BROKER–DEALERS AND INVESTMENT ADVISERS: THE ADMINISTRATION'S PLANS FOR THE FUTURE OF REGULATION

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INTRODUCTION

If someone asked you the difference between a broker–dealer and an investment adviser, would you be able to give them a straight answer? Elisse B. Walter, Commissioner of the Securities and Exchange Commission (SEC), cannot.[1] Today, most retail investors find themselves in a similar position when choosing between a broker–dealer and an investment adviser.[2]

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1. *See* Elisse B. Walter, Comm'r, U.S. Sec. & Exch. Comm'n, Speech at the Mutual Fund Directors Forum Ninth Annual Policy Conference: Regulating Broker-Dealers and Investment Advisers; Demarcation or Harmonization? (May 5, 2009), http://www.sec.gov/news/speech/2009/spch050509ebw.htm [hereinafter Walter Speech] (noting that broker–dealers and investment advisers "provide practically indistinguishable services to retail investors" and that the line between the two professions is continuing to blur).

2. *See* ANGELA A. HUNG ET AL., INVESTOR AND INDUSTRY PERSPECTIVES ON

Given that broker–dealers and investment advisers provide similar services, one would assume that the two professions are regulated in a similar fashion; yet they are not.[3] In fact, the regulation of broker–dealers and investment advisers is so disparate that it has allowed individuals like Bernie Madoff to perpetuate some of the biggest investment frauds in history.[4] In response to mounting concerns over the stability of the financial markets, the Obama Administration has set in motion a sweeping overhaul of the financial regulatory system, including a reconstruction of broker–dealer and investment-adviser regulations.[5] More specifically, the Administration is proposing new legislation that would harmonize the regulation of broker–dealers and investment advisers. Supporters of the harmonization approach argue that "[f]inancial services professionals who provide investment advice should be regulated under a unified system, and they each should come under the umbrella of a self-regulatory organization."[6]

This Recent Development discusses the broker–dealer and investment-adviser dynamic, looking at the present and what may be the future. This Recent Development argues in favor of the Administration's proposal, favoring a universal standard of care and conduct across the industry and self-regulation of both professions by the Financial Industry Regulatory Authority (FINRA), and concludes that such an arrangement would be the most efficient and effective solution.

INVESTMENT ADVISERS AND BROKER-DEALERS 117 (2008), http://www.sec.gov/news/press/2008/2008-1_randiabdreport.pdf (concluding that many investors, despite a long history with financial-service professionals, do not understand the difference between broker–dealers and investment advisers).

3. *See* Mary L. Schapiro, Chairman, U.S. Sec. & Exch. Comm'n, Address Before the New York Financial Writers' Association Annual Awards Dinner (June 18, 2009), http://www.sec.gov/news/speech/2009/spch061809mls-2.htm (discussing the vast regulatory differences between investment-adviser and broker–dealer regulation, despite convergence of practice).

4. *See* Timothy F. Geithner, Sec'y, U.S. Dep't of the Treasury, Statement Before the U.S. House of Representatives Comm. on Fin. Servs. 7–8 (Mar. 26, 2009), http://www.house.gov/apps/list/hearing/financialsvcs_dem/geithner032609.pdf (concluding that the Madoff scandal made it clear that regulatory gaps needed to be closed).

5. *See* Kevin Drawbaugh, *U.S. Financial Regulation Reforms Outlined*, REUTERS, June 15, 2009, http://www.reuters.com/article/wtUSInvestingNews/idUSTRE55E2G120090615 (discussing the Administration's plans to address critical weaknesses in the financial system).

6. *See* Sara Hansard, *Advisers Should Be Covered by Fiduciary Umbrella, SEC's Walter Says*, INVESTMENTNEWS, May 6, 2009, http://www.investmentnews.com/article/20090506/REG/905069966 (discussing Securities and Exchange Commission (SEC) Commissioner Elisse Walter's speech at the Mutual Fund Directors Forum Ninth Annual Policy Conference on May 5, 2009).

I. BACKGROUND

Investment advisers are regulated by the SEC through the Investment Advisers Act of 1940.[7] An *investment adviser* is defined as "any person who, for compensation, engages in the business of advising others . . . or who, . . . as part of a regular business, issues or promulgates analyses or reports concerning securities . . . ."[8] Investment advisers are held to a fiduciary-duty standard of care and must always act in the best interest of the client.[9] The client's interests must be paramount in any action.[10] There is no self-regulatory organization (SRO) for investment advisers, which means that regulation is left up to the SEC and state securities authorities.[11] The SEC is responsible for about 11,000 registered adviser firms.[12]

Broker–dealers are regulated by the SEC under the Securities Exchange Act of 1934.[13] The term *broker–dealer* represents two primary functions in the securities industry. A *broker* is broadly defined as any person who, as an agent, "effect[s] transactions in securities for the account of others."[14] A *dealer* is defined as any person who, as a principal, transacts securities for his or her own account.[15] Traditionally, when retail investors bought and sold securities through broker–dealers, any advice they received was only incidental to the business of the broker–dealer firm and was thus exempted from the requirements under the Investment Advisers Act.[16] Broker–dealers are subject to a suitability standard of care, meaning that any investments bought by a customer need only be suitable for that customer's purposes, and the interests of the customer may not necessarily be those of the broker–dealer.[17]

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7. *See* 15 U.S.C. § 80b (2006).

8. *See* § 80b-2(a)(11).

9. *See* § 80b-6(1)–(4) (stating that the SEC may enforce by any reasonable means); *see also* Mark J. Astarita, Registration and Regulation of Investment Advisers, http://www.seclaw.com/docs/RIAOverview.htm (last visited on Nov. 20, 2009).

10. *See* § 80b-6(1)–(4).

11. *See* Doug Halonen, *Madoff Scandal Spurs SRO Talk*, PENSIONS & INVESTMENTS, Jan. 12, 2009, *available at* http://www.pionline.com/article/20090112/PRINTSUB/901109970 (discussing how new regulatory proposals would subject money managers to SRO jurisdiction for the first time).

12. *See* Zachary A. Goldfarb, *Investment Advisers Would Face More Scrutiny Under SEC Proposal*, WASH. POST, May 15, 2009, at A13, *available at* http://www.washingtonpost.com/wp-dyn/content/article/2009/05/14/AR2009051403970.html?hpid=topnews.

13. *See* § 78*o*.

14. § 78c(a)(4)(A).

15. *See* § 78c(a)(5)(A).

16. *See* § 80b-2(a)(11)(c).

17. *See* Luis A. Aguilar, Comm'r, U.S. Sec. & Exch. Comm'n, Speech at the International Institute for the Regulation and Inspection of Investment Advisers: The Globalization of Investment Advisers—How Will Regulators Respond? (June 23, 2009), http://www.sec.gov/news/speech/2009/spch062309laa.htm (describing the suitability

FINRA is the SRO responsible for broker–dealers and oversees 4,900 firms employing 650,000 registered representatives.[18] The SRO is unique because it is not a taxpayer-funded government agency, yet it still has adjudicatory and rulemaking functions. FINRA can enforce federal securities laws as well as develop, implement, and enforce its own rules and regulations.[19]

From 2008 to the present, the financial sector has experienced great turmoil and uncertainty. The Obama Administration has unveiled a series of proposed financial reforms in response.[20] One of the most significant proposed reforms from the Administration involves the homogenization of the standard of care for broker–dealers and investment advisers, which could have the effect of bringing both industries under the direction of one SRO.[21] In light of the recent frauds perpetuated by Bernard Madoff and Allen Stanford, the Administration has correctly identified homogenization of standards and consolidation of regulation under one SRO as salient issues.

II. MADOFF AND STANFORD: STATUS QUO MUST GO

Bernie Madoff's Ponzi scheme rocked the world and shattered confidence in a market that was already reeling from a recession.[22] The $50 billion Ponzi scheme gave the appearance of returns by using money from new clients to pay off old clients and making no actual investments or growth.[23] Consequently, thousands of investors and charitable

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standard in greater detail, including that at a minimum, a broker–dealer must make certain inquiries prior to making recommendations to a customer). *See generally* Brown v. E.F. Hutton Group, Inc., 991 F.2d 1020, 1031 (2d Cir. 1993) (describing the five-part test to prove a violation of the suitability standard).

18. *See* Rick Ketchum, Chairman & Chief Executive Officer, Fin. Indus. Regulatory Auth., Speech at New York University Pollack Center for Law and Business (May 1, 2009), http://www.finra.org/Newsroom/Speeches/Ketchum/P118626 (noting that the Financial Industry Regulatory Authority (FINRA) acts as "the primary examiner and rule enforcer" of the firms and their employees).

19. *See* FINRA, About the Financial Industry Regulatory Authority, http://www.finra.org/AboutFINRA/index.htm (last visited Sept. 14, 2009).

20. *See* Washington Wire, http://blogs.wsj.com/washwire (June 17, 2009, 14:14 EST) (outlining Obama's proposals to regulate financial firms and financial markets and to protect consumers and investors).

21. *See id.* (imposing "duties of care" for stock brokers and financial advisers); Posting of David Gaffen to MarketBeat, http://blogs.wsj.com/marketbeat (Jan. 28, 2009, 9:59 EST) (recounting how recent testimony and expert opinion points to FINRA possibly taking over as the self-regulatory authority (SRO) for investment advisers).

22. *See* Robert Lenzner, *Bernie Madoff's $50 Billion Ponzi Scheme*, FORBES.COM, Dec. 12, 2008, http://www.forbes.com/2008/12/12/madoff-ponzi-hedge-pf-ii-in_rl_1212croesus_inl.html (characterizing the scandal as a "shocking revelation" and discussing subsequent market fallout).

23. *See* David Ellis, *Congress Looks for Answers in Madoff Scandal*,

organizations were completely wiped out. Almost as shocking as the scheme itself were revelations that Madoff's scam remained hidden for years despite several investigations by regulatory authorities.[24] Madoff registered his asset management business as an investment adviser with the SEC.[25] As a result, the SEC had sole jurisdiction to investigate that side of his organization under the Investment Advisers Act of 1940.[26] The SEC was warned several times by Boston investment banker Harry Markopolos over the six years prior to Madoff's collapse that Madoff's investment advisory business was producing impossible returns and should be investigated.[27] Yet little was done to address these concerns. In fact, the SEC never cracked the Madoff case; it was Madoff himself who confessed to his sons who then alerted the authorities.[28] While the exact nature of the SEC's deficiencies in this matter has yet to be addressed, the fact that a fraud of this magnitude went by unnoticed, despite credible concerns and warnings, indicates that the SEC may not be equipped to regulate the industry adequately.

Compounding this matter is the issue of compartmentalization—where two organizations that have the same fundamental purpose may not necessarily have the same reach. Recall that FINRA only has authority to regulate broker–dealers. Madoff had another business that was engaged in legitimate broker–dealer operations and FINRA had investigated that business in the past.[29] But while conducting their investigations, FINRA was unaware that the Ponzi scheme was being carried out on the same premises. While FINRA has taken fire in the press for failing to uncover Madoff's scheme, FINRA maintains that, statutorily, it could not have

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CNNMONEY.COM, Jan. 5, 2009, http://money.cnn.com/2009/01/05/news/companies/madoff_hearing/index.htm.

24. *See, e.g.*, Kara Scannell, *Madoff Chasers Dug for Years, to No Avail*, WALL ST. J., Jan. 5, 2009, at C1 (noting that the SEC had investigated Madoff at least eight times in the past sixteen years).

25. *See id.*

26. *See* 15 U.S.C. § 80a-41(a) (2006).

27. *See* Scannell, *supra* note 24 (mentioning that Markopolos began warning the agency as early as 2001); Ross Kerber, *The Whistleblower*, BOSTON GLOBE, Jan. 8, 2009, at A1, *available at* http://www.boston.com/business/articles/2009/01/08/the_whistleblower/?page=1 (discussing Markopolos's involvement at length and noting that he was relentless in trying to warn the SEC).

28. *See* David Voreacos & David Glovin, *Madoff Confessed $50 Billion Fraud Before FBI Arrest*, BLOOMBERG.COM, Dec. 12, 2008, http://www.bloomberg.com/apps/news?pid=20601087&sid=aYzclQY1HkVE.

29. *See* Rachelle Younglai, *FINRA Defends Its Role in Madoff Scandal*, REUTERS, Jan. 14, 2009, http://www.reuters.com/article/topNews/idUSTRE50E0EQ20090115 (noting that FINRA used lack of jurisdiction by statute as a defense to criticism for not detecting the Madoff scandal earlier).

investigated Madoff's advisory business even if it had felt compelled to.[30]

Less than three months after Madoff's confession, the SEC charged Allen Stanford with operating an $8 billion Ponzi scheme through his Stanford Group.[31] Unlike Madoff, the allegations against Stanford are pending trial, but the story alleged is a familiar one: an investment-advisory firm promises a product that seems improbably profitable and investors end up irreparably harmed.[32] Again, heated criticism has been directed at the SEC, but in this case the compounding issues stretch beyond compartmentalization and include questions of international jurisdiction and simple manpower.[33]

These two massive frauds, totaling nearly $60 billion during a severe recession, have heavily influenced the agenda of broader financial reform in the United States. The Administration has set forth a plan to homogenize the regulatory landscape for broker–dealers and investment advisers.[34] In recognizing that the present system must change, the Administration and its proposed reforms will go a long way in addressing some of the issues and oversights that have contributed to the current state of affairs.

III. THE MOVE TOWARD A UNIVERSAL REGULATORY FRAMEWORK

The Administration, following the same line of thought as Commissioner Walter,[35] seems to be approaching homogenization on two

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30. *See* Scannell, *supra* note 24 (describing FINRA's position that in spite of its investigations of Madoff's technical and reporting violations as a broker–dealer, FINRA did not have legal access to documents that would have allowed it to investigate Madoff more fully).

31. *See* Julie Creswell et al., *Fraud Parade: $8 Billion Case Is Next in Line*, N.Y. TIMES, Feb. 18, 2009, at A1 (describing the Stanford fraud in detail, which involved misleading investors into believing that certain purchases were safe by advertising investments in liquid securities that could be easily bought and sold).

32. *See id.* (pointing out the similarities between the Stanford and Madoff frauds and the SEC's failures in both).

33. *See* Alison Fitzgerald & Michael Forsythe, *Stanford Coaxed $5 Billion as SEC Weighed Powers*, BLOOMBERG.COM, Apr. 16, 2009, http://www.bloomberg.com/apps/news?sid=ae5qTPLFTvpg&pid=20601109 (noting that some of Stanford's operations were offshore, which causes jurisdictional uncertainty for the SEC); Robert Chew, *Can Mary Schapiro Revitalize the SEC?*, TIME.COM, Jan. 27, 2009, http://www.time.com/time/business/article/0,8599,1874218,00.html (noting the SEC's declining enforcement staff and the consensus among experts that the agency lacks the resources and manpower it needs to regulate effectively).

34. *See* Washington Wire, *supra* note 20; *see also* Sara Hansard, *Obama Administration to Create a Fiduciary Standard for Broker-Dealers*, INVESTMENT NEWS, June 17, 2009, http://www.investmentnews.com/article/20090617/REG/906179961 (discussing financial advisers' support of the Administration's proposal "to establish a fiduciary standard for broker-dealers offering investment advice").

35. *See* Walter Speech, *supra* note 1 (favoring the "harmonization approach," which would involve rulemaking to harmonize the broker–dealer and investment-adviser regimes).

fronts: first by introducing a universal standard of care for broker–dealers and investment advisers, and second by bringing investment advisers under an SRO, ideally the same SRO as broker–dealers (FINRA).[36] The rationale for these changes is compelling. As recognized by Chairman Schapiro, today there is little functional difference between most broker–dealer and investment-adviser operations.[37] Major broker–dealers now operate in the investment-advice business as well, blurring the lines between these professions and making compartmentalized regulation ineffective and obsolete.[38] By harmonizing regulation, the Administration will eliminate the regulatory gaps that exist between investment advisers and broker–dealers, thus reducing the likelihood of a Madoff or Stanford-type scandal from occurring again in the future. Each of the two proposed changes will be discussed in turn.

A. Common Standard of Care

The distinction between the fiduciary-duty standard of investment advisers and the suitability standard of broker–dealers would cease to exist under the new proposal, which advocates for a universal standard in their place.[39] At first the Administration advocated on behalf of a universal fiduciary-duty standard, which would require broker–dealers to always act in the best interests of the customer, much like investment advisers.[40] This is unlikely to be implemented in its purest form. As Madoff and Stanford have demonstrated, the fiduciary duty, which they were supposedly required to uphold, means little if the intent is to defraud from the outset. Instead, a more likely outcome is a strengthening of the fiduciary-duty concept with the rules-based system of conduct that governs the suitability standard.[41]

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36. *See supra* note 21 and accompanying text.

37. *See* Schapiro, *supra* note 3 (describing how the two fields have converged to the point where they are virtually indistinguishable, especially from the lay consumer's perspective).

38. *See* HUNG ET AL., *supra* note 2, at xvi–xviii (describing an increase in broker–dealers who are also registered as investment advisers and an increase in broker–dealers who expect to perform advisory functions in the future).

39. *See* Helen Kearney, *The 'F' Word Stirs up Controversy*, ON WALL STREET, July 2009, at 43, http://www.onwallstreet.com/ows_issues/2009_7/the-f-word-stirs-up-controversy-2663141-1.html (presenting opposing views on the harmonization approach and fiduciary-duty standard from groups such as the Investment Adviser Association and the Securities Industry and Financial Markets Association).

40. *See* Hansard, *supra* note 34 (reporting that the Administration's regulatory reform plan included a proposed fiduciary duty for broker–dealers).

41. *See* Sara Hansard, *Schapiro: Regs Governing Advisers Cannot Be Based Only on Fiduciary Duty*, INVESTMENT NEWS, June 19, 2009, http://www.investmentnews.com/article/20090619/REG/906199968 (describing the SEC Chairman's recognition that fiduciary duty alone would be insufficient and that a more

The likely intention behind placing a fiduciary duty on broker–dealer operations is to recognize that many brokers are increasingly offering fee-based services, where advice may be a prominent part of that service.[42] Given this trend, it makes sense to introduce a more comprehensive standard of care, such as the fiduciary duty, which aligns the broker's interests with the customer's interests. However, Chairman Schapiro herself has noted that fiduciary duty alone is insufficient to completely protect investors.[43] By requiring investment advisers and broker–dealers to also follow the rules-based regulatory regime formed around the suitability standard, a clear framework of conduct can be laid out, thereby reducing uncertainty and providing both the customer and the financial service provider with mutual understanding. Additionally, a rules-based conduct standard makes enforcement much easier, as regulatory violations are clear and systems of examination can be developed and implemented across the industry, reducing investigatory costs and delays.[44]

Naturally, multiple parties have voiced discontent with the proposed administrative action. Many large financial institutions have registered or bought brokerages that are only subject to a suitability standard.[45] A change to the fiduciary-duty standard may cut into broker profits by forcing brokerages to sell their clients the lowest cost products available.[46] These firms may fight the proposal on the basis of lost profits and the costs of expanding compliance. Conversely, many smaller investment adviser firms are against the implementation of any rules-based regulation such as the suitability standard.[47] These smaller firms make up the vast majority of

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harmonized regulatory approach would be better).

42. Fee-based brokerage services charge customers either a flat fee or a fee based on the amount of assets in the account. *See* HUNG ET AL., *supra* note 2, at 15 (describing fee-based broker services and their increasing popularity in the 1990s).

43. *See* Hansard, *supra* note 41 and accompanying text (quoting the SEC Chairman as stating that fiduciary standards are "not a panacea to deter . . . fraud").

44. *See* Troy A. Paredes, *Corporate Governance and Economic Development*, 28 REGULATION 34, 37 (2005), http://www.cato.org/pubs/regulation/regv28n1/v28n1-6.pdf (describing, in the context of corporate governance, how a rules-based regulatory system is more effective, straightforward, clear, predictable, and easy for the Judiciary to interpret and apply).

45. *See* Alexis Leondis & Elizabeth Hester, *Broker Fiduciary Plan Favors Investors, Roper Says*, BLOOMBERG.COM, June 19, 2009, http://www.bloomberg.com/apps/news?pid=20603037&sid=a8MJstZPh5xQ (describing recent brokerage purchases made by Morgan Stanley and Bank of America Corporation).

46. *See id.* (warning that a fiduciary standard could hurt brokers due to increased compliance and liability costs).

47. *See* David Tittsworth, Executive Director & Executive Vice President, Investment Adviser Ass'n, Statement to U.S. Senate Comm. on Banking, Housing, and Urban Affairs: Enhancing Investor Protection and the Regulation of Securities Markets—Part II, at 11–16 (Mar. 26, 2009), http://www.investmentadviser.org/eweb/docs/Publications_News/Comments_and_Statements/Current_Comments_Statements/Testimony_032609.pdf (describing the practical

investment-adviser firms and argue that the high costs of complying with rules-based regulation would damage their business.[48]

However, given the larger picture, the concerns of large broker–dealers and small investment advisers are misplaced. Authorities are correct in stating that the two professions now conduct essentially the same business. If the goal of regulation is to provide for investor protection and efficient markets, a unified standard of care would best achieve such goals. Large broker–dealers may not experience the costs they fear because they can spread their compliance practices across the entire organization and realize economies of scale. Smaller investment advisers will likely turn to technology in order to efficiently comply with a rules-based, suitability-standard type of regulation, but a large number of smaller advisers operating in concert can likely capture economies of scale as well.[49]

B. The Role of Self-Regulation

The second proposed change by the Administration, largely interpreted by the "harmonization" language, is bringing investment advisers under an SRO.[50] One of the major concerns the SEC has openly acknowledged in the aftermath of the Madoff and Stanford scandals is their lack of manpower to effectively police the 11,000 registered investment advisers.[51] Whereas broker–dealers can expect to be examined at least once a year by either FINRA or the SEC, it can take the SEC nearly a decade to get to some advisory firms.[52] By moving investment advisers under an SRO, the Administration can dramatically increase the manpower available to regulate the industry.[53] Allowing an SRO to regulate investment advisers

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differences between *fiduciary duty* and *suitability* and alleging that suitability and similar approaches are inappropriate for advisers).

48. *See id*. at 22 (describing how many advisory firms are small businesses with limited resources); Goldfarb, *supra* note 12 (explaining that the investment adviser industry is generally opposed to additional burdens because of the fear of increased costs without enough benefits).

49. *Cf*. Steven C. Deller, *Cooperation for Community Economic Development*, COMMUNITY ECONOMICS (Dep't of Agric. & Applied Econ., Univ. of Wis., Madison, Wis.), Oct. 2003 ("In the jargon of economists, by forming multicommunity collaborations, communities can capture economies of scale and scope . . . .").

50. *See* Gaffen, *supra* note 21 (describing industry indicators that self-regulation is increasingly likely).

51. *See* Rick Ketchum, Chairman and Chief Executive Officer, Fin. Indus. Regulatory Auth., Speech at the NAVA Government & Regulatory Affairs Conference (June 8, 2009), http://www.finra.org/Newsroom/speeches/Ketchum/P118889 (noting the 30% increase in investment-adviser registrations since 2005 and the lack of SEC resources to regulate investment advisers).

52. *See id.* (contrasting the 2,500 regulatory examinations FINRA conducts each year with the 1,500 the SEC conducts).

53. *See id.* (discussing Chairman Schapiro's statement that the SEC needs to rely on

would also eliminate the problem of compartmentalization because an SRO would have jurisdiction over advisory firms, reducing the chances of a Markopolos-type scenario from reoccurring and providing additional avenues for whistleblowers.

The self-regulatory model is an attractive one. Investment-advisory firms would pay into the regulatory program, reducing the taxpayers' burden.[54] The SEC would still maintain overriding jurisdiction—it would be able to adjudicate in the first instance or on appeal—but the SRO would allow the SEC to maximize its resources. The natural choice is to allow FINRA to expand its role to include the regulation of investment advisers.[55] However, many investment-adviser organizations oppose such a move. The Financial Planning Coalition (FPC), for example, would prefer to have the SEC maintain its role as the sole federal regulator working in conjunction with state regulatory agencies.[56] These opposing organizations claim the SEC is sufficiently capable of regulating the profession.[57] They assert that FINRA's rules-based regulatory system is inappropriate for investment advisers and incompatible with the fiduciary-duty standard of care.[58]

These investment-adviser organizations raise unfounded concerns. Like any industry, the reluctance to be regulated by an SRO has more to do with the reluctance toward increased regulation. When looking at the recent past, the arguments of the FPC become moot.[59] After considering the Madoff and Stanford cases and the SEC's own admissions of regulatory weaknesses, it is unlikely that the SEC will be able to improve the status quo of investment-adviser regulation. With regard to manpower and efficient allocation of resources, the industry-funded SRO model is the easiest solution to implement. Despite what critics like the Investment

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third parties to effectively regulate).

54. *See* Ketchum, *supra* note 18 (asserting that FINRA exists and operates at no cost to the taxpayer).

55. *See* Gaffen, *supra* note 21 (recounting statements and testimony from experts and industry insiders who agree that it is likely FINRA will be given authority to act as an SRO over investment advisers).

56. *See* Diahann W. Lassus, Financial Planning Coalition, Hearing Before the H. Comm. on Financial Servs. (July 17, 2009), http://www.cfp.net/downloads/Coalition_HFSC_Testimony.pdf (advocating a "professional oversight board" for financial planners and advisers, leaving the roles of the SEC and FINRA untouched).

57. *See* Tittsworth, *supra* note 47, at 21–22 (arguing that the SEC has the necessary expertise and experience to effectively govern investment advisers and that an additional bureaucratic layer would not significantly enhance investor protection).

58. *See id*. at 23–24 (asserting that FINRA's structure and rules-based approach would be inappropriate for adviser regulation).

59. *See supra* Part III.

Advisers Association argue,[60] a fully functional, well-established SRO already exists in FINRA.[61] Setting up a new SRO solely for investment advisers within FINRA would not incur new costs, and this additional oversight would further reduce the risk of compartmentalization. It is also incorrect to state that the rules-based regulation governing a suitability standard of care cannot be applied concurrently with a fiduciary-duty standard. Concrete rules governing the regulatory framework would greatly aid in avoiding the kinds of confusion, latency, and inefficiencies that allowed the Madoff and Stanford schemes to go undetected for so long.

CONCLUSION

The Administration has set out to remake the financial regulatory system. In focusing on the issue of investment-adviser regulation, the Administration has correctly identified the need to place broker–dealers and investment advisers under a universal standard of care.[62] These two professions have come to provide indistinguishable services and products. Maintaining separate standards for each profession makes little practical sense.[63] By having a clear universal standard, regulation can become more efficient and relevant.

The Administration may soon recognize the need for the self-regulation of investment advisers.[64] The most favorable choice would be to expand FINRA's jurisdiction to include investment advisers as well as broker–dealers. Having already established the need for a universal standard of care, where regulation of conduct between broker–dealers and investment advisers would be governed by the same standards and principles, it makes little sense to establish separate SROs and risk further compartmentalization of regulation. It is important to reiterate that compartmentalization was one of the factors that allowed the Madoff scandal to go by unnoticed for so long.[65] Additionally, FINRA would

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60. *See* Tittsworth, *supra* note 47, at 23 (arguing that SROs in general, and FINRA in particular, are inappropriate for investment-adviser regulation).

61. *See* Carol E. Curtis, *Merge FINRA and SEC's Adviser-Oversight Arm, Says TowerGroup*, SECURITIES INDUSTRY NEWS, Jan. 6, 2009, http://www.securitiesindustry.com/news/23111-1.html (describing the research firm TowerGroup's position that the SEC should leverage FINRA's existing resources in order to effectively carry out their role).

62. *See* Washington Wire, *supra* note 20.

63. *See* Schapiro, *supra* note 3 (arguing that the virtually identical services offered by both broker–dealers and investment advisers mean that virtually identical regulatory regimes should govern both); *see also* Walter, *supra* note 1 (emphasizing the convergence of services between broker–dealers and investment advisers).

64. *See* Gaffen, *supra* note 21 (noting that although the Administration has not yet called on FINRA, many industry professionals believe it will).

65. *See* David Z. Seide, *What Will the SEC Do Differently in the Aftermath of the*

augment the SEC's enforcement capabilities in the expanding investment-advisory field.

The Administration has set forth a credible plan for investment-adviser and broker–dealer regulation. Though the SEC and industry SROs must remain ever-vigilant in the face of defrauders and thieves, these proposals should go some way in arming the regulatory bodies with a structure and set of tools to make them more effective. What remains to be seen is how these reforms will be presented to Congress and how they may ultimately be implemented, but finally, the pieces are in play.

Madoff Scandal?, SECURITIES LITIGATION & REGULATION, Mar. 10, 2009, http://www.cm-p.com/siteFiles/News/C1AE54BDA125AD506B2595125B07F65E.pdf (predicting the elimination of compartmentalization between the SEC and SROs with Madoff as the catalyst for the change).