



Securities Arbitration Clinic
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Via email to NASAAComments@nasaa.org

Attn: Kristen Standifer, Patrick Costello, and Stephen Brey
North American Securities Administrators Association, Inc.
750 First Street NE, Suite 1140
Washington, DC 20002

Re: **Request for Public Comment Regarding a Proposed Model Rule
for Unpaid Arbitration Awards under the Uniform Securities Acts of
1956 and 2002**

Dear Project Group Chairs:

The St. John's University School of Law Securities Arbitration Clinic (the "Clinic") would like to thank you for the opportunity to comment on the NASAA's request for comment on its proposed rule change, *Proposed Model Rule for Unpaid Arbitration Awards under the Uniform Securities Acts of 1956 and 2002* ("Proposed Rules").

The Clinic is a curricular offering where students and supervising attorneys represent individual investors of limited means in disputes against their investment brokers on a pro bono basis. The Clinic represents aggrieved investors and is committed to investor education and protection. The Clinic handles cases brought within the Financial Industry Regulatory Authority ("FINRA") arbitration forum. The Clinic has a strong interest in the rules governing unpaid arbitration awards and in ensuring that investors are appropriately remedied. In 2019 alone, over \$19 million of awards went unpaid.¹ This represents nearly 20% of all monetary damages awarded for that year. Moreover, unpaid awards continue to accrue annually as unpaid awards from previous years remain unsatisfied. The Clinic recognizes that many individuals harmed by brokerages who fail to pay include retail investors who are typically older adults and other vulnerable members of our community.

¹ <https://www.finra.org/arbitration-mediation/statistics-unpaid-customer-awards-finra-arbitration>

The Clinic agrees that the Proposed Rules are significant because they create clear repercussions for investment advisers who have not paid arbitration awards. The Clinic agrees that brokers should not be able to move to the investment adviser space if they have failed to pay a FINRA arbitration award to an investor. As noted in the proposal, FINRA does take action against brokers who have not paid arbitration awards, but it does not have authority over investment advisers. Therefore, states must have clear authority to discipline investment advisers who do not comply with arbitration awards.

The Proposed Rules ensure that if a broker does not pay the awarded amount, the state can also consider the broker's failure to pay in connection with their investment adviser licensing. By adopting a model rule that would make it unethical not to pay an arbitration award, brokerage firms and brokers may, in turn, be more receptive to honoring awards rendered against them. Furthermore, brokers whose FINRA membership is suspended in connection to an unpaid award would no longer be able to continue misconduct in an investment adviser capacity. Additionally, the Proposed Rules may help eliminate regulatory arbitrage as FINRA registered individuals shift to the investment advisory side of the industry. This is critical since investment advisers would no longer be incentivized to leave a brokerage firm because they have unpaid awards against them and transition to a firm elsewhere with a new title and a clean slate.

The Proposed Rules are not clear that they would apply to formerly registered brokers and investment advisers. It should be clear that failure to pay an award, even if the broker or investment adviser is not presently registered, would still be deemed to be a "Dishonest or Unethical Business Practice" or "fraudulent, deceptive, or manipulative conduct."

Moreover, the Proposed Rules do not appear to apply to awards issued against investment advisers. The proposed language to amend the investment adviser versions of the Model Rule refer to "any final judgment or arbitration award resulting from an investment-related, client or customer-initiated arbitration or court proceeding, unless alternative payment arrangements are agreed to between the client or customer *and the broker-dealer or broker-dealer agent, in writing, and the broker-dealer or broker-dealer agent* complies with the terms of the alternative payment arrangement." (Emphasis added.) The second section includes substantially the same language. We believe this section should read "any final judgment or arbitration award resulting from an investment-related, client or customer-initiated arbitration or court proceeding, unless alternative payment arrangements are agreed to between the client or customer *and the investment adviser or investment adviser representative, in writing, and the investment adviser or investment adviser representative* complies with the terms of the alternative payment arrangement," and that corresponding changes be made to the second section.

While the Proposed Rules are a noble effort to help ensure award payment, there may still be room for other improvements. Although an investor may try to recover their award by asking a court to convert the arbitration award into a judgment, this still does not ensure that the investor is compensated. While the Clinic appreciates that such brokers or investment advisers would be prevented from committing further misconduct within the industry because they would be subject to disciplinary action, this does not protect the investors whom they have already wronged by failing to comply with arbitration awards. We believe that a compensation fund would be appropriate to ensure that investors may have some path by which they can be made whole.

Additionally, while failure to pay an arbitration award is deemed unethical under the Proposed Rules, there is no obligation within the proposal that investment advisers explicitly disclose to state regulators when they have to pay such an arbitration award. Mandating both disclosure and proof of payment of any and all judgments and arbitration awards would give regulators the information they need to regulate nonpayment.

In conclusion, we support the Proposed Rules. However, they are not a perfect tool to address unpaid arbitration awards because they do not ensure investors who have been harmed are compensated. We hope that NASAA continues to consider ways to further protect investors who have been harmed by the misconduct of brokers and investment advisers. Thank you for your consideration and for allowing our Clinic to comment on this important matter.

Respectfully Submitted,

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