TESTIMONY OF ROBERT S. BANKS IN SUPPORT OF SB 96

February 15, 2017

Dear Members of the Senate Committee On Business and Transportation:

I wish to testify in support of SB 96, which would require state investment advisers and broker-dealers in Oregon to maintain an errors and omissions insurance policy in the amount of at least $1 million. My statement is based upon personal knowledge and it is truthful and accurate.

I have worked on investor issues for the last thirty years. I am an adviser to the Financial Industry Regulatory Authority (FINRA), the agency responsible for oversight of all broker-dealers in the nation. I am one of 15 members nationwide (and the only one from Oregon) on FINRA's National Arbitration and Mediation Committee. I have been a member in good standing of the Oregon State Bar since 1982, and much of my practice involves representing Oregonians – usually senior citizens -- who have lost significant amounts of their life savings due to the negligence or intentionally wrongful conduct of stockbrokers and investment advisers.

The circumstances surrounding these losses can take many forms. Sometimes, an honest adviser simply makes an honest mistake. For example, an adviser might withdraw money for a client out of an IRA account rather than a joint account, triggering taxes and penalties. Other times, the conduct causing the loss is more circumspect. There are many instances where a broker sells to a senior citizen of modest means a high risk and illiquid investment that ends in failure, where the only reason for the sale is the high commission it paid to the broker. I see other circumstances where a broker "churns" an account, engaging in an excessive number of trades that generate large commissions to the broker and large losses to the investor. I recently completed a case in which an adviser was charging an elderly couple in their 80s (a retired fireman and homemaker) *annual* commissions and fees for years of over 16%. And, there are those unfortunate cases that involve outright fraud – purchasing investments without client authority, stealing client funds, and the like.

We have fair and balanced laws in Oregon that govern disputes between advisers and their clients. However, there are many, many times where there is simply no recourse for an investor who has lost her savings due to an adviser's mistake, even after a court or panel of arbitrators has heard the evidence, applied the law, and determined that the losses were due to the mistake or misconduct of the adviser. The reason is that there is no requirement for advisers or brokers to carry any liability insurance, and many of them do not.

As a licensed driver, the law requires me to maintain insurance. Financial institutions require home purchasers to have homeowner's insurance in order to get a mortgage. The law

requires Oregon attorneys to have liability insurance before they can represent clients. Doctors, dentists, accountants and other professionals also maintain liability insurance. You cannot rent an office in a Portland office building without having premises liability insurance. We all know that insurance plays a critical role in commerce. It provides protection to both the insured in the event of a mistake or misconduct, and to their clients, patients, tenants, and others who might be harmed by unforeseen events.

Financial advisers are a rare exception in the professional world. They assume tremendous responsibility for the life savings of their clients, yet are not required to have *any* liability insurance or meaningful personal reserves in order to pay their clients if mistakes are made or misconduct occurs. Most people are very surprised to learn that you can open an investment advisory business, or a stock brokerage, with virtually no cash of your own in the bank. There is a minimal net capital requirement imposed by FINRA, but that is typically a $5,000 requirement. It is meaningless. There are no federal or state agencies that will protect investors if an advisers' conduct causes significant losses and the adviser cannot or will not pay a court judgment or arbitration award. Neither SIPC – the Securities Investor Protection Corporation – nor the FDIC – the Federal Deposit Insurance Corporation -- provide assistance for investors who are victims of misconduct in all but the rarest of cases. I have had only one case in thirty years where SIPC coverage actually helped an investor, and that case involved organized crime masquerading as a brokerage firm.

The fact is that investors have no recourse if they are the victims of fraud or negligence and their adviser has chosen not to carry insurance, and does not have the resources to pay an award.

Most investors that have disputes with a stockbroker have to file arbitration with FINRA. It is difficult for investors to prevail in those cases. In fact, fewer than 45 percent of investors who file such claims and go to arbitration actually get an award in their favor, according to FINRA's own statistics available on its website, *finra.org*. And, after going through the entire arbitration process, which typically takes between 14-18 months, even where the investors do prove their case to the satisfaction of the FINRA arbitration panel, investors run a very high risk of never being paid. According to an article dated February 25, 2016 in *The Wall Street Journal* by Jean Eaglesham, more than $24 million of arbitration awards issued in 2014 remained unpaid as of the date of the article. FINRA does not dispute this statistic.

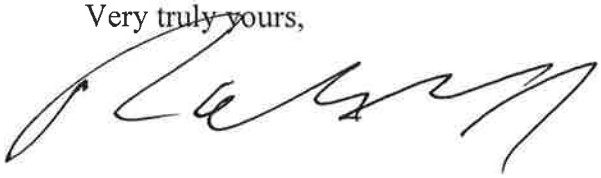
The unpaid award statistic is bad, but it is only the tip of the iceberg. The reality is that, for most investors who have been abused by a small brokerage or advisory firm, no one will file claims for them because the experienced lawyers know that there is a high likelihood that, even if they win, the clients will never be paid. In my practice, I have advised many, many defrauded investors not to spend money pursuing a claim because of the high likelihood of non-payment. I give that advice a few times a month at least, and in fact I raised it this morning with

an accountant who called me about a group of his clients who allege they were the victims of a penny stock fraud scheme.

FINRA is well aware of this problem. Richard Ketchum, who retired as its chief executive last year, said "One way or another, there should be a fund to address this [unpaid award problem] for small investors who are harmed by this." In my role on the FINRA National Arbitration and Mediation Committee, I have asked FINRA to establish a fund for unpaid awards. Others on the committee have done so as well as well. FINRA is not opposed to the idea, but regrettably, the industry has not done anything to meaningfully address the problem.

Oregon should take a stance and begin to address this problem and protect its citizens. I urge you to support SB 96.

Very truly yours,



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