and/or Disciplined Firm		0.280		0.288		0.294
		(0.273)		(0.273)		(0.271)
Num. Brokers		-0.000***		-0.000***		-0.000***
		(0.000)		(0.000)		(0.000)
Total Expungements per Year		0.000		0.000		0.000
		(0.001)		(0.001)		(0.001)
Total Misconducts per Year		0.000*		0.000*		0.000*
		(0.000)		(0.000)		(0.000)
Arbitrator Characteristics						
Female		0.005		0.005		0.004
		(0.012)		(0.012)		(0.012)
Panel of Arbitrators		-0.035*		-0.035*		-0.034*
		(0.019)		(0.019)		(0.019)
Controls		Yes		Yes		Yes
Year × Region FE	Yes	Yes	Yes	Yes	Yes	Yes
Observations	3,135	3,135	3,135	3,135	3,135	3,135

Table 9 IV estimates of the effect of expungement on future employment outcomes.
This table shows the effect of a successful expungement on career outcomes. In Panel A, the dependent variable is a dummy variable for whether the broker separated from her employer after the expungement request. In Panel B, the dependent variable captures the number of years the broker is registered after the expungement request. Only brokers with expungements adjudicated prior to 2017 are included. Columns (1) and (2) reflect the OLS results. Columns (3)–(6) use 2SLS, where the instrument is the relative leniency of the randomly assigned list of potential arbitrators. The relative leniency of the arbitrator list is calculated as the mean (or median) leave-out success rate of all arbitrators on the list minus the mean annual success rate in the FINRA geographic region. Success rate is the number of successful expungement awards divided by the total number of expungement awards over which the arbitrator has presided. Columns (3) and (4) reflect the results using the first instrument: List Leniency (Mean) (the relative leniency of the mean arbitrator on the initial list). Columns (5) and (6) reflect the results using the second instrument: List Leniency (Median) (the relative leniency of the median arbitrator on the initial list). All control variables are defined in the appendix, and all models include region-year fixed effects. Standard errors are clustered by firm. Statistical significance of 10%, 5%, and 1% is represented by *, **, and ***, respectively.

Panel A

	OLS	OLS	2SLS	2SLS	2SLS	2SLS
	(1)	(2)	(3)	(4)	(5)	(6)
	Separation	Separation	Separation	Separation	Separation	Separation
Successful Expungement	-0.138***	-0.087***				
	(0.027)	(0.031)				
Predicted Success (using List Leniency, Mean)			-0.242***	-0.211**		
			(0.082)	(0.086)		
Predicted Success (using List Leniency, Median)					-0.146	-0.111
					(0.089)	(0.094)
Broker Characteristics						
Prior Successful Expungement		0.085**		0.081**		0.085**
		(0.040)		(0.041)		(0.041)
Prior Unsuccessful Expungement		0.257***		0.248***		0.255***
		(0.079)		(0.077)		(0.079)
Female		-0.048*		-0.043		-0.047*
		(0.026)		(0.026)		(0.026)
Non-White		0.033		0.030		0.032
		(0.037)		(0.037)		(0.038)
Experience		-0.061***		-0.061***		-0.061***
		(0.012)		(0.012)		(0.012)
Total Qualifications		-0.017		-0.018		-0.017
		(0.012)		(0.012)		(0.012)
Case Characteristics						
Settlement		-0.024		-0.020		-0.023
		(0.022)		(0.022)		(0.022)
Opposed		0.017		-0.007		0.013
		(0.022)		(0.027)		(0.028)
Intra Industry		0.087*		0.083*		0.086*
		(0.050)		(0.050)		(0.050)
Customer Initiated		0.007		0.004		0.006
		(0.048)		(0.047)		(0.048)
Firm Characteristics						
Taping and/or Disciplined Firm		0.311***		0.292***		0.307***
		(0.112)		(0.103)		(0.111)
Num. Brokers		-0.000***		-0.000***		-0.000***
		(0.000)		(0.000)		(0.000)
Total Expungements per Year		-0.001*		-0.001*		-0.001*
		(0.001)		(0.001)		(0.001)
Total Misconducts per Year		0.000		0.000		0.000
		(0.000)		(0.000)		(0.000)
Arbitrator Characteristics						
Female		-0.008		-0.007		-0.008
		(0.012)		(0.013)		(0.012)
Panel of Arbitrators		0.020		0.019		0.020
		(0.022)		(0.022)		(0.022)
Controls		Yes		Yes		Yes
Year × Region FE	Yes	Yes	Yes	Yes	Yes	Yes
Observations	3,135	3,135	3,135	3,135	3,135	3,135

Panel B

	OLS	OLS	2SLS	2SLS	2SLS	2SLS
	(1)	(2)	(3)	(4)	(5)	(6)
	Num. Yrs. Reg'd	Num. Yrs. Reg'd	Num. Yrs. Reg'd	Num. Yrs. Reg'd	Num. Yrs. Reg'd	Num. Yrs. Reg'd
Successful Expungement	0.446***	0.464***				
	(0.133)	(0.128)				
Predicted Success (using List Leniency, Mean)			0.650**	0.613**		
			(0.318)	(0.310)		
Predicted Success (using List Leniency, Median)					0.416	0.301
					(0.336)	(0.353)
Broker Characteristics						
Prior Successful Expungement		1.907***		1.912***		1.901***
		(0.130)		(0.131)		(0.129)
Prior Unsuccessful Expungement		1.851***		1.861***		1.839***
		(0.386)		(0.387)		(0.387)
Female		-0.136		-0.142*		-0.130
		(0.083)		(0.084)		(0.084)
Non-White		0.037		0.039		0.033
		(0.113)		(0.113)		(0.115)
Experience		0.250***		0.250***		0.249***
		(0.053)		(0.053)		(0.054)
Total Qualifications		0.120**		0.120**		0.119**
		(0.051)		(0.051)		(0.051)
Case Characteristics						
Settlement		-0.075		-0.080		-0.069
		(0.081)		(0.082)		(0.083)
Opposed		0.015		0.044		-0.017
		(0.067)		(0.086)		(0.089)
Intra Industry		-0.043		-0.038		-0.048
		(0.103)		(0.105)		(0.104)
Customer Initiated		0.075		0.078		0.071
		(0.072)		(0.073)		(0.072)
Firm Characteristics						
Taping and/or Disciplined Firm		-0.755		-0.731		-0.782
		(0.733)		(0.725)		(0.760)
Num. Brokers		0.000***		0.000***		0.000***
		(0.000)		(0.000)		(0.000)
Total Expungements per Year		-0.000		-0.000		-0.000
		(0.002)		(0.002)		(0.002)
Total Misconducts per Year		-0.000		-0.000		-0.000
		(0.001)		(0.001)		(0.001)
Arbitrator Characteristics						
Female		0.058*		0.057*		0.060*
		(0.032)		(0.032)		(0.033)
Panel of Arbitrators		-0.050		-0.049		-0.052
		(0.062)		(0.062)		(0.062)
Controls		Yes		Yes		Yes
Year × Region FE	Yes	Yes	Yes	Yes	Yes	Yes
Observations	3,135	3,135	3,135	3,135	3,135	3,135

Table 10 Reduced form estimates of the effect of arbitrator leniency on recidivism.
This table presents the reduced form OLS regressions of future recidivism on each of the instrumental variables: List Leniency (Mean) (the relative leniency of the mean arbitrator on the initial list of randomly assigned arbitrators), and List Leniency (Median) (the relative leniency of the median arbitrator on the initial list of randomly assigned arbitrators). To determine the relative leniency of the mean (or median) arbitrator on the initial list, we calculate the leave-out success rate of all arbitrators on the list minus the mean annual success rate in the FINRA geographic region. The success rate is the number of successful expungement awards divided by the total number of expungement awards over which the arbitrator has presided. In columns (1)–(4), the dependent variable reflects the number of future years with allegations of misconduct (including expunged misconduct) after the initial expungement request. In columns (5)–(8), the dependent variable reflects the number of future years with successful expungements after the initial expungement request. All control variables are defined in the appendix, and all models include region-year fixed effects. Standard errors are clustered by firm. Statistical significance of 10%, 5%, and 1% is represented by *, **, and ***, respectively.

	(1) Num. Yrs. w/ Misc.	(2) Num. Yrs. w/ Misc.	(3) Num. Yrs. w/ Misc.	(4) Num. Yrs. w/ Misc.	(5) Num. Yrs. w/ Exp.	(6) Num. Yrs. w/ Exp.	(7) Num. Yrs. w/ Exp.	(8) Num. Yrs. w/ Exp.
List Leniency, Mean	0.068	0.055			0.284***	0.212**		
	(0.156)	(0.131)			(0.077)	(0.082)		
List Leniency, Median			0.315**	0.278**			0.235***	0.179**
			(0.128)	(0.109)			(0.087)	(0.088)
Broker Characteristics								
Prior Successful Expungement		1.432***		1.430***		1.150***		1.150***
		(0.111)		(0.111)		(0.099)		(0.099)
Prior Unsuccessful Expungement		1.328***		1.330***		0.656***		0.657***
		(0.202)		(0.203)		(0.145)		(0.146)
Female		-0.035		-0.037		0.050		0.050
		(0.050)		(0.050)		(0.043)		(0.042)
Non-White		0.129*		0.130*		-0.038		-0.039
		(0.068)		(0.068)		(0.026)		(0.026)
Experience		0.028*		0.028*		0.008		0.008
		(0.017)		(0.017)		(0.008)		(0.008)
Total Qualifications		0.006		0.007		0.017*		0.017*
		(0.020)		(0.020)		(0.010)		(0.010)
Case Characteristics								
Settlement		0.048		0.046		0.011		0.011
		(0.036)		(0.037)		(0.023)		(0.023)
Opposed		0.005		0.008		-0.041*		-0.041*
		(0.035)		(0.034)		(0.022)		(0.022)
Intra Industry		-0.187*		-0.188*		-0.098		-0.099
		(0.112)		(0.111)		(0.093)		(0.093)
Customer Initiated		-0.194*		-0.193*		-0.122		-0.123
		(0.107)		(0.107)		(0.096)		(0.095)
Firm Characteristics								
Taping and/or Disciplined Firm		1.020***		1.020***		0.268		0.264
		(0.287)		(0.286)		(0.276)		(0.277)
Num. Brokers		-0.000***		-0.000***		-0.000***		-0.000***
		(0.000)		(0.000)		(0.000)		(0.000)
Total Expungements per Year		0.001		0.001		0.000		0.000
		(0.001)		(0.001)		(0.001)		(0.001)
Total Misconducts per Year		0.000		0.000		0.000*		0.000*
		(0.000)		(0.000)		(0.000)		(0.000)
Arbitrator Characteristics								
Female		0.023		0.022		0.006		0.006
		(0.018)		(0.018)		(0.012)		(0.013)
Panel of Arbitrators		-0.035		-0.051		-0.042**		-0.047**
		(0.038)		(0.040)		(0.019)		(0.021)
Controls		Yes		Yes		Yes		Yes
Year × Region FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Observations	3,135	3,135	3,135	3,135	3,135	3,135	3,135	3,135

Table 11 Reduced form estimates of the effect of arbitrator leniency on future employment outcomes.
This table presents the reduced form OLS regressions of career outcomes on each of the instrumental variables: List Leniency (Mean) (the relative leniency of the mean arbitrator on the initial list of randomly assigned arbitrators), and List Leniency (Median) (the relative leniency of the median arbitrator on the initial list of randomly assigned arbitrators). To determine the relative leniency of the mean (or median) arbitrator on the initial list, we calculate the leave-out success rate of all arbitrators on the list minus the mean annual success rate in the FINRA geographic region. The success rate is the number of successful expungement awards divided by the total number of expungement awards over which the arbitrator has presided. In columns (1)–(4), the dependent variable is a dummy variable for whether the broker separated from her employer. In columns (5)–(8), the dependent variable captures the number of years the broker is registered after the expungement request. Only brokers with expungements adjudicated prior to 2017 are included. All control variables are defined in the appendix, and all models include region-year fixed effects. Statistical significance of 10%, 5%, and 1% is represented by *, **, and ***, respectively.

	(1) Separation	(2) Separation	(3) Separation	(4) Separation	(5) Num. Yrs. Reg'd	(6) Num. Yrs. Reg'd	(7) Num. Yrs. Reg'd	(8) Num. Yrs. Reg'd
List Leniency, Mean	-0.342***	-0.275**			0.918*	0.799*		
	(0.123)	(0.117)			(0.468)	(0.423)		
List Leniency, Median			-0.138	-0.101			0.395	0.273
			(0.085)	(0.085)			(0.330)	(0.328)
Broker Characteristics								
Prior Successful Expungement		0.090**		0.090**		1.885***		1.887***
		(0.040)		(0.040)		(0.130)		(0.129)
Prior Unsuccessful Expungement		0.262***		0.262***		1.820***		1.820***
		(0.080)		(0.081)		(0.389)		(0.389)
Female		-0.049*		-0.050*		-0.124		-0.121
		(0.026)		(0.026)		(0.080)		(0.081)
Non-White		0.032		0.034		0.034		0.029
		(0.039)		(0.039)		(0.115)		(0.116)
Experience		-0.062***		-0.061***		0.251***		0.249***
		(0.012)		(0.012)		(0.054)		(0.054)
Total Qualifications		-0.017		-0.017		0.119**		0.118**
		(0.012)		(0.012)		(0.051)		(0.051)
Case Characteristics								
Settlement		-0.026		-0.026		-0.063		-0.060
		(0.022)		(0.022)		(0.080)		(0.080)
Opposed		0.031		0.033		-0.065		-0.072
		(0.020)		(0.020)		(0.065)		(0.065)
Intra Industry		0.088*		0.089*		-0.052		-0.057
		(0.051)		(0.051)		(0.105)		(0.104)
Customer Initiated		0.007		0.009		0.069		0.065
		(0.049)		(0.049)		(0.073)		(0.072)
Firm Characteristics								
Taping and/or Disciplined Firm		0.318***		0.325***		-0.809		-0.828
		(0.117)		(0.119)		(0.779)		(0.782)
Num. Brokers		-0.000***		-0.000***		0.000***		0.000***
		(0.000)		(0.000)		(0.000)		(0.000)
Total Expungements per Year		-0.001*		-0.001*		-0.000		-0.000
		(0.001)		(0.001)		(0.002)		(0.002)
Total Misconducts per Year		0.000		0.000		-0.000		-0.000
		(0.000)		(0.000)		(0.001)		(0.001)
Arbitrator Characteristics								
Female		-0.009		-0.008		0.062*		0.061*
		(0.012)		(0.012)		(0.032)		(0.033)
Panel of Arbitrators		0.028		0.027		-0.076		-0.072
		(0.022)		(0.024)		(0.064)		(0.068)
Controls		Yes		Yes		Yes		Yes
Year × Region FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Observations	3,135	3,135	3,135	3,135	3,135	3,135	3,135	3,135

Figure 1 Expungement outcomes by year.
This figure shows the number of successful, unsuccessful, and moot expungement requests from 2007 to 2016. An expungement is "successful" if granted, "unsuccessful" if denied, and "moot" if resolved prior to adjudication (i.e. the request was not resolved on the merits). The year reflects when the expungement request was filed.

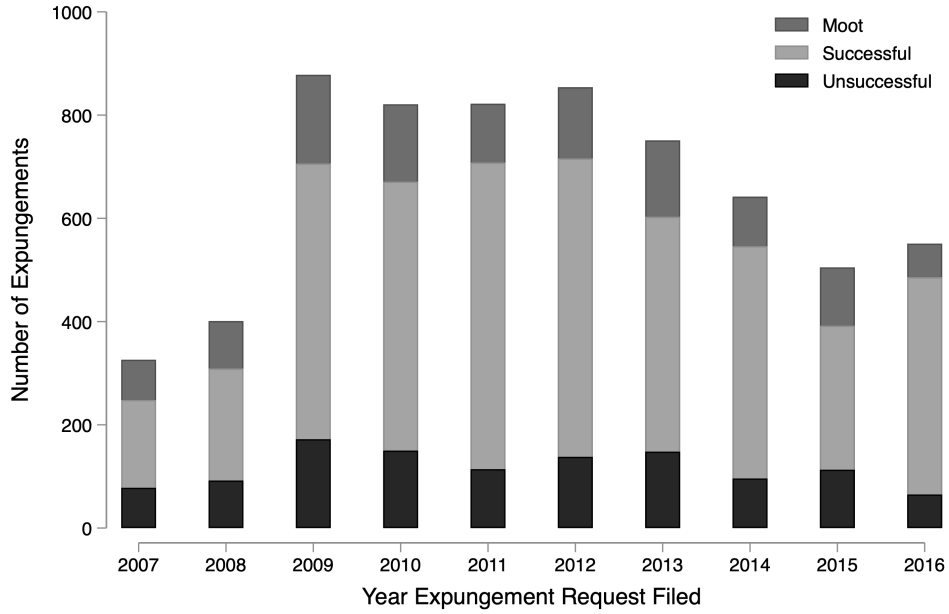


Figure 2 Brokers with multiple expungement requests.
This figure shows the proportion of brokers who filed one, two, or three or more expungement requests from 2007 to 2016. The left hand axis reflects the number of brokers, and the right hand axis reflects the percentage of total brokers. The figure is limited to brokers who filed for expungement at least once in our sample period.

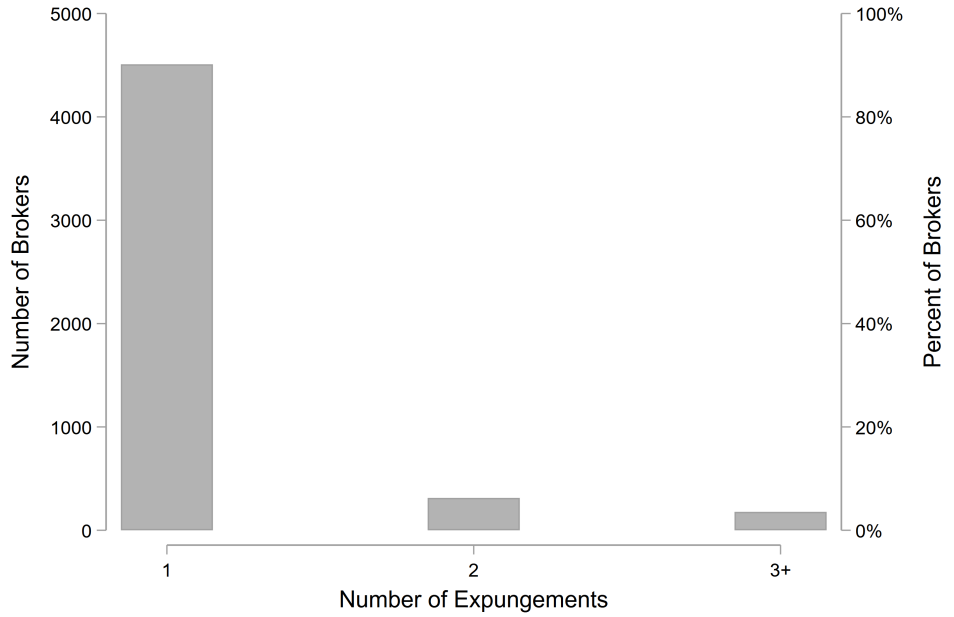
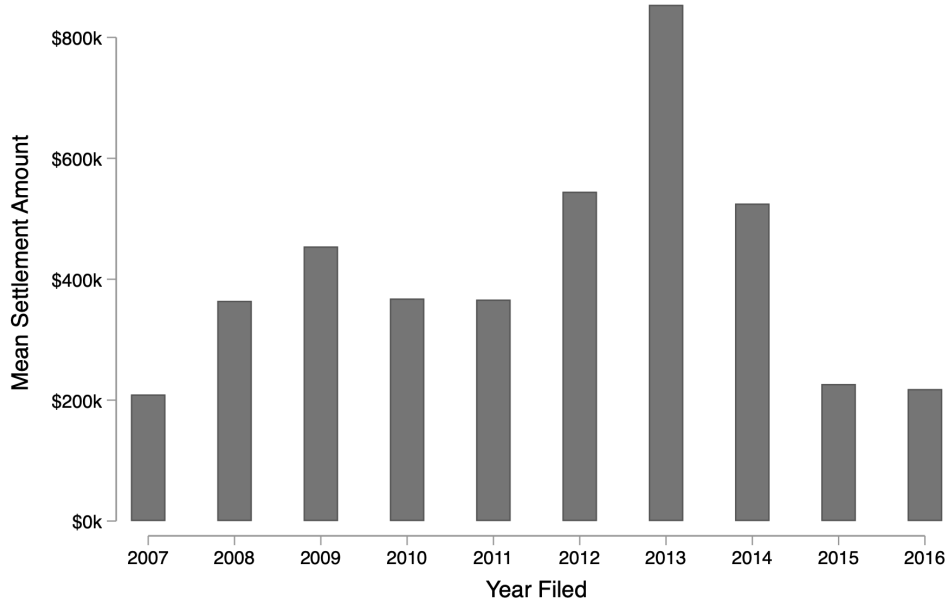


Figure 3 Broker settlements in expungement awards.
This figure shows the distribution of non-zero settlements for customer arbitrations that include a request for expungement. Panel A plots the mean settlement and Panel B plots the median settlement. The year represents when the expungement request was filed. Settlements are only included if the settlement amount is disclosed in the arbitration award, and one outlier settlement of $9.4 million has been dropped.

Panel A



Panel B

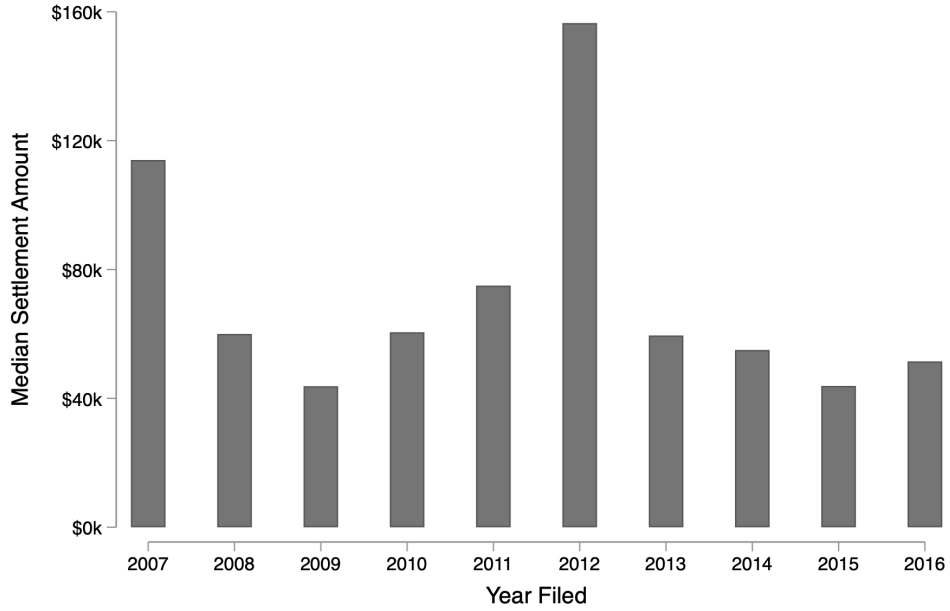


Figure 4 Recidivism following expungement requests.
This figure shows the probability of misconduct or successful expungement at time t = 1, 2, 3 ...8 conditional on recording a misconduct or expungement at t = 0. We drop observations where a broker records both an expungement and misconduct in the same initial year. To aid interpretation of the magnitudes, we also plot the baseline (unconditional) misconduct rate (including successful expungements).

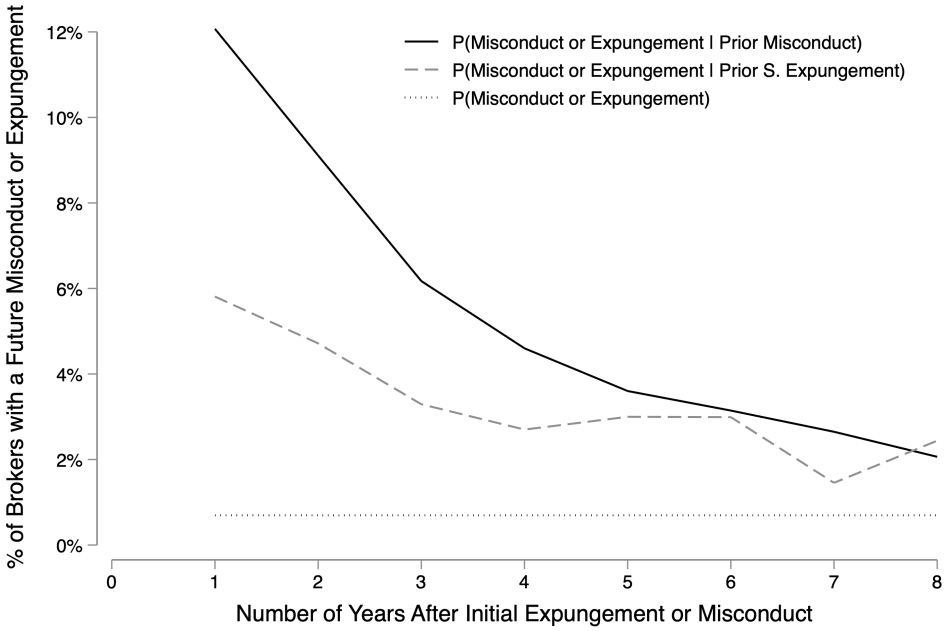


Figure 5 Employment outcomes following the first incidence of misconduct.
This figure examines career consequences for the subset of expungement brokers with only one misconduct (i.e., brokers who would have "clean" records after a successful expungement). The figure compares the "clean" brokers (i.e., those with successful expungements), and the two categories of one-misconduct brokers (those with unsuccessful expungements and those with no expungement attempt). The figure plots the out-of-industry survival function for all employment separations preceded by an expungement award in the previous year.

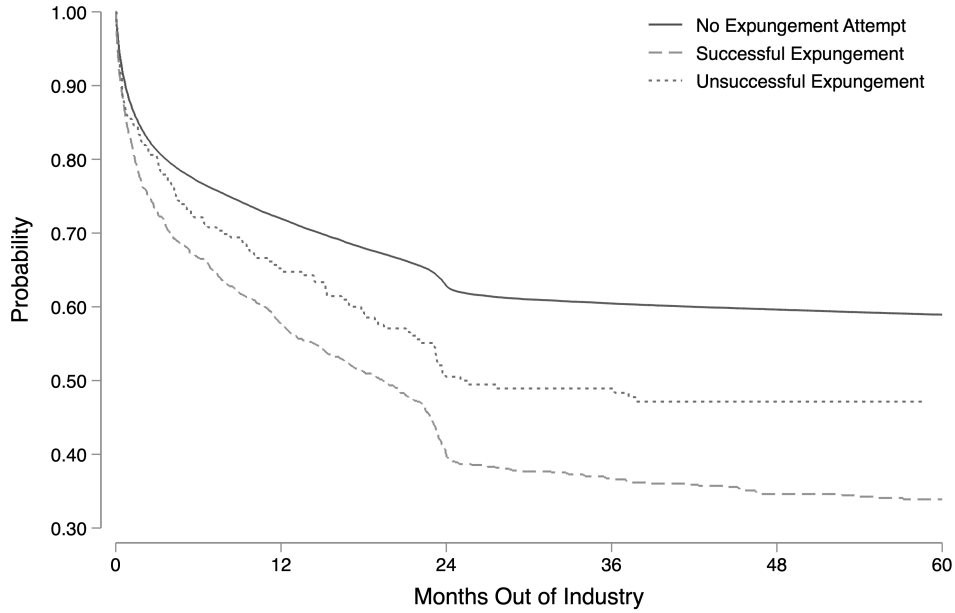
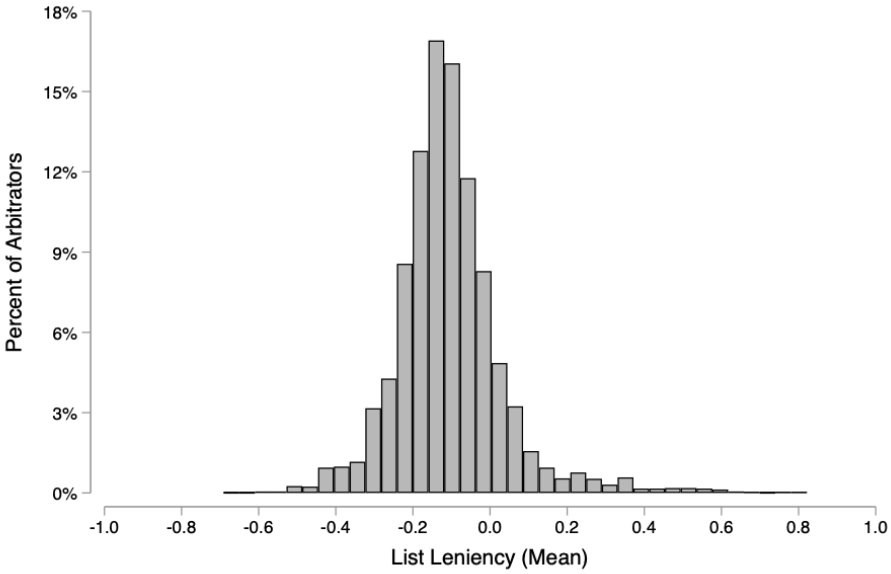


Figure 6 Distribution of IV.
This figure shows the distribution of relative leniencies of the randomly assigned list of arbitrators. Panel A shows the relative leniency of the mean arbitrator on the randomly assigned list of arbitrators, while Panel B shows relative leniency of the median arbitrator on the randomly assigned list of arbitrators. To determine relative leniency, we calculate the leave-out success rate (i.e., the number of expungements awarded relative to the number of expungement requests presided over) of all arbitrators on the list and determine the mean (or median) arbitrator on that list. We then subtract the mean success rate of all potential arbitrators in the same region and year.

Panel A



Panel B

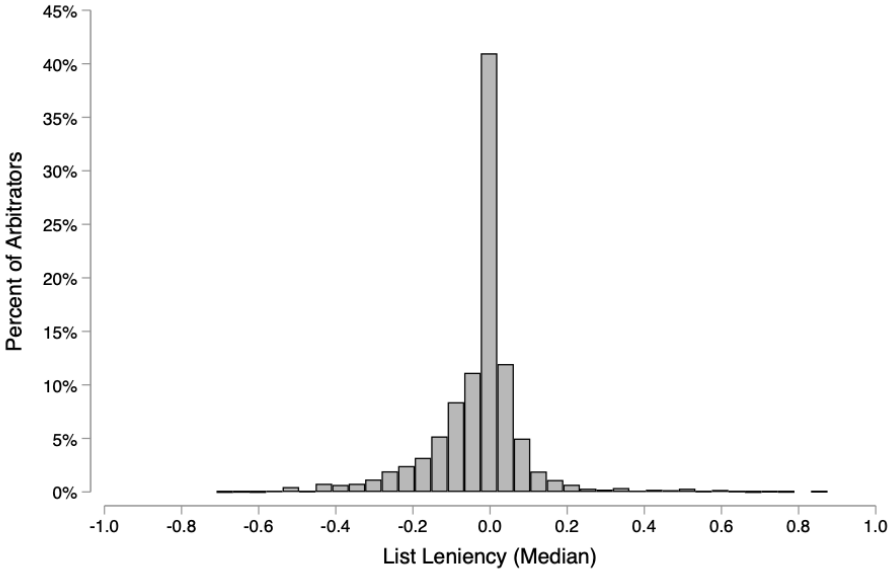
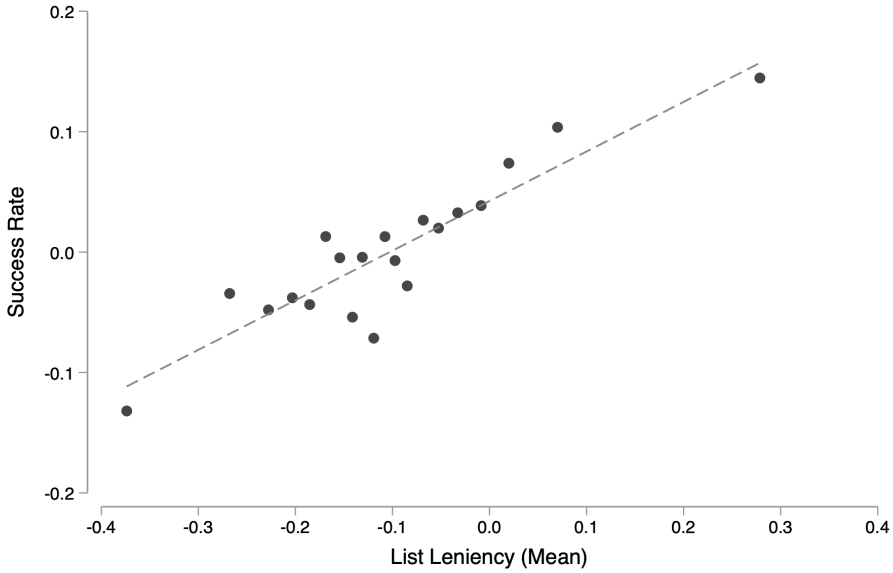


Figure 7 Strength of IV.
This figure plots the relationship between the relative leniency of the list of potential arbitrators and a success indicator. To construct the binned scatter plots, we first regress an indicator for successful expungement on year-region fixed effects. We then group observations into 20 bins and plot mean values of the x and y variables within each bin. Panel A shows the mean leniency of the randomly assigned list of arbitrators, while Panel B shows median leniency of the randomly assigned list of arbitrators.

Panel A



Panel B

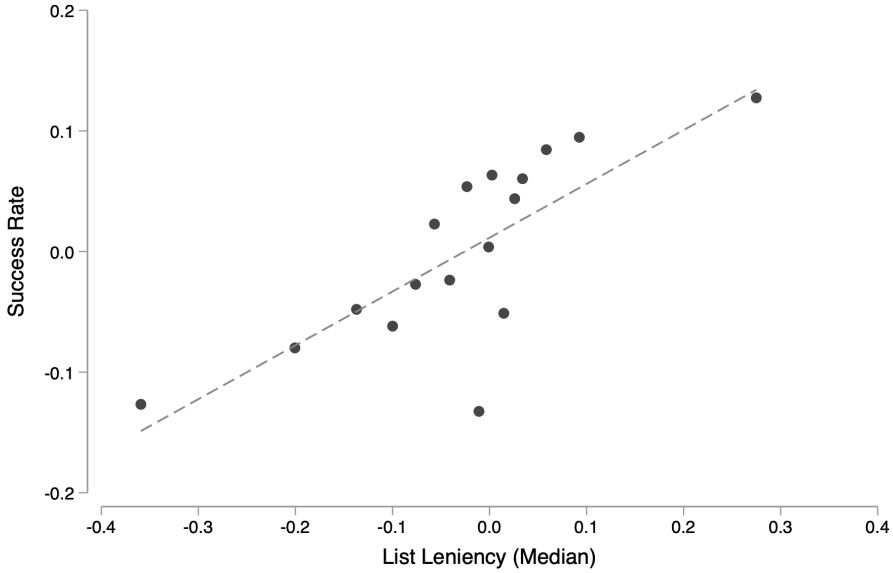


Exhibit 1

BrokerCheck web traffic for "FINRA.org"
This exhibit summarizes web traffic to FINRA.org. The information was provided by Amazon's Alexa.

Usage Statistics from Amazon Alexa

- Global rank – 24,545
- US rank – 4,877
- Past 30-days (as of September 1st, 2018)
  - 709,991 unique visitors - The estimated number of unique people to visit this site over the past 30 days.
  - 2,334,642 estimated visits - The estimated number of visits to this site over the past 30 days. A visit is a single browsing session, meaning the visitor used the site with no breaks longer than 30 minutes. A single visitor may have made multiple visits.
  - 6,514,325 estimated pageviews - The estimated number of pageviews for this site over the past 30 days. A pageview is recorded whenever a full page of the website is viewed or refreshed. Partial page refreshes don't count as a pageviews. A single visit may consist of multiple pageviews.
  - 3.29 visits per visitor
  - 2.79 pageviews per visit
  - 84.1% of visitors are from the US

How to identify BrokerCheck users specifically?

- 37.11% of visitors to FINRA.org go to the brokercheck.finra.org subdomain
  - Hence, a back-of-the-envelope calculation suggests 0.3711 * 709,991 = 263,478 unique users to BrokerCheck each month.

Visitor Demographics

- Please see the output from Alexa below. All of the demographic variables from the Alexa report are relative to the 'internet average' which comes Alexa's overall panel of users.

Exhibit 2

Example of BrokerCheck webpage.
FINRA's BrokerCheck website displays the total number of disclosures for each broker and detail on each specific disclosure. Below we present an example of a broker with three disclosures. This individual appeared to have a clean record prior to December 2012, but he had expunged a prior infraction in 2011. He was barred from the industry due to improper behavior in 2014.

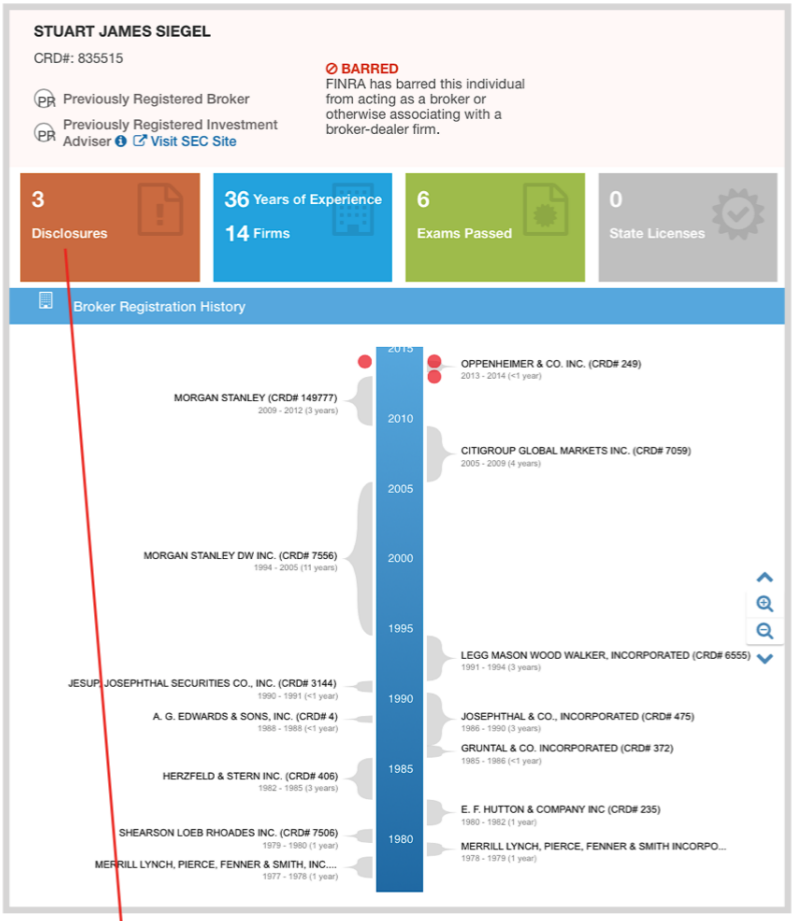


Exhibit 3

Number of allegations per BrokerCheck disclosure category.
This table presents the complete set of BrokerCheck Disclosure Categories. The "Misconduct" categories are highlighted in grey.

Full BrokerCheck Sample		
	Number	Percent
Civil - Final	800	0.4%
Civil - On Appeal	12	0.0%
Civil - Pending	340	0.2%
Civil - Bond	137	0.1%
Criminal - Final Disposition	5,359	2.5%
Criminal - On Appeal	21	0.0%
Criminal - Pending Charge	721	0.3%
Customer Dispute - Award / Judgment	1,921	0.9%
Customer Dispute - Closed-No Action	5,581	2.6%
Customer Dispute - Denied	25,039	11.8%
Customer Dispute - Dismissed	128	0.1%
Customer Dispute - Final	208	0.1%
Customer Dispute - Pending	3,920	1.8%
Customer Dispute - Settled	35,350	16.6%
Customer Dispute - Withdrawn	1,347	0.6%
Employment Separation After Allegations	15,789	7.4%
Financial - Final	60,984	28.7%
Financial - Pending	4,167	2.0%
Investigation	468	0.2%
Judgment / Lien	32,530	15.3%
Regulatory - Final	17,565	8.3%
Regulatory - On Appeal	69	0.0%
Regulatory - Pending	233	0.1%
Total Misconduct Infractions	76,784	36.1%
Total Infractions	212,689	

Exhibit 4

Data pulled from arbitration awards.
Below we summarize the information we retrieved from the expungement arbitration awards.

Scraped Variables

- FINRA_Ref
  - This the number FINRA has assigned to each award. The award number does not uniquely identify a case—that is, multiple award numbers may refer to one arbitration case. Thus, duplicates were removed during the hand-collection.
- Rule
  - This refers to the rule under which expungement was granted. Only cases pertaining to customer disputes will list a rule; a broker-firm dispute regarding a Form-U5 issue will not cite a rule.
- Erroneous
  - Dummy variable where "1" indicates expungement was granted under Rule 2080's "[t]he claim, allegation, or information is factually impossible or clearly erroneous" standard (it includes variations such as simply "the claims are erroneous"). This variable was checked by hand after scraping.
- False
  - Dummy variable where "1" indicates expungement was granted under Rule 2080's "[t]he claim, allegation, or information is false" standard.
- Involved
  - Dummy variable where "1" indicates expungement was granted under Rule 2080's "[t]he registered person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation, or conversion of funds" standard. This variable was checked by hand after scraping.
- Success
  - Dummy variable for whether or not an expungement was successful, where "1" indicates success.
- Panel
  - Dummy variable for whether a case was heard by a panel of three arbitrators or a single arbitrator, where "1" indicates that it was heard by a panel.
- Award Date
  - This corresponds to the "Date of Award" column from the Arbitration Awards Online section of FINRA's website.
- Hearing Site
  - This corresponds to where the arbitrator was held and can be found on the first page of the award.
- Settlement
  - Dummy variable where "1" indicates that the complaint was settled.
- Form U5
  - Dummy variable where "1" indicates that the award contained the phrase "Form U5".

Hand Collected Variables

- Claim Date
  - Date that the claim was filed according to the FINRA award. This can be found in the "Case Information" section and is preceded by the phrase "Statement of Claim filed".
- Unopposed
  - Dummy variable set to "1" if the request for expungement was unopposed by the customer. If a customer was present or arguments were heard it was marked as opposed. To determine unopposed, we made use of phrases in the award such as "unopposed expungement", "opted not to participate in the expungement hearing", or similar phrases that indicated the customer was not involved or was not raising objections to expungement.
- CRD
  - This corresponds to the CRD number for each broker in an award. In rare instances, multiple brokers requested expungement and the arbitrator reached a split decision. In such instances, we separately record the CRD number for each type of expungement outcome.
- Firm CRD
  - This corresponds to the firm CRD for each broker in an award. When multiple firms were listed for a single broker, the firm where the broker was most recently employed prior to the award was included.
- Settlement/Damages
  - This variable reflects the dollar value of the net settlement or damages mentioned in an award. This amount is frequently not disclosed, in which case we leave the observation blank.
- Complaint Initiation
  - This variable indicates who filed the complaint that gave rise to the FINRA award. The complaint could have been filed by a customer, broker, or firm.
    - Customer initiated – Customer initiated awards are those where a customer filed the complaint and was listed as the claimant on the FINRA award.
    - Broker initiated – These are awards in which a broker filed the complaint and is listed as the claimant on the FINRA award. The broker can file a complaint against a customer to expunge an award from their record. Additionally, a broker can be named a claimant when they bring a complaint against a firm over either employment disputes, expungement of a customer complaint, or expungement of their industry employment record (i.e., U5).
    - Firm initiated – Occasionally, firms will file complaints against either brokers or customers and are named the claimant in a given award. Firms will bring complaints against a customer to seek expungement either for themselves or for their brokers. An award brought against a broker usually involves a business dispute.
- Intra Industry
  - This is a dummy variable set to 1 if the dispute concerned only FINRA registered firms and their employees. In intra-industry complaints, there are two kinds of cases: those brought by firms against brokers and those brought by brokers against their firms. Broadly, these two kinds of complaints are (1) employment-related such as wrongful termination and (2) U4/U5 related, as brokers may bring cases against their former firms to have their U5 and U4 cleansed (these are FINRA-required forms that contain a record of complaints against the broker).

- Who Pays
  - Variable to indicate whether the firm, broker, or both paid any damages/settlement noted in the award.
- Infraction Date
  - This is the earliest date of wrongdoing mentioned in an award. Most of the analysis using this variable was collapsed to an infraction year due to inconsistent reporting of the date of the actual offense from case to case.
- Unsuitable
  - The award states in its cause of action that a given investment or investment advice was unsuitable.
- Misrepresentation
  - The award states in its cause of action that a broker misrepresented critical information.
- Unauthorized
  - The award states in its cause of action that a broker initiated unauthorized trades or transactions.
- Omission
  - The award states in its cause of action that a broker omitted critical information.
- Fee/Commissions
  - The award states in its cause of action a reference to fees/commissions.
- Fraud
  - The award states in its cause of action "fraud".
- Fiduciary duty
  - The award states in its cause of action a breach of fiduciary duty or simply "duty".
- Negligence
  - The award states in its cause of action negligence. Some awards claimed "negligent misrepresentations" as a cause of action. This would be recorded as a "1" for both "Misrepresentations" and "Negligence".
- Risky
  - The award states in its cause of action that an investment-related decision was risky, over-concentrated, or illiquid.
- Churning/Excessive Trading
  - The award states either "churning" or "excessive trading" in its cause of action.
- Other
  - The award states something other than the prior ten categories as a cause of action.
- Slander Libel Defamation
  - This is where the award explicitly mentions slander, libel, or defamation as a cause of action in an intra-industry complaint. This is typically regarding information published by a firm regarding the broker's record.
- Interference

  - This is a claim that the other party—either firm or broker(s)—interfered with the broker's business in an intra-industry complaint (e.g., contacted a broker's customers or took a client list).

- Unfair Practices
  - This is like the interference claim and usually involves unfair competition as part of an intra-industry complaint (e.g., a broker claims that the firm terminated his franchise agreement and forced him to sell his practice below fair value).

- Wrongful Termination
  - Dummy variable for whether wrongful termination was explicitly mentioned as a cause of action in the award in an intra-industry complaint.

- Other Employment Related
  - Dummy variable for whether the cause of action in an intra-industry complaint did not fit the prior four categories.

- Truly Erroneous
  - Dummy variable for whether a case expunged under the "erroneous" standard would be interpreted by the lay person as erroneous (e.g., broker was not employed at the relevant firm at the time of the offense, broker was misnamed in the case filing, or broker had no contact with client).

Exhibit 5

Expungement requests per category of misconduct.
This table shows the allegations in the expungement awards, broken down by the party that made the initial complaint. Many awards involve multiple allegations, so the percentages sum to more than 100.

	All Expungements		Customer-Initiated Complaints		Broker-Initiated Complaints		Firm-Initiated Complaints	
	Total	Percent	Total	Percent	Total	Percent	Total	Percent
Unsuitable	2,365	36%	2,358	48%	5	0%	1	0%
Misrepresentation	2,726	41%	2,660	54%	61	4%	5	2%
Unauthorized	644	10%	641	13%	3	0%	0	0%
Omission	1,393	21%	1,370	28%	23	1%	0	0%
Fee/Commission	156	2%	152	3%	2	0%	2	1%
Fraud	2,553	38%	2,433	50%	107	7%	12	5%
Fiduciary Duty	4,020	60%	3,945	81%	45	3%	29	13%
Negligence	3,807	57%	3,682	75%	119	8%	5	2%
Risky	349	5%	349	7%	0	0%	0	0%
Churning/Excessive Trading	415	6%	413	8%	2	0%	0	0%
Other	4,505	68%	4,461	91%	34	2%	9	4%
Slander/Libel/Defamation	474	7%	1	0%	463	30%	10	4%
Interference	280	4%	2	0%	236	15%	42	19%
Unfair Practices	123	2%	1	0%	80	5%	42	19%
Wrongful Termination	226	3%	0	0%	225	15%	1	0%
Other Employment Related	1,554	23%	0	0%	1,340	87%	214	94%
Total Awards	6,660		4,888		1,540		227	

Exhibit 6

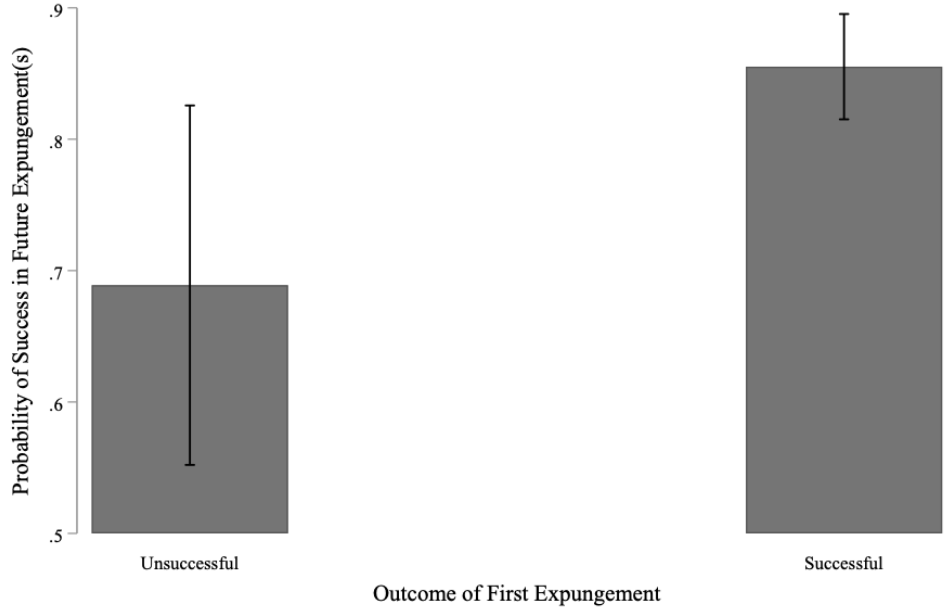
Effect of expungement on expungement requests.
This table analyzes the incidence of future expungement requests. The dependent variable captures the number of years with an expungement request after the initial expungement request. Only brokers with expungements adjudicated prior to 2017 are included. Columns (1) and (2) reflect the OLS results. Columns (3)–(6) use 2SLS, where the instrument is the relative leniency of the randomly assigned list of potential arbitrators. The relative leniency of the arbitrator list is calculated as the mean (or median) leave-out success rate of all arbitrators on the list minus the mean annual success rate in the FINRA geographic region. Success rate is the number of successful expungement awards divided by the total number of expungement awards over which the arbitrator has presided. Columns (3) and (4) reflect the results using the first instrument: List Leniency (Mean) (the relative leniency of the mean arbitrator on the initial list). Columns (5) and (6) reflect the results using the second instrument: List Leniency (Median) (the relative leniency of the median arbitrator on the initial list). All control variables are defined in the appendix, and all models include region-year fixed effects. Standard errors are clustered by firm. Statistical significance of 10%, 5%, and 1% is represented by *, **, and ***, respectively.

	OLS	OLS	2SLS	2SLS	2SLS	2SLS
	(1)	(2)	(3)	(4)	(5)	(6)
	Num. Yrs. w/ Req.	Num. Yrs. w/ Req.	Num. Yrs. w/ Req.	Num. Yrs. w/ Req.	Num. Yrs. w/ Req.	Num. Yrs. w/ Req.
Successful Expungement	0.017	0.031				
	(0.023)	(0.021)				
Predicted Success (using List Leniency, Mean)			0.096*	0.093**		
			(0.050)	(0.047)		
Predicted Success (using List Leniency, Median)					0.105	0.107
					(0.073)	(0.079)
Broker Characteristics						
Prior Successful Expungement		0.794***		0.797***		0.797***
		(0.090)		(0.090)		(0.090)
Prior Unsuccessful Expungement		0.533***		0.537***		0.538***
		(0.145)		(0.146)		(0.145)
Female		0.021		0.019		0.018
		(0.037)		(0.037)		(0.036)
Non-White		-0.030		-0.029		-0.028
		(0.030)		(0.030)		(0.030)
Experience		0.019*		0.020*		0.020*
		(0.010)		(0.010)		(0.010)
Total Qualifications		0.026**		0.026**		0.026**
		(0.013)		(0.013)		(0.013)
Case Characteristics						
Settlement		0.028		0.025		0.025
		(0.020)		(0.021)		(0.021)
Opposed		-0.002		0.010		0.013
		(0.020)		(0.021)		(0.019)
Intra Industry		-0.064		-0.062		-0.061
		(0.081)		(0.080)		(0.080)
Customer Initiated		-0.115		-0.114		-0.113
		(0.077)		(0.077)		(0.076)
Firm Characteristics						
Taping and/or Disciplined Firm		0.405		0.415		0.417
		(0.256)		(0.256)		(0.255)
Num. Brokers		-0.000		-0.000*		-0.000
		(0.000)		(0.000)		(0.000)
Total Expungements per Year		-0.000		-0.000		-0.000
		(0.000)		(0.000)		(0.000)
Total Misconducts per Year		0.000		0.000		0.000
		(0.000)		(0.000)		(0.000)
Arbitrator Characteristics						
Female		0.006		0.006		0.005
		(0.009)		(0.009)		(0.009)
Panel of Arbitrators		-0.047**		-0.046**		-0.046**
		(0.021)		(0.021)		(0.021)
Controls		Yes		Yes		Yes
Year × Region FE	Yes	Yes	Yes	Yes	Yes	Yes
Observations	3,135	3,135	3,135	3,135	3,135	3,135

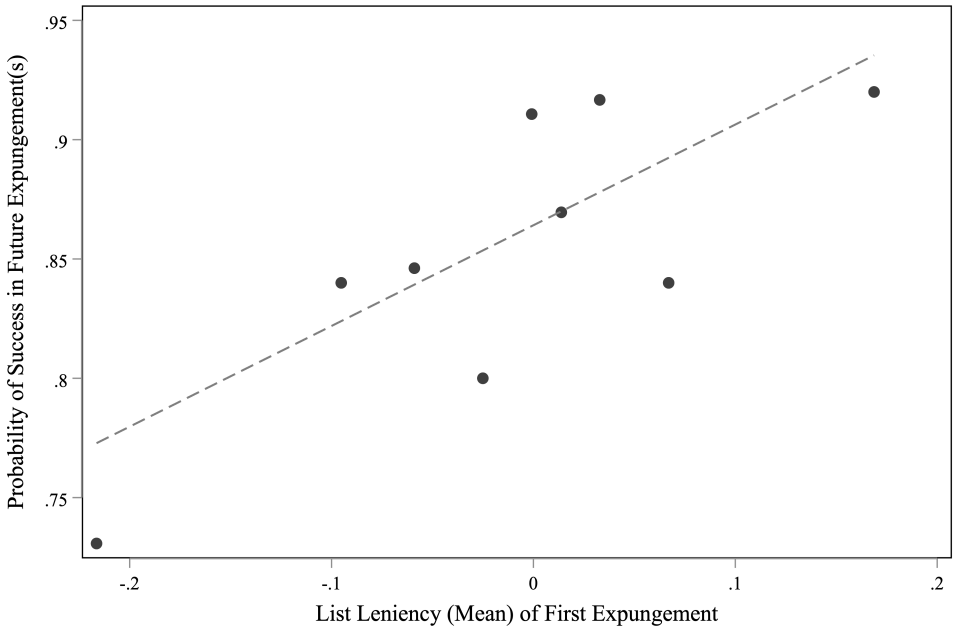
Exhibit 7

Expungement success following initial expungement request.
These figures analyze the relationship between prior expungements and the probability future expungement success. Panel A shows a bar chart of the mean probability (and 95% confidence interval) of future expungement success, split by the outcome of a broker's first expungement case. Panels B and C present binned scatter plots to show how arbitrator leniency from a broker's first expungement request affects their future likelihood of success. Panel B uses List Leniency (Mean) (the relative leniency of the mean arbitrator on the initial list) to measure arbitrator leniency, while Panel C uses List Leniency (Median) (the relative leniency of the median arbitrator on the initial list).

Panel A



Panel B



Panel C

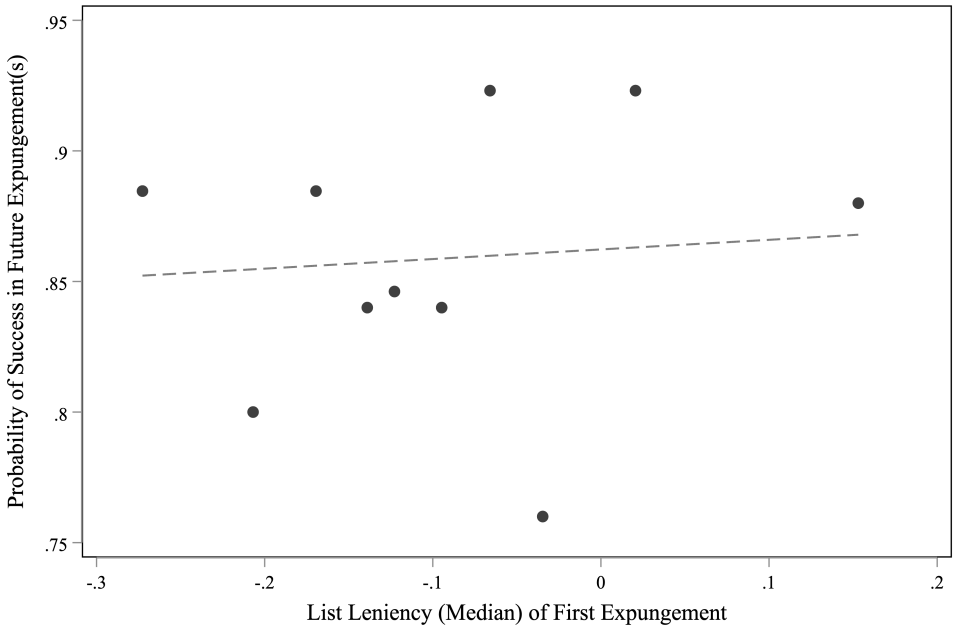


Exhibit 8

Effect of expungement on recidivism, restricted to initial expungement.
This table replicates Table 8, but includes only the first expungement for each broker. In Panel A, the dependent variable reflects the number of future years with allegations of misconduct (including expunged misconduct) after the initial expungement request. In Panel B, the dependent variable reflects the number of future years with successful expungement awards after the initial expungement request. Only brokers who applied for expungement prior to 2017 are included. Columns (1) and (2) reflect the OLS results. Columns (3)–(6) use 2SLS, where the instrument is the relative leniency of the randomly assigned list of potential arbitrators. The relative leniency of the arbitrator list is calculated as the mean (or median) leave-out success rate of all arbitrators on the list minus the mean annual success rate in the FINRA geographic region. Success rate is the number of successful expungement awards divided by the total number of expungement awards over which the arbitrator has presided. Columns (3) and (4) reflect the results using the first instrument: List Leniency (Mean) (the relative leniency of the mean arbitrator on the initial list). Columns (5) and (6) reflect the results using the second instrument: List Leniency (Median) (the relative leniency of the median arbitrator on the initial list). All control variables are defined in the appendix, and all models include region-year fixed effects. Standard errors are clustered by firm. Statistical significance of 10%, 5%, and 1% is represented by *, **, and ***, respectively.

Panel A

	OLS	OLS	2SLS	2SLS	2SLS	2SLS
	(1)	(2)	(3)	(4)	(5)	(6)
	Num. Yrs. w/ Misc.	Num. Yrs. w/ Misc.	Num. Yrs. w/ Misc.	Num. Yrs. w/ Misc.	Num. Yrs. w/ Misc.	Num. Yrs. w/ Misc.
Successful Expungement	-0.141***	-0.149***				
	(0.048)	(0.048)				
Predicted Success (using List Leniency, Mean)			-0.034	-0.012		
			(0.105)	(0.109)		
Predicted Success (using List Leniency, Median)					0.197*	0.231*
					(0.112)	(0.127)
Female		-0.053		-0.058		-0.067*
		(0.039)		(0.039)		(0.040)
Non-White		0.080		0.083		0.087
		(0.064)		(0.064)		(0.065)
Experience		0.009		0.009		0.010
		(0.012)		(0.012)		(0.013)
Total Qualifications		0.022		0.022		0.022
		(0.016)		(0.016)		(0.017)
Case Characteristics						
Settlement		0.060*		0.057*		0.050
		(0.033)		(0.034)		(0.035)
Opposed		-0.024		0.002		0.048
		(0.032)		(0.036)		(0.038)
Intra Industry		-0.190*		-0.184*		-0.174*
		(0.099)		(0.098)		(0.095)
Customer Initiated		-0.178**		-0.175**		-0.170**
		(0.088)		(0.087)		(0.085)
Firm Characteristics						
Taping and/or Disciplined Firm		0.901***		0.920***		0.952***
		(0.280)		(0.274)		(0.267)
Num. Brokers		-0.000***		-0.000***		-0.000***
		(0.000)		(0.000)		(0.000)
Total Expungements per Year		0.002*		0.002*		0.002**
		(0.001)		(0.001)		(0.001)
Total Misconducts per Year		0.000*		0.000*		0.000*
		(0.000)		(0.000)		(0.000)
Arbitrator Characteristics						
Female		0.037**		0.035**		0.033*
		(0.017)		(0.017)		(0.017)
Panel of Arbitrators		-0.016		-0.016		-0.015
		(0.034)		(0.034)		(0.036)
Controls		Yes		Yes		Yes
Year × Region FE	Yes	Yes	Yes	Yes	Yes	Yes
Observations	2,910	2,910	2,910	2,910	2,910	2,910

Panel B

	OLS	OLS	2SLS	2SLS	2SLS	2SLS
	(1)	(2)	(3)	(4)	(5)	(6)
	Num. Yrs. w/ Exp.	Num. Yrs. w/ Exp.	Num. Yrs. w/ Exp.	Num. Yrs. w/ Exp.	Num. Yrs. w/ Exp.	Num. Yrs. w/ Exp.
Successful Expungement	0.035*	0.028				
	(0.019)	(0.019)				
Predicted Success (using List Leniency, Mean)			0.096**	0.112**		
			(0.048)	(0.056)		
Predicted Success (using List Leniency, Median)					0.110	0.150*
					(0.070)	(0.089)
Female		0.005		0.002		0.001
		(0.023)		(0.023)		(0.022)
Non-White		-0.019		-0.018		-0.017
		(0.022)		(0.022)		(0.022)
Experience		-0.004		-0.004		-0.003
		(0.006)		(0.006)		(0.006)
Total Qualifications		0.023***		0.023***		0.023***
		(0.008)		(0.008)		(0.008)
Case Characteristics						
Settlement		0.024		0.021		0.020
		(0.018)		(0.019)		(0.019)
Opposed		-0.007		0.008		0.016
		(0.018)		(0.020)		(0.022)
Intra Industry		-0.099*		-0.095*		-0.094*
		(0.056)		(0.056)		(0.055)
Customer Initiated		-0.072		-0.070		-0.070
		(0.054)		(0.054)		(0.054)
Firm Characteristics						
Taping and/or Disciplined Firm		0.357		0.369		0.374
		(0.284)		(0.282)		(0.281)
Num. Brokers		-0.000***		-0.000***		-0.000***
		(0.000)		(0.000)		(0.000)
Total Expungements per Year		0.000		0.000		0.000
		(0.001)		(0.001)		(0.000)
Total Misconducts per Year		0.000**		0.000**		0.000**
		(0.000)		(0.000)		(0.000)
Arbitrator Characteristics						
Female		0.005		0.004		0.004
		(0.008)		(0.008)		(0.009)
Panel of Arbitrators		-0.026		-0.026		-0.025
		(0.018)		(0.018)		(0.018)
Controls		Yes		Yes		Yes
Year × Region FE	Yes	Yes	Yes	Yes	Yes	Yes
Observations	2,910	2,910	2,910	2,910	2,910	2,910

Exhibit 9

Career outcomes after expungement, split by firm misconduct rate.
This table analyzes the likelihood of separation after expungement, replicating Table 9 Panel A, split by the firm misconduct rate. The firm misconduct rate is defined as the average number of allegations of misconduct (including expunged misconduct) per retail broker registered to a firm in a given year. The dependent variable is a dummy variable for whether the broker separated from her employer after the expungement. Only brokers with expungements adjudicated prior to 2017 are included. Columns (1) and (2) reflect the OLS results. Columns (3)–(6) use 2SLS, where the instrument is the relative leniency of the randomly assigned list of potential arbitrators. The relative leniency of the arbitrator list is calculated as the mean (or median) leave-out success rate of all arbitrators on the list minus the mean annual success rate in the FINRA geographic region. Success rate is the number of successful expungement awards divided by the total number of expungement awards over which the arbitrator has presided. Columns (3) and (4) reflect the results using the first instrument: List Leniency (Mean) (the relative leniency of the mean arbitrator on the initial list). Columns (5) and (6) reflect the results using the second instrument: List Leniency (Median) (the relative leniency of the median arbitrator on the initial list). All control variables are defined in the appendix, and all models include region-year fixed effects. Standard errors are clustered by firm. Statistical significance of 10%, 5%, and 1% is represented by *, **, and ***, respectively.

	Firms with Higher than Avg. Misconduct Rate			Firms with Lower than Avg. Misconduct Rate		
	(1)	(2)	(3)	(4)	(5)	(6)
	Separation	Separation	Separation	Separation	Separation	Separation
Successful Expungement	-0.120**			-0.045		
	(0.057)			(0.035)		
Predicted Success (using List Leniency, Mean)		-0.333*			-0.185*	
		(0.171)			(0.107)	
Predicted Success (using List Leniency, Median)			-0.274			-0.112
			(0.207)			(0.110)
Broker Characteristics						
Prior Successful Expungement	0.136	0.138	0.138	0.117***	0.115***	0.116***
	(0.098)	(0.099)	(0.098)	(0.043)	(0.043)	(0.043)
Prior Unsuccessful Expungement	0.192	0.065	0.100	0.173	0.185	0.179
	(0.205)	(0.206)	(0.217)	(0.111)	(0.115)	(0.112)
Female	-0.072	-0.054	-0.059	-0.030	-0.027	-0.029
	(0.080)	(0.088)	(0.088)	(0.029)	(0.028)	(0.029)
Non-White	0.034	0.046	0.043	0.040	0.041	0.040
	(0.081)	(0.083)	(0.083)	(0.042)	(0.041)	(0.041)
Experience	-0.067**	-0.068**	-0.067**	-0.040***	-0.041***	-0.041***
	(0.034)	(0.033)	(0.033)	(0.013)	(0.013)	(0.013)
Total Qualifications	-0.050*	-0.040	-0.043	-0.003	-0.004	-0.004
	(0.026)	(0.028)	(0.028)	(0.012)	(0.012)	(0.012)
Case Characteristics						
Settlement	-0.063	-0.041	-0.047	-0.015	-0.009	-0.012
	(0.069)	(0.074)	(0.073)	(0.021)	(0.022)	(0.022)
Opposed	-0.028	-0.084	-0.068	0.031	0.009	0.021
	(0.064)	(0.071)	(0.079)	(0.023)	(0.029)	(0.028)
Intra Industry	0.227	0.188	0.199	0.081	0.074	0.078
	(0.153)	(0.166)	(0.165)	(0.050)	(0.050)	(0.051)
Customer Initiated	0.084	0.055	0.063	0.026	0.023	0.025
	(0.154)	(0.166)	(0.164)	(0.046)	(0.046)	(0.047)
Firm Characteristics						
Taping and/or Disciplined Firm	0.215	0.187	0.195	0.000	0.000	0.000
	(0.167)	(0.158)	(0.160)	(.)	(.)	(.)
Num. Brokers	-0.000***	-0.000***	-0.000***	-0.000***	-0.000***	-0.000***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Total Expungements per Year	-0.001	-0.002	-0.002	-0.001	-0.001	-0.001
	(0.006)	(0.006)	(0.006)	(0.001)	(0.001)	(0.001)
Total Misconducts per Year	0.001***	0.001***	0.001***	-0.000	-0.000	-0.000
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Arbitrator Characteristics						
Female	-0.073**	-0.081**	-0.078**	0.006	0.008	0.007
	(0.033)	(0.035)	(0.035)	(0.014)	(0.014)	(0.014)
Panel of Arbitrators	0.058	0.041	0.046	0.016	0.014	0.015
	(0.069)	(0.071)	(0.072)	(0.021)	(0.021)	(0.021)
Equality Across Groups						
p-value				0.241	0.425	0.414
Controls	Yes	Yes	Yes	Yes	Yes	Yes
Year × Region FE	Yes	Yes	Yes	Yes	Yes	Yes
Observations	517	517	517	2,746	2,746	2,746

Exhibit 10

Career outcomes after expungement, split by one vs. multiple misconduct brokers.
This table analyzes the likelihood of separation after expungement, replicating Table 9 Panel A, split by one vs. multiple misconduct brokers (i.e. the table compares the brokers with one misconduct, who would appear "clean" after the expungement, with all other expunged brokers). The dependent variable is a dummy variable for whether the broker separated from her employer after the expungement. Only brokers with expungements adjudicated prior to 2017 are included. Columns (1) and (2) reflect the OLS results. Columns (3)–(6) use 2SLS, where the instrument is the relative leniency of the randomly assigned list of potential arbitrators. The relative leniency of the arbitrator list is calculated as the mean (or median) leave-out success rate of all arbitrators on the list minus the mean annual success rate in the FINRA geographic region. Success rate is the number of successful expungement awards divided by the total number of expungement awards over which the arbitrator has presided. Columns (3) and (4) reflect the results using the first instrument: List Leniency (Mean) (the relative leniency of the mean arbitrator on the initial list). Columns (5) and (6) reflect the results using the second instrument: List Leniency (Median) (the relative leniency of the median arbitrator on the initial list). All control variables are defined in the appendix, and all models include region-year fixed effects. Standard errors are clustered by firm. Statistical significance of 10%, 5%, and 1% is represented by *, **, and ***, respectively.

	One Misconduct Brokers			Multiple Misconduct Brokers		
	(1)	(2)	(3)	(4)	(5)	(6)
	Separation	Separation	Separation	Separation	Separation	Separation
Successful Expungement	-0.046			-0.045		
	(0.046)			(0.035)		
Predicted Success (using List Leniency, Mean)		-0.291**			-0.303***	
		(0.131)			(0.096)	
Predicted Success (using List Leniency, Median)			-0.144			-0.233
			(0.159)			(0.145)
Broker Characteristics						
Prior Successful Expungement	-0.679**	-0.901***	-0.768**	0.128***	0.134***	0.133***
	(0.309)	(0.338)	(0.345)	(0.037)	(0.038)	(0.038)
Prior Unsuccessful Expungement	0.479*	0.349	0.426	0.225**	0.219**	0.220**
	(0.260)	(0.268)	(0.268)	(0.094)	(0.095)	(0.095)
Female	-0.009	-0.001	-0.006	-0.103***	-0.103***	-0.103***
	(0.031)	(0.031)	(0.032)	(0.036)	(0.035)	(0.035)
Non-White	-0.002	0.006	0.001	0.085*	0.078	0.080
	(0.045)	(0.046)	(0.046)	(0.050)	(0.049)	(0.050)
Experience	-0.044***	-0.045***	-0.045***	-0.071***	-0.072***	-0.071***
	(0.014)	(0.014)	(0.014)	(0.018)	(0.018)	(0.018)
Total Qualifications	-0.045**	-0.042**	-0.044**	0.004	0.001	0.002
	(0.018)	(0.018)	(0.018)	(0.017)	(0.017)	(0.017)
Case Characteristics						
Settlement	-0.022	-0.024	-0.023	-0.055	-0.023	-0.032
	(0.031)	(0.030)	(0.030)	(0.035)	(0.037)	(0.039)
Opposed	0.032	-0.002	0.018	-0.005	-0.061	-0.046
	(0.030)	(0.030)	(0.034)	(0.034)	(0.041)	(0.043)
Intra Industry	0.093	0.096	0.094	0.132**	0.122*	0.125**
	(0.076)	(0.076)	(0.076)	(0.064)	(0.062)	(0.063)
Customer Initiated	-0.017	-0.024	-0.020	0.093	0.090	0.091
	(0.074)	(0.073)	(0.074)	(0.062)	(0.060)	(0.061)
Firm Characteristics						
Taping and/or Disciplined Firm	0.323*	0.226	0.284	0.251**	0.221*	0.229*
	(0.177)	(0.236)	(0.210)	(0.126)	(0.115)	(0.119)
Num. Brokers	-0.000***	-0.000**	-0.000***	-0.000***	-0.000***	-0.000***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Total Expungements per Year	-0.002**	-0.002**	-0.002**	-0.001*	-0.002*	-0.002*
	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)
Total Misconducts per Year	-0.000	-0.000	-0.000	0.000	0.000	0.000
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Arbitrator Characteristics						
Female	-0.004	-0.001	-0.003	-0.017	-0.015	-0.016
	(0.015)	(0.015)	(0.015)	(0.021)	(0.021)	(0.021)
Panel of Arbitrators	0.019	0.018	0.018	-0.003	-0.005	-0.005
	(0.029)	(0.030)	(0.029)	(0.037)	(0.037)	(0.037)
Equality Across Groups						
p-value				0.978	0.883	0.544
Controls	Yes	Yes	Yes	Yes	Yes	Yes
Year × Region FE	Yes	Yes	Yes	Yes	Yes	Yes
Observations	1,676	1,676	1,676	1,547	1,547	1,547

Exhibit 11

Career outcomes after expungement, split by standard under which expungement was granted.
This table analyzes the likelihood of separation after expungement, replicating Table 9 Panel A, split by the standard under which expungement was granted (Erroneous vs. Non-Erroneous). In theory, "erroneous" expungements under Rule 2080 should represent the weakest claims of misconduct. The dependent variable is a dummy variable for whether the broker separated from her employer after the expungement. Only brokers with expungements adjudicated prior to 2017 are included. Columns (1) and (2) reflect the OLS results. Columns (3)–(6) use 2SLS, where the instrument is the relative leniency of the randomly assigned list of potential arbitrators. The relative leniency of the arbitrator panel is calculated as the mean (or median) leave-out success rate of all arbitrators on the list minus the mean annual success rate in the FINRA geographic region. Success rate is the number of successful expungement awards divided by the total number of expungement awards over which the arbitrator has presided. Columns (3) and (4) reflect the results using the first instrument: List Leniency (Mean) (the relative leniency of the mean arbitrator on the initial list). Columns (5) and (6) reflect the results using the second instrument: List Leniency (Median) (the relative leniency of the median arbitrator on the initial list). All control variables are defined in the appendix, and all models include region-year fixed effects. Standard errors are clustered by firm. Statistical significance of 10%, 5%, and 1% is represented by *, **, and ***, respectively.

	Erroneous Expungements			Non-erroneous Expungements		
	(1)	(2)	(3)	(4)	(5)	(6)
	Separation	Separation	Separation	Separation	Separation	Separation
Successful Expungement	-0.081**			-0.073***		
	(0.036)			(0.028)		
Predicted Success (using List Leniency, Mean)		-0.225**			-0.121	
		(0.098)			(0.102)	
Predicted Success (using List Leniency, Median)			-0.097			-0.001
			(0.126)			(0.115)
Broker Characteristics						
Prior Successful Expungement	0.068	0.066	0.068	0.171***	0.170***	0.172***
	(0.072)	(0.073)	(0.073)	(0.045)	(0.045)	(0.044)
Prior Unsuccessful Expungement	0.380***	0.342***	0.376***	0.279**	0.281**	0.278**
	(0.095)	(0.098)	(0.101)	(0.109)	(0.109)	(0.111)
Female	-0.046	-0.046	-0.046	-0.031	-0.028	-0.035
	(0.028)	(0.028)	(0.028)	(0.032)	(0.032)	(0.032)
Non-White	0.026	0.022	0.026	0.064	0.066	0.063
	(0.069)	(0.064)	(0.067)	(0.045)	(0.045)	(0.045)
Experience	-0.062***	-0.063***	-0.062***	-0.051***	-0.051***	-0.051***
	(0.016)	(0.016)	(0.016)	(0.012)	(0.012)	(0.013)
Total Qualifications	-0.030	-0.031	-0.030	-0.008	-0.008	-0.008
	(0.021)	(0.021)	(0.021)	(0.014)	(0.013)	(0.014)
Case Characteristics						
Settlement	-0.048	-0.032	-0.047	-0.023	-0.021	-0.026
	(0.030)	(0.035)	(0.036)	(0.030)	(0.029)	(0.029)
Opposed	0.037	-0.008	0.032	0.002	-0.010	0.020
	(0.032)	(0.039)	(0.047)	(0.027)	(0.041)	(0.041)
Intra Industry	-0.075	-0.103	-0.078	0.143**	0.142**	0.145**
	(0.084)	(0.089)	(0.093)	(0.057)	(0.056)	(0.056)
Customer Initiated	-0.046	-0.053	-0.047	0.033	0.031	0.037
	(0.079)	(0.078)	(0.080)	(0.057)	(0.056)	(0.056)
Firm Characteristics						
Taping and/or Disciplined Firm	0.470***	0.443***	0.466***	0.282**	0.273**	0.294**
	(0.106)	(0.107)	(0.109)	(0.136)	(0.133)	(0.148)
Num. Brokers	-0.000***	-0.000***	-0.000***	-0.000***	-0.000***	-0.000***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Total Expungements per Year	-0.001	-0.001	-0.001	-0.001	-0.001	-0.001
	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)
Total Misconducts per Year	0.000	0.000	0.000	0.000	0.000	0.000
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Arbitrator Characteristics						
Female	0.023	0.025	0.023	-0.030*	-0.030*	-0.031*
	(0.016)	(0.017)	(0.017)	(0.017)	(0.017)	(0.017)
Panel of Arbitrators	0.040	0.034	0.040	-0.024	-0.024	-0.023
	(0.027)	(0.028)	(0.029)	(0.027)	(0.027)	(0.027)
Equality Across Groups						
p-value				0.004	0.648	0.403
Controls	Yes	Yes	Yes	Yes	Yes	Yes
Year × Region FE	Yes	Yes	Yes	Yes	Yes	Yes
Observations	1,647	1,647	1,647	2,113	2,113	2,113