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Report to Congressional Addressees

January 2011

CONSUMER FINANCE

Regulatory Coverage Generally Exists for Financial Planners, but Consumer Protection Issues Remain

GAO-11-235

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Highlights

Highlights of GAO-11-235, a report to congressional addressees

January 2011

CONSUMER FINANCE

Regulatory Coverage Generally Exists for Financial Planners, but Consumer Protection Issues Remain

Why GAO Did This Study

Consumers are increasingly turning for help to financial planners—individuals who help clients meet their financial goals by providing assistance with such things as selecting investments and insurance products, and managing tax and estate planning. The Dodd-Frank Wall Street Reform and Consumer Protection Act mandated that GAO study the oversight of financial planners. This report examines (1) how financial planners are regulated and overseen at the federal and state levels, (2) what is known about the effectiveness of this regulation, and (3) the advantages and disadvantages of alternative regulatory approaches. To address these objectives, GAO reviewed federal and state statutes and regulations, analyzed complaint and enforcement activity, and interviewed federal and state government entities and organizations representing financial planners, various other arms of the financial services industry, and consumers.

What GAO Recommends

GAO recommends that (1) NAIC assess consumers' understanding of the standards of care associated with the sale of insurance products, (2) SEC assess investors' understanding of financial planners' titles and designations, and (3) SEC collaborate with the states to identify methods to better understand problems associated specifically with the financial planning activities of investment advisers. NAIC said it would consider GAO's recommendation and SEC provided no comments.

View GAO-11-235 or key components.
For more information, contact Alicia Puente Cackley at (202) 512-8678 or cackleya@gao.gov.

What GAO Found

There is no specific, direct regulation of "financial planners" *per se* at the federal or state level, but various laws and regulations apply to most of the services they provide. Financial planners are primarily regulated as investment advisers by the Securities and Exchange Commission (SEC) and the states, and are subject to laws and regulation governing broker-dealers and insurance agents when they act in those capacities. Federal and state agencies have regulations on marketing and the use of titles and designations that also can apply to financial planners.

The regulatory structure applicable to financial planners covers the great majority of their services, but the attention paid to enforcing existing regulation can vary and certain consumer protection issues remain. First, consumers may be unclear about when a financial planner is required to serve the client's best interest, particularly when the same financial planner provides multiple services associated with different standards of care. SEC is studying these issues with regard to securities transactions, but no complementary review is under way by the National Association of Insurance Commissioners (NAIC) related to the sale of high-risk insurance products. Second, financial planners can adopt numerous titles and designations, which vary greatly in the expertise or training that they signify, but consumers may not understand or be able to distinguish among them. SEC has a mandated review under way on financial literacy among investors and incorporating this issue into that review could assist in assessing further changes that may be needed. Finally, the extent of problems related to financial planners is not fully known because SEC generally does not track data on complaints, examination results, and enforcement activities associated with financial planners specifically, and distinct from investment advisers as a whole. A regulatory system should have data to identify risks and problem areas, and given that financial planning is a growing industry that has raised certain consumer protection issues, regulators could benefit from better information on the extent of problems specifically involving financial planning services.

A number of stakeholders have proposed different approaches to the regulation of financial planners, including (1) creation of a federally chartered board overseeing financial planners as a distinct profession; (2) augmenting oversight of investment advisers with a self-regulatory organization; (3) extending the fiduciary standard of care to more financial services professionals; and (4) specifying standards for financial planners and the designations that they use. While the views of stakeholder interests vary, a majority of the regulatory agencies and financial services industry representatives GAO spoke with did not favor significant structural change to the overall regulation of financial planners because they said existing regulation provides adequate coverage of most financial planning activities. Given available information, an additional layer of regulation specific to financial planners does not appear to be warranted at this time.

Contents

Abbreviations

Advisers Act	Investment Advisers Act of 1940
Dodd-Frank Act	Dodd-Frank Wall Street Reform and Consumer Protection Act
FINRA	Financial Industry Regulatory Authority
Form ADV	Uniform Application for Investment Adviser Registration
FTC	Federal Trade Commission
NAIC	National Association of Insurance Commissioners
NASAA	North American Securities Administrators Association
SEC	Securities and Exchange Commission

United States Government Accountability Office
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Congressional Addressees

Consumers are increasingly turning for help to professionals who describe themselves as financial planners for assistance with a broad range of services, such as selecting the right balance of stocks and bonds for an investment portfolio, choosing among insurance products, and tax and estate planning. Although there is no statutory or single definition of financial planning, it can be broadly defined as a systematic process that individuals use to achieve their financial goals. Between 2000 and 2008, the number of financial planners more than doubled and may continue to climb as more individuals are asked to take responsibility for their retirement savings and must choose among a growing array of investment options.

Some financial planning organizations have raised concerns that no single law governs providers of financial planning services, broadly describing this situation as a regulatory gap. Concerns also exist that financial planners may have an inherent conflict of interest in recommending products they may stand to benefit from selling. In addition, some consumer advocates believe consumers may be confused by the numerous titles and designations that financial planners can use. This report responds to a mandate included in Section 919C of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) that directed GAO to conduct a study on the oversight and regulation of financial planners. Our objectives are to address (1) how financial planners are regulated and overseen at the federal and state levels, (2) what is known about the effectiveness of regulation of financial planners and what regulatory gaps or overlap may exist, and (3) alternative approaches for the regulation of financial planners and the advantages and disadvantages of these approaches.

To address these objectives, we reviewed federal and selected state statutes and regulations applicable to financial planners. We also reviewed regulations issued by the Securities and Exchange Commission (SEC) and the Financial Industry Regulatory Authority (FINRA), and model laws developed by the National Association of Insurance Commissioners (NAIC) and by the North American Securities Administrators Association (NASAA). In addition, we reviewed applicable securities and insurance laws and regulations of five states—California, Illinois, North Carolina, Pennsylvania, and Texas. We also interviewed representatives of, and gathered documentation from, SEC, FINRA, the Federal Trade Commission (FTC), NAIC, and organizations representing the interests of consumers, financial planners, and various arms of the financial services industry. In addition, we gathered information on complaints and enforcement activity, as available, from SEC, FINRA, FTC, and selected state regulators and organizations. A more extensive discussion of our scope and methodology appears in appendix I.

We conducted this performance audit from June 2010 to January 2011 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

Financial planning typically involves a variety of services, including preparing financial plans for clients based on their financial circumstances and objectives and making recommendations for specific actions clients may take. In many cases, financial planners also help implement these recommendations by, for example, providing insurance products, securities, or other investments. Individuals who provide financial planning services may call themselves a variety of different titles, such as financial planner, financial consultant, financial adviser, trust advisor, or wealth manager. In addition, many financial planners have privately conferred professional designations or certifications, such as Certified Financial Planner®, Chartered Financial Consultant®, or Personal Financial Specialist.

The number of financial planners in the United States rose from approximately 94,000 in 2000 to 208,400 in 2008, according to the Bureau of Labor Statistics. The bureau projects the number will rise to 271,200 by 2018 because of the need for advisers to assist the millions of workers expected to retire in the next 10 years.[1] According to the bureau, 29 percent of financial planners are self-employed and the remaining 71

[1]While the Bureau of Labor Statistics reports these statistics using the term "financial adviser," bureau officials said that this term could be used interchangeably with financial planner. The bureau broadly defined a "personal financial adviser" as an individual who provides financial planning services and that private bankers or wealth managers would also be categorized as financial advisers.

percent are employees of firms, some of them large entities with offices nationwide that provide a variety of financial services. The median annual wage for financial planners was $68,200 in May 2009.

According to an analysis of the 2007 Survey of Consumer Finances, the most recent year for which survey results are available, in 2007 about 22 percent of U.S. households used a financial planner for investment and saving decisions and about 12 percent of U.S. households used a financial planner for making credit and borrowing decisions. Those households most likely to use a financial planner were those with higher incomes. For example, 37 percent of households in the top income quartile used a financial planner to make investment and saving decisions compared to 10 percent of households in the bottom quartile.[2]

Various Federal and State Laws and Regulations Apply to Financial Planners and Their Activities

Financial planners are primarily regulated by federal and state investment adviser laws, because planners typically provide advice about securities as part of their business. In addition, financial planners that sell securities or insurance products are subject to applicable laws governing broker-dealers and insurance agents. Certain laws and regulations can also apply to the use of the titles, designations, and marketing materials that financial planners use.

Financial Planners Are Primarily Regulated by Federal and State Investment Adviser Laws

There is no specific, direct regulation of "financial planners" *per se* at the federal or state level. However, the activities of financial planners are primarily regulated under federal and state laws and regulations governing investment advisers—that is, individuals or firms that provide investment advice about securities for compensation. According to SEC staff, financial planning normally includes making general or specific recommendations about securities, insurance, savings, and anticipated retirement.[3] SEC has issued guidance that broadly interprets the Investment Advisers Act of 1940 (Advisers Act) to apply to most financial planners, because the advisory services they offer clients typically include

[2]Our percentage estimates based on the 2007 Survey of Consumer Finances have 95 percent confidence intervals of +/- 2.5 percentage points or less. For example, we are 95 percent confident that between 8.2 and 11.8 percent of households in the bottom quartile used financial planners for investment decisions. See appendix I for additional information.

[3]Investment Adviser Act Release No. 1092, 52 Fed. Reg. 38400, 38401 (Oct. 16, 1987) (IA Rel. No. 1092).

providing advice about securities for compensation.[4] Similarly, NASAA representatives told us that states take a similar approach on the application of investment adviser laws to financial planners and, as a result, generally register and oversee financial planners as investment advisers. As investment advisers, financial planners are subject to a fiduciary standard of care when they provide advisory services, so that the planner "[is] held to the highest standards of conduct and must act in the best interest of [the adviser's] clients."[5]

SEC and state securities departments share responsibility for the oversight of investment advisers in accordance with the Advisers Act.[6] Under that act, SEC generally oversees investment adviser firms that manage $25 million or more in client assets, and the states that require registration oversee those firms that manage less.[7] However, as a result of section 410 of the Dodd-Frank Act, as of July 2011 the states generally will have registration and oversight responsibilities for investment adviser firms that manage less than $100 million in client assets, instead of firms that manage less than $25 million in assets as under current law.[8] This will result in the states gaining responsibility for firms with assets under management between $25 million and $100 million. As shown in figure 1, as of October 2010, of the approximately 16,000 investment adviser firms providing

[4]The Advisers Act defines an investment adviser as any person (i.e., individual or firm) who is in the business of providing advice, or issuing reports or analyses, regarding securities, for compensation. 15 U.S.C. § 80b-2(a)(11); IA Rel. No. 1092. In addition to applicable securities law, investment advice related to a retirement savings plan, such as a 401(k) plan, may also be subject to the Employee Retirement Income Security Act. The requirements under that act are outside the scope of this study. A forthcoming GAO report, GAO-11-119, will provide more information on investment advice in 401(k) plans.

[5]In *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 189-192 (1963), the U.S. Supreme Court recognized that the Advisers Act imposes a fiduciary duty on investment advisers. This standard imposes an affirmative duty to act solely in the best interests of the client. The investment adviser also must eliminate or disclose all conflicts of interest.

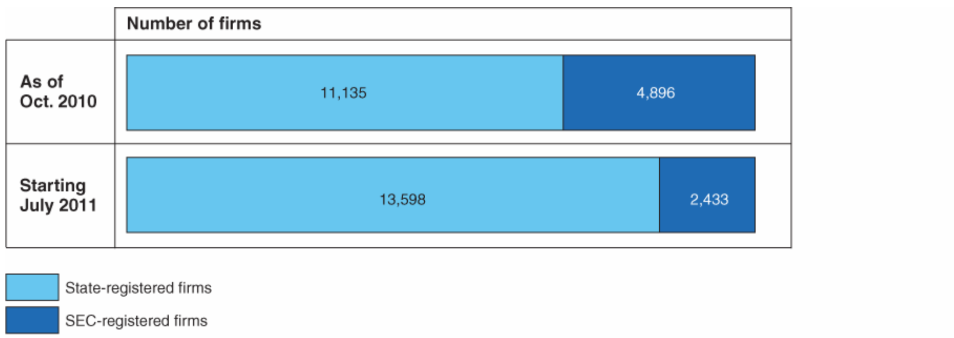
[6]15 U.S.C. § 80b-3a. The term investment adviser can refer to a person or firm. Investment adviser firms generally register with SEC or state securities departments as registered investment advisers. According to NASAA, certain natural persons that are employed by firms generally register with the state securities departments as investment adviser representatives.

[7]*Id.* Under 17 C.F.R. § 275.203A-1, SEC registration has been optional for certain investment advisers having assets under management between $25 and $30 million. Firms also may have a different basis for registering with SEC (other than the amount of client assets the firm has under management), such as whether the principal office and place of business are within a state that has no registration requirement.

[8]Pub. L. No. 111-203, § 410, 124 Stat. 1376, 1576-77 (2010).

financial planning services, the states were overseeing about 11,100 firms and SEC was overseeing about 4,900 such firms.[9] However, in July 2011 about 2,400 of investment adviser firms that provided financial planning services (15 percent of the 16,000 firms) may shift from SEC to state oversight.[10]

Figure 1: Change in Regulatory Oversight of Investment Adviser Firms Providing Financial Planning Services as a Result of the Dodd-Frank Act



Source: GAO.

SEC's supervision of investment adviser firms includes evaluating their compliance with federal securities laws by conducting examinations of firms—including reviewing disclosures made to customers—and investigating and imposing sanctions for violations of securities laws. According to SEC staff, in its examinations, the agency takes specific steps to review the financial planning services of investment advisers. For example, SEC may review a sample of financial plans that the firm prepared for its customers to check whether the firm's advice and investment recommendations are consistent with customers' goals, the contract with the firm, and the firm's disclosures.

[9]In registering with SEC or a state, investment adviser firms are required to report whether they provide financial planning services in Part 1A of the Uniform Application for Investment Adviser Registration, Item 5 G(1). SEC does not provide a definition of financial planning services for firms to use when completing the registration form. The total number of investment adviser firms overseen—including both those that do and do not provide financial planning services—is 15,016 for the states and 11,873 for SEC. For data on investment adviser firms, firms that were registered with both SEC and the states were counted with SEC-registered investment adviser firms.

[10]See 75 Fed. Reg. 77052 (Dec. 10, 2010) (SEC proposed rule, which, if finalized, would give advisers until August 20, 2011, to report the market value of their assets under management to the SEC as the first step in the process).

However, the frequency with which SEC conducts these examinations varies, largely because of resource constraints faced by the agency.[11] SEC staff told us that the agency examined only about 10 percent of the investment advisers it supervises in 2009. In addition, they noted that generally an investment adviser is examined, on average, every 12 to 15 years, although firms considered to be of higher risk are examined more frequently. In 2007, we noted that harmful practices could go undetected because investment adviser firms rated lower-risk are unlikely to undergo routine examinations within a reasonable period of time, if at all.[12]

According to NASAA, state oversight of investment adviser firms generally includes activities similar to those undertaken by SEC, including taking specific steps to review a firm's financial planning services. According to NASAA, states generally register not just investment adviser firms but also investment adviser representatives—that is, individuals who provide investment advice and work for a state- or federally registered investment adviser firm.[13]

Financial Planners Are Subject to Broker-Dealer and Insurance Laws When Acting in Those Capacities

In addition to providing advisory services, such as developing a financial plan, financial planners generally help clients implement the plan by making specific recommendations and by selling securities, insurance products, and other investments. SEC data show that, as of October 2010, 19 percent of investment adviser firms that provided financial planning

[11]GAO, *Securities and Exchange Commission: Steps Being Taken to Make Examination Program More Risk-Based and Transparent*, GAO-07-1053 (Washington, D.C.: Aug. 14, 2007). As we noted, since the detection of mutual fund trading abuses in late 2003, in light of limited resources, SEC has shifted its approach to examinations of investment advisers from one that focused on routinely examining all registered firms, regardless of risk, to one that focuses on more frequently examining those firms and industry practices at higher risk for compliance issues.

[12]GAO-07-1053. SEC reported in February 2010 that it is now placing a greater emphasis on fraud detection, in addition to identifying potential violations of securities laws and rules, strengthening procedures and internal controls to maximize limited resources, recruiting examiners with specialized skills, and increasing expertise through enhanced training.

[13]According to NASAA, New York, Minnesota, and Wyoming do not register investment adviser representatives, although New York and Minnesota do have certain examination and other requirements that must be met.

services also provided brokerage services, and 27 percent provided insurance.[14]

Financial planners that provide brokerage services, such as buying or selling stocks, bonds, or mutual fund shares, are subject to broker-dealer regulation at the federal and state levels. At the federal level, SEC oversees U.S. broker-dealers, and SEC's oversight is supplemented by self-regulatory organizations (SRO).[15] The primary SRO for broker-dealers is FINRA. State securities offices work in conjunction with SEC and FINRA to regulate securities firms. Salespersons working for broker-dealers are subject to state registration requirements, including examinations. About half of broker-dealers were examined in 2009 by SEC and SROs. Under broker-dealer regulation, financial planners are held to a suitability standard of care when making a recommendation to a client to buy or sell a security, meaning that they must recommend those securities that they reasonably believe are suitable for the customer.[16]

Financial planners that sell insurance products, such as life insurance or annuities, must be licensed by the states to sell these products and are subject to state insurance regulation. In contrast to securities entities (other than national banks) that are subject to dual federal and state oversight, the states are generally responsible for regulating the business of insurance. When acting as insurance agents, financial planners are

[14]The brokerage and insurance services provided by these investment adviser firms are not necessarily a part of their financial planning services. In addition, many financial planners may sell securities- or insurance-related products through affiliated brokers or agents.

[15]The primary law for regulating broker-dealers is the Securities Exchange Act of 1934, codified at 15 U.S.C. §§ 78a-78oo. Brokers effect transactions for the account of others, while dealers buy and sell securities for their own accounts. 15 U.S.C. § 78c. The term registered representative is generally used to refer to certain employees of a broker-dealer firm who are engaged in providing securities recommendations. Broker-dealers must be members of a qualifying self-regulatory organization (either a national exchange or a registered securities association). 15 U.S.C. § 78o(b)(8).

[16]Under NASD Conduct Rule 2310, a FINRA member making an investment recommendation to a customer must have grounds for believing that the recommendation is suitable for that customer's financial situation and needs. In November 2010, SEC approved FINRA's proposed new consolidated rules governing the suitability obligations of its members. 75 Fed. Reg. 71479 (Nov. 23, 2010). This rule, proposed FINRA Rule 2111, requires salespersons to have a reasonable basis for believing, based on adequate due diligence, that a recommendation of a transaction or strategy is suitable for at least some investors; that the recommendation is suitable for a specific customer, based on that customer's profile; and that a series of recommended transactions is not excessive and unsuitable for the customer.

subject to state standard of care requirements, which can vary by product and by state. As of October 2010, 32 states had adopted a previous version of the NAIC Suitability in Annuities Transactions Model Regulation, according to NAIC.[17] In general, this regulation requires insurance agents to appropriately address consumers' insurance needs and financial objectives at the time of an annuity transaction.[18] Thirty-four states had also adopted the Life Insurance Disclosure Model Regulation in a uniform and substantially similar manner as of July 2010, according to NAIC. This regulation does not include a suitability requirement, although it does require insurers to provide customers with information that will improve their ability to select the most appropriate life insurance plan for their needs and improve their understanding of the policy's basic features.

Financial planners that sell variable insurance products, such as variable life insurance or variable annuities, are subject to both state insurance regulation and broker-dealer regulation, because these products are regulated as both securities and insurance products. When selling variable insurance, financial planners are subject to FINRA sales practice standards requiring that such sales be subject to suitability standards.[19] In addition, other FINRA rules and guidance, such as those governing standards for communication with the public, apply to the sale of variable insurance products.[20] In addition, as previously discussed, 32 states also generally require insurance agents and companies to appropriately address a consumer's insurance needs and financial objectives at the time of an annuity transaction. However, in the past, we have reported that the effectiveness of market conduct regulation—that is, examination of the sales practices and behavior of insurers—may be limited by a lack of

[17]NAIC amended this model regulation in March 2010; according to NAIC, one state has adopted the updated model and additional states are expected to do so.

[18]According to NAIC, in 4 of these 32 states the regulation applies only when the consumers are senior citizens.

[19]NASD Notice to Members 96-86 outlines that variable contracts for insurance products are subject to suitability requirements.

[20]NASD Interpretive Material 2210-2 outlines guidance concerning communications with the public about variable life insurance and variable annuities. FINRA has proposed that this guidance be replaced by a separate new FINRA Rule 2211. See FINRA Rule Filing No. SR-FINRA-2009-070.

reciprocity and uniformity, which may lead to uneven consumer protection across states.[21]

Federal and State Laws and Regulations Can Apply to the Use of Marketing Materials and Financial Planning Titles and Designations

At the federal level, SEC and FINRA have regulations on advertising and standards of communication that apply to the strategies investment adviser firms and broker-dealers use to market their financial planning services. For example, SEC-registered investment advisers must follow SEC regulations on advertising and other communications, which prohibit false or misleading advertisements, and these regulations apply to investment advisers' marketing of financial planning services.[22] FINRA regulations on standards for communication with the public similarly prohibit false, exaggerated, unwarranted, or misleading statements or claims by broker-dealers, and broker-dealer advertisements are subject to additional approval, filing, and recordkeeping requirements and review procedures.[23] According to many company officials we spoke with, their companies responded to these requirements by putting procedures in place to determine which designations and titles their registered representatives may use in their marketing materials, such as business cards.

SEC and state securities regulators also regulate information that investment advisers are required to disclose to their clients. In the Uniform Application for Investment Adviser Registration (Form ADV), regulators have typically required investment adviser firms to provide new and prospective clients with background information, such as the basis of the advisory fees, types of services provided (such as financial planning services), and strategies for addressing conflicts of interest that may arise

[21]GAO, *Insurance Reciprocity and Uniformity: NAIC and State Regulators Have Made Progress in Producer Licensing, Product Approval and Market Conduct Regulation, but Challenges Remain*, GAO-09-372 (Washington, D.C.: Apr. 6, 2009). Reciprocity refers to the extent to which state regulators accept other states' regulatory actions. Uniformity refers to the extent to which states have implemented either the same, or substantially similar, regulatory standards and procedures.

[22]17 C.F.R. § 275.206(4)-1.

[23]NASD Rule 2210.

from their business activities.[24] Recent changes to Form ADV are designed to improve the disclosures that firms provide to clients. For example, firms must now provide clients with information about the advisory personnel on whom they rely for investment advice, including the requirements and applicability of any professional designations or certifications advisers may choose to include in their background information.

Most states regulate the use of the title "financial planner," and state securities and insurance laws can apply to the misuse of this title and other titles. For example, according to NASAA, at least 29 states specifically include financial planners in their definition of investment adviser.[25] According to NAIC, in many states, regulators can use unfair trade practice laws to prohibit insurance agents from holding themselves out as financial planners when in fact they are only engaged in the sale of life or annuity insurance products. However, as noted earlier, the effectiveness of the regulation of insurers' market conduct varies across states. In particular, in 2010 we noted inconsistencies in the state regulation of life settlements, a potentially high-risk transaction in which financial planners may participate.[26]

In addition, we were told some states had adopted regulations limiting the use of "senior-specific designations"—that is, designations that imply expertise or special training in advising senior citizen or elderly investors. According to NAIC, as of December 2010, 25 states had adopted in a uniform and substantially similar manner the NAIC Model Regulation on the Use of Senior-Specific Certifications and Professional Designations in the Sale of Life Insurance and Annuities, which limits the use of senior-specific designations by insurance agents. According to NASAA, as of December 2010, 31 states had adopted—and at least 9 other states were

[24]SEC and the states use Form ADV to register investment adviser firms and collect information from them. Part 2 of Form ADV provides information about the investment adviser and its business for use of the clients and is publicly available on the Investment Adviser Public Depository Web site. The SEC adopted amendments to Form ADV that were effective October 12, 2010, requiring Part 2 of Form ADV be written in a plain English narrative format. *See* Amendments to Form ADV, 75 Fed. Reg. 49,234 (Aug. 12, 2010) (to be codified at 17 C.F.R. pt. 275 and 279).

[25]The District of Columbia and Puerto Rico also include financial planners in their definitions of investment adviser, according to NASAA.

[26]GAO, *Life Insurance Settlements: Regulatory Inconsistencies May Pose a Number of Challenges*, GAO-10-775 (Washington, D.C.: July 9, 2010).

planning to adopt—the NASAA Model Rule on the Use of Senior-Specific Certifications and Professional Designations, which prohibits the misleading use of senior-specific designations by investment adviser representatives and other financial professionals.

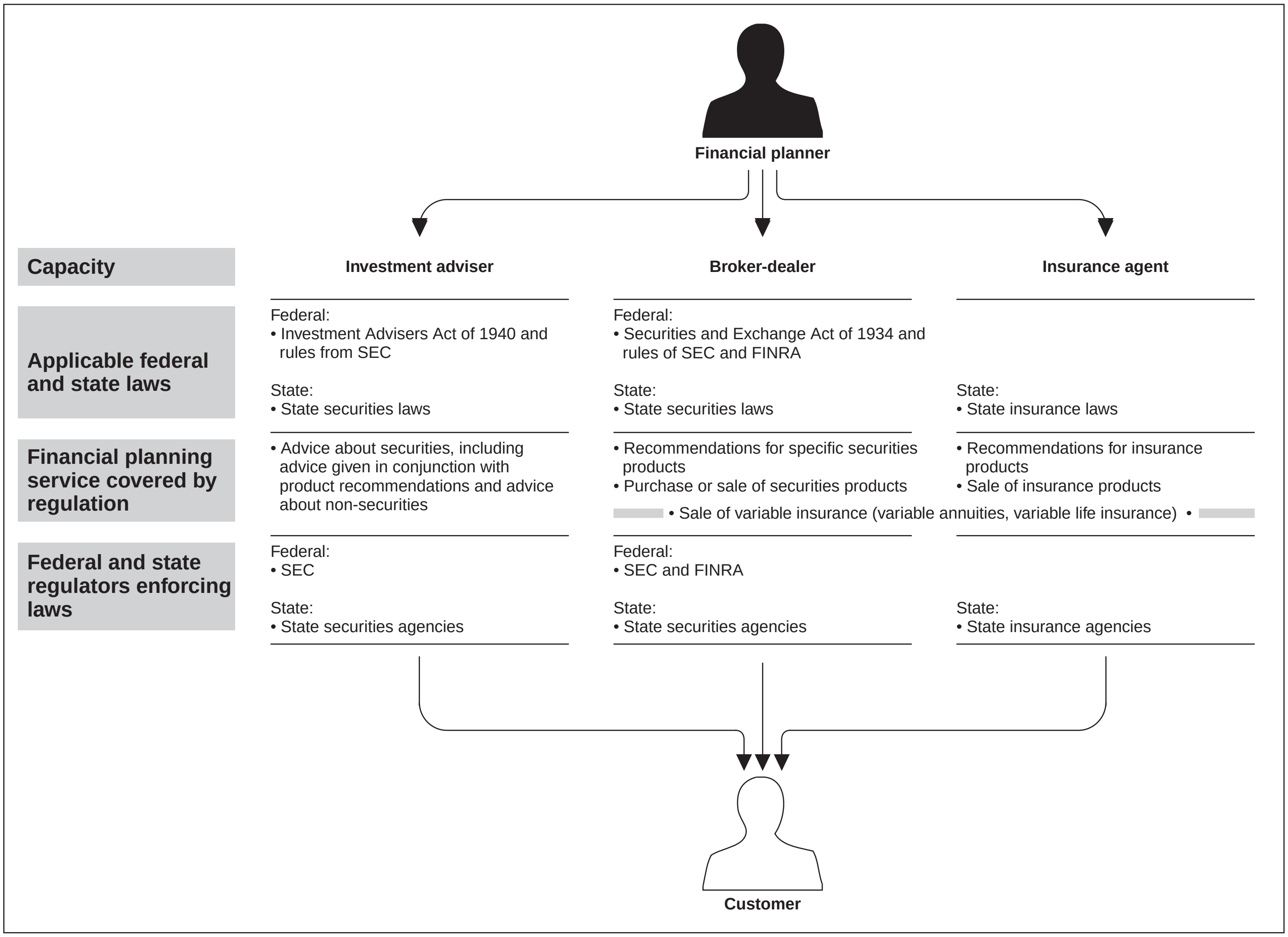
Regulatory Structure for Financial Planners Covers Most Activities, but Some Consumer Protection Issues Exist, and Data Tracking Complaints and Regulatory Actions against Planners Are Limited

The regulatory system for financial planners covers most activities in which they engage. However, enforcement of regulation may be inconsistent and some questions exist about consumers' understanding of the roles, standards of care, and titles and designations that a financial planner may have. The ability of regulators to identify potential problems is limited because they do not specifically track complaints, inspections, and enforcement actions specific to financial planning services.

Existing Regulation Covers Most Financial Planning Services

Although there is no single stand-alone regulatory body with oversight of financial planners, the regulatory structure for financial planners covers most activities in which they engage. As discussed earlier, and summarized in figure 2, the primary activities a financial planner performs are subject to existing regulation at the federal or state level, primarily through regulation pertaining to investment advisers, broker-dealers, and insurance agents. As such, SEC, FINRA, and NASAA staff, a majority of state securities regulators, financial industry representatives, consumer groups, and academic and subject matter experts with whom we spoke said that, in general, they believe the regulatory structure for financial planners is comprehensive, although, as discussed below, the attention paid to enforcing existing regulation has varied.

Figure 2: Summary of Key Statutes and Regulations That Can Apply to Financial Planners



Source: GAO.

Note: This figure highlights three major areas of regulatory oversight but is not comprehensive and does not include other regulatory regimes or practice standards that may be applicable to financial planners. In addition, not all investment advisers, broker-dealers, or insurance agents are financial planners.

As noted earlier, the activities a financial planner normally engages in generally include advice related to securities—and such activities make financial planners subject to regulation under the Advisers Act. One industry association and an academic expert noted that it would be very difficult to provide financial planning services without offering investment advice or considering securities. SEC staff told us that financial planners holding even broad discussions of securities—for example, what proportion of a portfolio should be invested in stocks—would be required to register as investment advisers or investment adviser representatives. In theory, a financial planner could offer only services that do not fall under existing regulatory regimes—for example, advice on household budgeting—but such an example is likely hypothetical and such a business model may be hard to sustain. SEC and NASAA staff, a majority of the state securities regulators we spoke with, and many representatives of the financial services industry told us that they were not aware of any individuals serving as financial planners who were not regulated as investment advisers or regulated under another regulatory regime. Some regulators and industry representatives also said that, to the extent that financial planners offered services that did not fall under such regulation, the new Bureau of Consumer Financial Protection potentially could have jurisdiction over such services.[27]

However, not everyone agreed that regulation of financial planners was comprehensive. One group, the Financial Planning Coalition, has argued that a regulatory gap exists because no single law governs the delivery of the broad array of financial advice to the public.[28] According to the coalition, the provision of integrated financial advice—which would cover topics such as selecting and managing investments, income taxes, saving for college, home ownership, retirement, insurance, and estate planning—is unregulated. Instead, the coalition says that there is patchwork regulation of financial planning advice, and it views having two sets of laws—one regulating the provision of investment advice and another regulating the sale of products—as problematic.

[27]Section 1011 of the Dodd-Frank Act established the Bureau of Consumer Financial Protection to regulate "the offering and provision of consumer financial products or services under the Federal consumer financial laws." A financial product or service is defined in section 1002(15)(A)(viii) of the act to include financial advisory services to consumers on individual financial matters, with the exception of advisory services related to securities provided by a person regulated by SEC or a state securities commission to the extent that such person acts in a regulated capacity. Accordingly, it appears that the bureau may have jurisdiction over financial planners to the extent that they may offer services that would not be under the jurisdiction of SEC or a state securities commission.

[28]The members of this coalition include the Certified Financial Planner Board of Standards, Inc.; the Financial Planning Association; and the National Association of Personal Financial Advisors.

In addition, although the regulatory structure itself for financial planners may generally be comprehensive, attention paid to enforcing existing statute and regulation has varied. For example, as noted earlier, due to resource constraints, the examination of SEC-supervised investment advisers is infrequent. Further, as also noted earlier, market conduct regulation of insurers—which would include the examination of the sales practices and behavior of financial planners selling insurance products—has been inconsistent. Some representatives of industry associations told us that they believed that a better alternative to additional regulation of financial planners would be increased enforcement of existing law and regulation, particularly related to fraud and unfair trade practices.

Certain professionals—including attorneys, certified public accountants, broker-dealers, and teachers—who provide financial planning advice are exempt from regulation under the Advisers Act if such advice is "solely incidental" to their other business activities.[29] According to an SEC staff interpretation, this exemption would not apply to individuals who held themselves out to the public as providing financial planning services, and would apply only to individuals who provided specific investment advice on anything other than "rare, isolated and non-periodic instances."[30] Banks and bank employees are also excluded from the Advisers Act and are subject to separate banking regulation.[31] The American Bankers Association told us that the financial planning activities of bank employees such as trust advisors or wealth managers were typically utilized by clients with more than $5 million in investable assets. The association noted that these activities were subject to a fiduciary standard and the applicable supervision of federal and state banking regulators.

Most regulators and academic experts and many financial services industry representatives we spoke with told us that there is some overlap in the regulation of individuals who serve as financial planners because

[29] 15 U.S.C. § 80b-2(a)(11); IA Rel. No. 1092(II)(B), at 38403. Under 15 U.S.C. § 80b-2(a)(11)(C), brokers and dealers also cannot receive any special compensation for their services in order to be exempt from registration as an investment adviser.

[30] *Id.*

[31] *Id.* The Advisers Act excludes bank and bank holding companies from the definition of investment adviser. Further, a bank and a bank holding company is an investment adviser under the act to the extent that the bank or bank holding company serves or acts as an adviser to a registered investment company. If such services are performed in a separate department or division of a bank, the department or division and not the bank itself is the investment adviser.

such individuals might be subject to oversight by different regulatory bodies for the different services they provide. For example, a financial planner who recommends and sells variable annuities as part of a financial plan is regulated as a registered representative of a broker-dealer as well as an insurance agent under applicable federal and state laws. However, some state regulators we spoke with told us that such overlap may be appropriate since the regulatory regimes cover different functional areas.

Consumers May Not Understand That Financial Planners Have Potential Conflicts of Interest When Selling Products

As seen in figure 3, financial planners are subject to different standards of care in their capacities as investment advisers, broker-dealers, and insurance agents.

- *Fiduciary Standard of Care*: As noted earlier, investment advisers are subject to a fiduciary standard of care—that is, they must act in their client's best interest, ensure that recommended investments are suitable for the client, and disclose to the client any material conflicts of interest.[32] According to SEC and NASAA representatives, the fiduciary standard applies even when investment advisers provide advice or recommendations about products other than securities, such as insurance, in conjunction with advice about securities.

- *Suitability Standard of Care When Recommending Security Products*: FINRA regulation requires broker-dealers to adhere to a suitability standard when rendering investment recommendations—that is, they must recommend only those securities that they reasonably believe are suitable for the customer.[33] Unlike the fiduciary standard, suitability rules do not necessarily require that the client's best interest be served. According to FINRA staff, up-front general disclosure of a broker-dealer's business activities and relationships that may cause conflicts of interest is not

[32]The SEC has, in effect, established rules of conduct for investment advisers, including requirements for disclosing conflicts of interest, obtaining the best execution on behalf of clients, allocating investments among clients fairly, ensuring that investments are suitable for clients, and ensuring that there is a reasonable basis for recommendations. SEC also requires investment advisers to maintain records pertaining to client accounts and business operations.

[33]A broker-dealer must have an adequate and reasonable basis for any recommendation and must make recommendations based on a customer's financial situation, needs and other securities holdings.

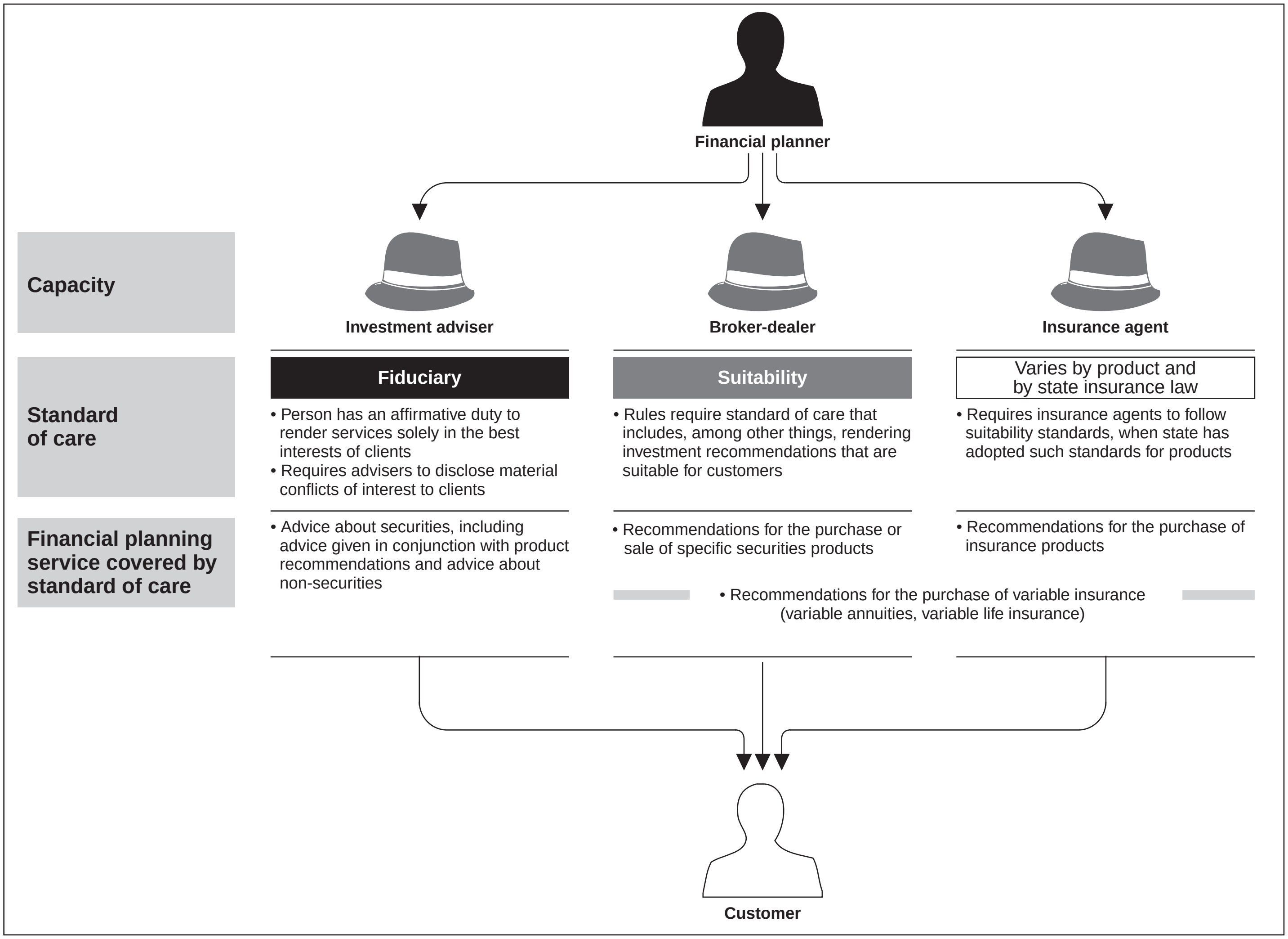
required.[34] However, according to SEC, broker-dealers are subject to many FINRA rules that require disclosure of conflicts in certain situations, although SEC staff also note that those rules may not cover every possible conflict of interest, and disclosure may occur after conflicted advice has already been given.[35]

- *Suitability Standard of Care When Recommending Insurance Products*: Standards of care for the recommendation and sale of insurance products vary by product and by state. For example, as seen earlier, NAIC's model regulations on the suitability standard for annuity transactions, adopted by some states but not others, require consideration of the insurance needs and financial objectives of the customer, while NAIC's model regulation for life insurance does not include a suitability requirement *per se*.

[34]Letter from Marc Menchel, Executive Vice President and General Counsel, FINRA, to Elizabeth M. Murphy, Secretary, SEC 4 (Aug. 25, 2010), available at http://www.finra.org/web/groups/industry/@ip/@reg/@guide/documents/industry/p121983.pdf.

[35]The standards of conduct for broker-dealers may also be based on antifraud provisions of the securities law and agency principles. Broker-dealers also have a duty of fairness in their contracts with a customer, which requires them to disclose material information that the customer would consider important as an investor. In addition, broker-dealers that handle discretionary accounts are generally thought to owe fiduciary obligations to their customers.

Figure 3: Differences in the Standards of Care Required of Financial Planners



Source: GAO.

Note: This figure is illustrative and is not comprehensive: financial planners may serve in capacities other than those shown here, and not all investment advisers, broker-dealers, and insurance agents serve as financial planners.

Conflicts of interest can exist when, for example, a financial services professional earns a commission on a product sold to a client. Under the fiduciary standard applicable to investment advisers, financial planners must mitigate any potential conflicts of interest and disclose any that remain. But under a suitability standard applicable to broker-dealers, conflicts of interest may exist and generally may not need to be disclosed up-front.[36] For example, as confirmed by FINRA, financial planners functioning as broker-dealers may recommend a product that provides them with a higher commission than a similar product with a lower commission, as long as the product is suitable and the broker-dealer complies with other requirements. Because the same individual or firm can offer a variety of services to a client—a practice sometimes referred to as "hat switching"—these services could be subject to different standards of care. As such, representatives of consumer groups and others have expressed concern that consumers may not fully understand which standard of care, if any, applies to a financial professional. As shown above, the standards of care—and the extent to which conflicts of interest must be disclosed—can vary depending on the capacity in which the individual serves.[37] A 2007 report by the Financial Planning Association stated that "it would be difficult, if not impossible, for an individual investor to discern when the adviser was acting in a fiduciary capacity or in a non-fiduciary capacity."[38] A 2008 SEC study conducted by the RAND Corporation, consisting of a national household survey and six focus group discussions with investors, found that consumers generally did not understand not only the distinction between a suitability and fiduciary standard of care but also the differences between broker-dealers and investment advisers.[39] Similarly, a 2010 national study of investors found that most were confused about which financial professionals are required to operate under a fiduciary standard that requires professionals to put their client's interest ahead of their own.[40]

[36]FINRA officials have stated that they believe that the regulation of broker-dealers—while lacking an express fiduciary duty—prescribes in great detail the conduct and supervision of broker-dealers who provide investment advice to retail customers.

[37]Black's Law Dictionary (9th ed. 2009) defines the term "conflict of interest" as a "real or seeming incompatibility between one's private interests and one's public or fiduciary duties."

[38]*Final Report on Financial Planner Standards of Conduct*, FPA Fiduciary Task Force, June 2007.

[39]Angela A. Hung et al., RAND Institute for Civil Justice, *Investor and Industry Perspectives on Investment Advisers and Broker-Dealers* (2008).

[40]Infogroup, Opinion Research Corporation, *U.S. Investors & The Fiduciary Standard: A National Opinion Survey*, September 15, 2010. The survey was conducted among a sample of 2,012 adults living in the continental United States, including 1,319 who identified themselves as investors. The survey was sponsored by AARP, the Consumer Federation of America, NASAA, the Investment Adviser Association, the Certified Financial Planner Board of Standards, the Financial Planning Association, and the National Association of Personal Financial Advisors.

Representatives of financial services firms that provide financial planning told us they believe that clients are sufficiently informed about the differing roles and accompanying standards of care that a firm representative may have. They noted that when they provide both advisory and transactional services to the same customer, each service—such as planning, brokerage, or insurance sales—is accompanied by a separate contract or agreement with the customer. These agreements disclose that the firm's representatives have different obligations to the customer depending on their role. In addition, once a financial plan has been provided, some companies told us that they have customers sign an additional agreement stating that the financial planning relationship with the firm has ended.

Recent revisions by SEC to Form ADV disclosure requirements were designed to address, among other things, consumer understanding of potential conflicts of interest by investment advisers and their representatives. Effective October 12, 2010, SEC revised Form ADV, Part 2, which financial service firms must provide to new and prospective clients.[41] The new form, which must be written in plain English, is intended to help consumers better understand the activities and affiliations of their investment adviser. It requires additional disclosures about a firm's conflicts of interest, compensation, business activities, and disciplinary information that is material to an evaluation of the adviser's integrity. Similarly, in October 2010 FINRA issued a regulatory notice requesting comments on a concept proposal regarding possible new disclosure requirements that would, among other things, detail for consumers in plain English the conflicts of interest that broker-dealers may have associated with their services.[42]

Section 913 of the Dodd-Frank Act requires SEC to study the substantive differences between the applicable standards of care for broker-dealers and investment advisers; the effectiveness of the existing legal or regulatory standards of care for brokers, dealers, and investment advisers; and consumers' ability to understand the different standards of care. SEC

[41]Amendments to Form ADV, 75 Fed. Reg. 49234 (Aug. 12, 2010) (requires investment advisers registered with SEC to provide new and prospective clients with a brochure and brochure supplements clearly setting forth a meaningful, current disclosure of the business practices, conflicts of interest and background of the investment adviser and its advisory personnel; and requires the brochures to be filed with SEC electronically, which will make them available to the public through its Web site).

[42]FINRA Regulatory Notice 10-54.

will also consider the potential impact on retail customers of imposing the same fiduciary standard that now applies to investment advisers on broker-dealers when they provide personalized investment advice. Under the act, SEC may promulgate rules to address these issues and is specifically authorized to establish a uniform fiduciary duty for broker-dealers and investment advisers that provide personalized investment advice about securities to customers. As a result, further clarification of these standards may be forthcoming. FINRA officials told us that they support a fiduciary standard of care for broker-dealers when they provide personalized investment advice to retail customers.

Consumer confusion on standards of care may also be a source of concern with regard to the sale of some insurance products. A 2010 national survey of investors found that 60 percent mistakenly believed that insurance agents had a fiduciary duty to their clients.[43] Some insurance products, such as annuities, are complex and can be difficult to understand, and annuity sales practices have drawn complaints from consumers and various regulatory actions from state regulators as well as SEC and FINRA for many years.[44] According to NAIC, many states have requirements that insurance salespersons sell annuities only if the product is suitable for the customer. However, NAIC notes that some states do not have a suitability requirement for annuities. Consumer groups and others have stated that high sales commissions on certain insurance products, including annuities, may provide salespersons with a substantial financial incentive to sell these products, which may or may not be in the consumer's best interest. As a result of section 989J of the Dodd-Frank Act, one type of annuity—the indexed annuity—is to be regulated by states as an insurance product, rather than regulated by SEC as a security, under certain conditions.[45]

SEC's pending study related to the applicable standards of care for broker-dealers and investment advisers will not look at issues of insurance that

[43]Infogroup, Opinion Research Corporation, *U.S. Investors & The Fiduciary Standard: A National Opinion Survey*, September 15, 2010.

[44]See, for example, Securities and Exchange Commission Rule 151A and Annuities: Issues and Legislation, CRS Report for Congress 7-7500 (July 29, 2010).

[45]State regulation applies so long as a state has adopted NAIC's Suitability in Annuity Transactions model regulation or if an insurance company adopts and implements practices on a nationwide basis that meet or exceed the minimum requirements established by NAIC's model regulation. Indexed annuities are products that guarantee a purchaser's principal and a certain rate of return, and offer a chance for additional returns linked to a securities index or indices.

fall outside of SEC's jurisdiction. NAIC has not undertaken a similar study regarding consumer understanding of the standard of care for insurance agents. As we reported in the past, financial markets function best when consumers understand how financial service providers and products work and know how to choose among them.[46] Given the evidence of consumer confusion about differing standards of care and given the increased risks that certain insurance products can pose, there could be benefits to an NAIC review of consumers' understanding of standards of care for high-risk insurance products.

Consumers May Be Confused about the Ways Financial Professionals Present Themselves to the Public

Individuals who provide financial planning services may use a variety of titles when presenting themselves to the public, including financial planner, financial consultant, and financial adviser, among many others. However, evidence suggests that the different titles financial professionals use can be confusing to consumers. The 2008 RAND study found that even experienced investors were confused about the titles used by broker-dealers and investment advisers, including financial planner and financial adviser. Similarly, in consumer focus groups of investors conducted by SEC in 2005 as part of a rulemaking process, participants were generally unclear about the distinctions among titles, including broker, investment adviser, and financial planner.[47] In addition, a representative of one consumer advocacy group has expressed concern that some financial professionals may use as a marketing tool titles suggesting that they provide financial planning services, when in fact they are only selling products. One industry group, the Financial Planning Coalition, also has noted that some individuals may hold themselves out as financial planners without meeting minimum training or ethical requirements. Federal and state regulators told us they generally focused their oversight and enforcement actions on financial planners' activities rather than the titles they use. Moreover, NASAA has said that no matter what title financial planners use, most are required to register as investment adviser representatives and must satisfy certain competency requirements,

[46]GAO, *Financial Regulation: A Framework for Crafting and Assessing Proposals to Modernize the Outdated U.S. Financial Regulatory System*, GAO-09-216 (Washington, D.C.: Jan. 8, 2009).

[47]*Results of Investor Focus Group Interviews About Proposed Brokerage Account Disclosures.* Report to the Securities and Exchange Commission by Siegel & Gale LLC and Gelb Consulting Group, Inc., Mar. 10, 2005.

including passing an examination or obtaining a recognized professional designation.[48]

Financial planners' professional designations are typically conferred by a professional or trade organization. These designations may indicate that a planner has passed an examination, met certain educational requirements, or had related professional experience. Some of these designations require extensive classroom training and examination requirements and include codes of ethics with the ability to remove the designation in the event of violations. State securities regulators view five specific designations as meeting or exceeding the registration requirements for investment adviser representatives, according to NASAA, and allow these professional designations to satisfy necessary competency requirements for prospective investment adviser representatives.[49] For example, one of these five designations requires a bachelor's degree from an accredited college or university, 3 years of full-time personal financial planning experience, a certification examination, and 30 hours of continuing education every 2 years.

The criteria used by organizations that grant professional designations for financial professionals vary greatly. FINRA has stated that while some designations require formal certification procedures, including examinations and continuing professional education credits, others may merely signify that membership dues have been paid. The Financial Planning Coalition and The American College, a nonprofit educational institution that confers several financial designations, similarly told us that privately conferred designations range from those with rigorous competency, practice, and ethical standards and enforcement to those that can be obtained with minimal effort and no ongoing evaluation.

[48]According to NASAA, all but three states—New York, Minnesota, and Wyoming—register investment adviser representatives and require that they pass either the Series 65 (Uniform Investment Adviser Law Examination) or the Series 66 (Uniform Combined State Law Examination), or obtain a recognized professional designation. While New York and Minnesota do not register individual investment adviser representatives, their state laws require that the representatives meet other requirements, such as passing certain examinations or obtaining a professional designation accepted by the state.

[49]The five designations recognized as such are Certified Financial Planner®, Chartered Financial Consultant®, Personal Financial Specialist, Chartered Financial Analyst, and Chartered Investment Counselor.

As noted earlier, designations that imply expertise or special training in advising senior citizen or elderly investors have received particular attention from regulators. A joint report of SEC, FINRA, and NASAA described cases in which financial professionals targeted seniors by using senior-specific designations that implied that they had a particular expertise for senior investors, when in fact they did not; as noted earlier, NASAA and NAIC have developed a model rule to address the issue.[50] The report also noted these professionals targeted seniors through the use of so-called free-lunch seminars, where free meals are offered in exchange for attendance of a financial education seminar. However, the focus of the seminars was actually on the sale of products rather than the provision of financial advice.

Given the large number of designations financial planners may use, concerns exist that consumers may have difficulty distinguishing among them. To alleviate customer confusion, FINRA has developed a Web site for consumers that provides the required qualifications and other information about the designations used by securities professionals. The site lists more than 100 professional designations, 5 of which include the term "financial planner," and 24 of which contain comparable terms such as financial consultant or counselor.[51] The American College told us that it had identified 270 financial services designations. Officials from NASAA, NAIC, and a consumer advocacy organization told us that consumers might have difficulty distinguishing among the various designations. Officials from The American College told us that the number of designations itself was not necessarily a cause for concern, but rather consumers' broadly held misperception that all designations or credentials are equal.

To help address these concerns, FINRA plans to expand its Web site on professional designations to include several dozen additional designations related to insurance. However, FINRA officials noted that consumers' use of this tool has been limited. For example, in 2009, the site received only 55,765 visits. A recent national study of the financial capability of American adults sponsored by FINRA found that only 15 percent of adults

[50]*Protecting Senior Investors: Report of Examinations of Securities Firms Providing "Free Lunch" Sales Seminars* by the Office of Compliance Inspections and Examination, Securities and Exchange Commission; North American Securities Administrators Association; and the Financial Industry Regulatory Authority, September 2007.

[51]See http://apps.finra.org/DataDirectory/1/prodesignations.aspx.

who had used a financial professional in the last 5 years claimed to have checked the background, registration, or license of a financial professional.[52] In addition, SEC staff acknowledged that there have been concerns about confusing designations, and SEC's October 2010 changes to investment adviser disclosure requirements mandate that investment adviser representatives who list professional designations and certifications in their background information also provide the qualifications needed for these designations, so that the consumer can understand the value of the designation for the services being provided.

Section 917 of the Dodd-Frank Act includes a requirement that SEC conduct a study identifying the existing level of financial literacy among retail investors, including the most useful and understandable relevant information that they need to make informed financial decisions before engaging a financial intermediary. While the section does not specifically mention the issue of financial planners' titles and designations, the confusion we found to exist could potentially be addressed or mitigated if SEC incorporated this issue into its overall review of financial literacy among investors. SEC staff told us that at this time its review would not likely address this issue, although it would address such things as the need for conducting background checks on financial professionals. Financial markets function best when consumers have information sufficient to understand and assess financial service providers and products.[53] Including financial planners' use of titles and designations in SEC's financial literacy review could provide useful information on the implications of consumers' confusion on this issue.

Consumer Complaints and Enforcements Actions Appear to Be Relatively Limited, but Regulators Generally Do Not Track Data Specific to Financial Planners

Available data do not show a large number of consumer complaints and enforcement actions involving financial planners, but the exact extent to which financial planners may be a source of problems is unknown. We were able to find limited information on consumer complaints from various agencies. For example, representatives of FTC and the Better Business Bureau said that they had received relatively few complaints related to financial planners. FTC staff told us that a search in its Consumer Sentinel Network database for the phrase "financial planner"

[52]Applied Research & Consulting LLC, *Financial Capability in the United States: Initial Report of the Research Findings from the 2009 National Survey*, prepared for the FINRA Investor Education Foundation (New York: December 2009).

[53]GAO-09-216.

found 141 complaints in the 5-year period from 2005 through 2010 but that only a handful of these appeared to actually involve activity connected to the financial planning profession.[54] The staff added that additional searches on other titles possibly used by financial planners, such as financial consultant and personal financial adviser, did not yield significant additional complaints. In addition, a representative of the Better Business Bureau told us that it had received relatively few complaints related to financial planners, although the representative noted that additional complaints might exist in broader categories, such as "financial services."

Consumer complaint data may not be an accurate gauge of the extent of problems. Complaints may represent only a small portion of potential problems and complaints related to "financial planners" may not always be recorded as such. As we have previously reported, consumers also may not always know where they can report complaints.[55] At the same time, some complaints that are made may not always be valid.

SEC has limited information on the extent to which the activities of financial planners may be causing consumers harm. The agency does record and track whether federally and state-registered investment adviser firms provide financial planning services, but its data tracking systems for complaints, examination results, and enforcement actions are not programmed to readily determine and track whether the complaint, result, or action was specifically related to a financial planner or financial planning service. For example, SEC staff told us the number of complaints about financial planners would be undercounted in their data system that receives and tracks public inquiries, known as the Investor Response Information System, because this code would likely be used only if it could not be identified whether the person (or firm) was an investment adviser or broker-dealer. In addition, the data system that SEC uses to record examination results, known as the Super Tracking and Reporting System,

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[54]The Consumer Sentinel Network database is a secure online database of millions of consumer complaints available only to law enforcement. In addition to storing complaints received by FTC, the Consumer Sentinel Network also includes complaints filed with the Internet Crime Complaint Center, Better Business Bureaus, Canada's PhoneBusters, the U.S. Postal Inspection Service, the Identity Theft Assistance Center, and the National Fraud Information Center, among others.

[55]GAO, *Telecommunications: FCC Needs to Improve Oversight of Wireless Phone Service*, GAO-10-34 (Washington, D.C.: November 2009), p. 18.

does not allow the agency to identify and extract examination results specific to the financial planning services of investment advisers.

However, SEC staff told us that a review of its Investor Response Information System identified 51 complaints or inquiries that had been recorded using their code for issues related to “financial planners” between November 2009 and October 2010. SEC staff told us that the complaints most often involved allegations of unsuitable investments or fraud, such as misappropriation of funds.[56] A review of a separate SEC database called Tips, Complaints, and Referrals—an interim system that was implemented in March 2010—found 124 allegations of problems possibly related to financial planners from March 2010 to October 2010.[57]

SEC staff told us that they did not have comprehensive data on the extent of enforcement activities related to financial planners *per se*. In addition, NASAA said that states generally do not track enforcement data specific to financial planners. At our request, SEC and NASAA provided us with examples of enforcement actions related to individuals who held themselves out as financial planners. Using a keyword search, SEC identified 10 such formal enforcement actions between August 2009 and August 2010. According to SEC documents, these cases involved allegations of such activities as defrauding clients through marketing schemes, receiving kickbacks without making proper disclosures, and misappropriation of client funds. Although NASAA also did not have comprehensive data on enforcement activities involving financial planners, representatives provided us with examples of 36 actions brought by 30 states from 1986 to 2010. These cases involved allegations of such things as the sale of unsuitable products, fraudulent misrepresentation of qualifications, failure to register as an investment adviser, and misuse of client funds for personal expenses.

[56]Of these 51 complaints or inquiries, 29 involved allegations of fraud, 9 involved allegations of unsuitable investments, and the remaining 13 represented questions on a variety of topics.

[57]Of these 124 allegations, 13 were coded as “fraudulent or unregistered offer or sale of securities, including Ponzi schemes, high yield investment programs or other investment programs”; 12 as “manipulation of a security’s price or volume”; 6 as “theft or misappropriation of funds or securities”; 5 as “false or misleading statements about a company”; 3 as “problems with my brokerage or advisory account”; and 2 as “insider trading.” An additional 14 were coded as “other fraudulent conduct” and 69 were coded simply as “other.”

Because of limitations in how data are gathered and tracked, SEC and state securities regulators are not currently able to readily determine the extent to which financial planning services may be causing consumers harm. NASAA officials told us that, as with SEC, state securities regulators did not typically or routinely track potential problems specific to financial planners. SEC and NASAA representatives told us that they had been meeting periodically in recent months to prepare for the transition from federal to state oversight of certain additional investment adviser firms, as mandated under the Dodd-Frank Act, but they said that oversight of financial planners in particular had not been part of these discussions. SEC staff have noted that additional tracking could consume staff time and other resources. They also said that because there are no laws that directly require registration, recordkeeping, and other responsibilities of "financial planners" *per se*, tracking such findings relating to those entities would require expenditure of resources on something that SEC does not have direct responsibility to oversee. Yet as we have reported in the past, while we recognize the need to balance the cost of data collection efforts against the usefulness of the data, a regulatory system should have data sufficient to identify risks and problem areas and support decisionmaking.[58] Given the significant growth in the financial planning industry, ongoing concerns about potential conflicts of interest, and consumer confusion about standards of care, regulators may benefit from identifying ways to get better information on the extent of problems specifically involving financial planners and financial planning services.

[58]GAO, *Managing for Results, Using GPRA to Help Congressional Decisionmaking and Strengthen Oversight*, GAO/T-00-95 (Washington, D.C.: March 2000), p. 13. GAO, *Executive Guide, Effectively Implementing the Government Performance and Results Act*, GAO/GGD-96-118 (Washington, D.C.: June 1996), p. 27.

Some Changes in the Oversight of Financial Planners Could Be Beneficial, but Most Stakeholders Believe Substantial Overhaul Is Not Needed

Stakeholders Have Suggested a Variety of Approaches to the Regulation of Financial Planners

Over the past few years, a number of stakeholders—including consumer groups, FINRA, and trade associations representing financial planners, securities firms, and insurance firms—have proposed different approaches to the regulation of financial planners. Following are four of the most prominent approaches, each of which has both advantages and disadvantages.

Creation of a Board to Oversee Financial Planners

In 2009, the Financial Planning Coalition—comprised of the Certified Financial Planner Board of Standards, Financial Planning Association, and the National Association of Personal Financial Advisors—proposed that Congress establish a professional standards-setting oversight board for financial planners. According to the coalition, its proposed legislation would establish federal regulation of financial planners by allowing SEC to recognize a financial planner oversight board that would set professional standards for and oversee the activities of individual financial planners, although not financial planning firms. For example, the board would have the authority to establish baseline competency standards in the areas of education, examination, and continuing education, and would be required to establish ethical standards designed to prevent fraudulent and manipulative acts and practices. It would also have the authority to require registration or licensing of financial planners and to perform investigative and disciplinary actions. Under the proposal, states would retain antifraud authority over financial planners as well as full oversight for financial planners' investment advisory activity. However, states would not be allowed to impose additional licensing or registration requirements for financial planners or set separate standards of conduct. Supporters of a new oversight board have noted that its structure and governance would be analogous to the Public Company Accounting Oversight Board, a private nonprofit organization subject to SEC oversight that in turn oversees the audits of public companies that are subject to securities laws.

According to the Financial Planning Coalition, a potential advantage of this approach is that it would treat financial planning as a distinct profession and would regulate across the full spectrum of activities in which financial planners may engage, including activities related to investments, taxes, education, retirement planning, estate planning, insurance, and household budgeting. Proponents argue that a financial planning oversight board would also help ensure high standards and consistent regulation for all financial planners by establishing common standards for competency, professional practices, and ethics.

However, many securities regulators and financial services trade associations with whom we spoke said that they believe such a board would overlap with and in many ways duplicate existing state and federal regulations, which already cover virtually all of the products and services that a financial planner provides. Some added that the board would entail unnecessary additional financial costs and administrative burdens for the government and regulated entities. In addition, some opponents of this approach question whether "financial planning" should be thought of as a distinct profession that requires its own regulatory structure, noting that financial planning is not easily defined and can span multiple professions, including accounting, insurance, investment advice, and law. One consumer group also noted that the regulation of individuals and professions is typically a state rather than a federal responsibility. Finally, we note that the analogy to the Public Company Accounting Oversight Board may not be apt. That board was created in response to a crisis involving high-profile bankruptcies and investor losses caused in part by inadequacies among public accounting firms. In the case of financial planners, there is limited evidence of an analogous crisis or, as noted earlier, of severe harm to consumers.

Augmenting Oversight of Investment Advisers with an SRO

A number of proposals over the years have considered having FINRA or a newly created SRO supplement SEC oversight of investment advisers. These proposals date back to at least 1963, when an SEC study recommended that all registered investment advisers be required to be a member of an SRO.[59] In 1986, the National Association of Securities Dealers, a predecessor to FINRA, explored the feasibility of examining the investment advisory activities of members who were also registered as investment advisers. The House of Representatives passed a bill in 1993 that would have amended the Advisers Act to authorize the creation of an "inspection only" SRO for investment advisers, although the bill did not become law.[60] In 2003, SEC requested comments on whether one or more SROs should be established for investment advisers, citing, among other reasons, concerns that the agency's own resources were inadequate to address the growing numbers of advisers.[61] However, SEC did not take further action. Section 914 of the Dodd-Frank Act required SEC to issue a study in January 2011 on the extent to which one or more SROs for investment advisers would improve the frequency of examinations of investment advisers.[62]

According to FINRA, the primary advantage of augmenting investment adviser oversight with an SRO is that doing so would allow for more frequent examinations, given the limited resources of states and SEC. The Financial Services Institute, an advocacy organization for independent broker-dealers and financial advisers, has stated that an industry-funded SRO with the resources necessary to appropriately supervise and examine all investment advisers would close the gap that exists between the regulation of broker-dealers and investment advisers. FINRA said that it finds this gap troubling given the overlap between the two groups (approximately 88 percent of all registered advisory representatives are also broker-dealer representatives). FINRA adds that any SRO should operate subject to strong SEC oversight and that releasing SEC of some of its responsibilities for investment advisers would free up SEC resources for other regulatory activities.

[59]See Securities and Exchange Commission, News Digest Issue No. 63-4-3, 8 (1963), which describes SEC's report to Congress, regarding the adequacy of the rules of national securities exchanges and national securities associations, pursuant to Pub. L. No. 87-196, 75 Stat. 465 (1961), wherein SEC points out that the framework of industry self-regulation permitted many broker-dealer firms and registered investment advisers to remain outside of any official self-regulatory group. According to the SEC News Digest, the report suggested that membership in an SRO should be a prerequisite to registration with SEC as a broker-dealer or investment adviser.

[60]H.R. 578, 103rd Cong. (1993).

[61]Investment Advisers Act Release No. 2107, 68 Fed. Reg. 7038 (Feb. 11, 2003).

[62]SEC is required to report the results of its study within 180 days of enactment of the Dodd-Frank Act.

However, NASAA, some state securities regulators, and one academic with whom we spoke opposed adding an SRO component to the regulatory authority of investment advisers. NASAA said it believed that investment adviser regulation is a governmental function that should not be outsourced to a private, third-party organization that lacks the objectivity, independence, expertise, and experience of a government regulator. Further, NASAA said it is concerned with the lack of transparency associated with regulation by SROs because, unlike government regulators, they are not subject to open records laws through which the investing public can obtain information. Two public interest groups, including the Consumer Federation of America, have asserted that one SRO—FINRA—has an "industry mindset" that has not always put consumer protection at the forefront. In addition, the Investment Adviser Association and two other organizations we interviewed have noted that funding an SRO and complying with its rules can impose additional costs on a firm.[63]

Extending Coverage of the Fiduciary Standard

Proposals have been made to extend coverage of the fiduciary standard of care to all those who provide financial planning services. Some consumer groups and others have stated that a fiduciary standard should apply to anyone who provides personalized investment advice about securities to retail customers, including insurance agents who recommend securities. The Financial Planning Coalition has proposed that the fiduciary standard apply to all those who hold themselves out as financial planners. Proponents of extending the fiduciary standard of care, which also include consumer groups and NASAA, generally maintain that consumers should be able to expect that financial professionals they work with will act in their best interests. They say that a fiduciary standard is more protective of consumers' interests than a suitability standard, which requires only that a product be suitable for a consumer rather than in the consumer's best interest. In addition, the Financial Planning Coalition notes that extending a fiduciary standard would somewhat reduce consumer confusion about financial planners that are covered by the fiduciary standard in some capacities (such as providing investment advice) but not in others (such as selling a product).

However, some participants in the insurance and broker-dealer industries have argued that a fiduciary standard of care is vague and undefined. They say that replacing a suitability standard with a fiduciary standard could

[63]The Investment Adviser Association is a not-for-profit association that represents the interests of SEC-registered investment adviser firms.

actually weaken consumer protections since the suitability of a product is easier to define and enforce. Opponents also have argued that complying with a fiduciary standard would increase compliance costs that in turn would be passed along to consumers or otherwise lead to fewer consumer choices.

Clarifying Financial Planners' Credentials and Standards

The American College has proposed clarifying the credentials and standards of financial professionals, including financial planners. In particular, it has proposed creating a working group of existing academic and practice experts to establish voluntary credentialing standards for financial professionals. As noted previously, consumers may be unable to distinguish among the various financial planning designations that exist and may not understand the requirements that underpin them. Clarifying the credentials and standards of financial professionals could conceivably take the form of prohibiting the use of certain designations, as has been done for senior-specific designations in some states, or establishing minimum education, testing, or work experience requirements needed to obtain a designation. The American College has stated that greater oversight of such credentials and standards could provide a "seal of approval" that would generally raise the quality and competence of financial professionals, including financial planners, help consumers distinguish among the various credentials, and help screen out less qualified or reputable players.

However, the ultimate effectiveness of such an approach is not clear, since the extent to which consumers take designations into account when selecting or working with financial planners is unknown, as is the extent of the harm caused by misleading designations. In addition, implementation and ongoing monitoring of financial planners' credentials and standards could be challenging. Further, the issue of unclear designations has already been addressed to some extent—for example, as noted earlier, some states regulate the use of certain senior-specific designations and allow five professional designations to satisfy necessary competency requirements for prospective investment adviser representatives. State securities regulators also have the authority to pursue the misleading use of credentials through their existing antifraud authority.

Most Stakeholders Saw Little Need for an Additional Oversight Body Governing Financial Planners

In general, a majority of the regulatory agencies, consumer groups, academics, trade associations, and individual financial services companies with which we spoke did not favor substantial structural change in the regulation of financial planners. In particular, few supported an additional oversight body, which was generally seen as duplicative of existing regulation. Some stakeholders in the securities and insurance industries noted that given the dynamic financial regulatory environment under way as a result of the Dodd-Frank Act—such as creation of a new Bureau of Consumer Financial Protection—more time should pass before additional regulatory changes related to financial planning services were considered. Several industry associations also noted that opportunities existed for greater enforcement of existing law and regulation, as discussed earlier.

Conclusions

Existing statutes and regulations appear to cover the great majority of financial planning services, and individual financial planners nearly always fall under one or more regulatory regimes, depending on their activities. While no single law governs the broad array of activities in which financial planners may engage, given available information, it does not appear that an additional layer of regulation specific to financial planners is warranted at this time. At the same time, as we have previously reported, more robust enforcement of existing laws could strengthen oversight efforts. In addition, there are some actions that can be taken that may help address consumer protection issues associated with the oversight of financial planners.

First, as we have reported, financial markets function best when consumers understand how financial providers and products work and know how to choose among them. Yet consumers may be unclear about standards of care that apply to financial professionals, particularly when the same individual or firm offers multiple services that have differing standards of care. As such, consumers may not always know whether and when a financial planner is required to serve their best interest. While SEC is currently addressing the issue of whether the fiduciary standard of care should be extended to broker-dealers when they provide personalized investment advice about securities, the agency is not addressing whether this extension should also apply to insurance agents, who generally fall outside of SEC's jurisdiction. Sales practices involving some high-risk insurance products, such as annuities, have drawn attention from federal and state regulators. A review by NAIC of consumers' understanding of the standards of care with regard to the sale of insurance products could provide information on the extent of consumer confusion in the area and actions needed to address the issue.

Second, we have seen that financial planners can adopt a variety of titles and designations. The different designations can imply different types of qualifications, but consumers may not understand or distinguish among these designations, and thus may be unable to properly assess the qualifications and expertise of financial planners. SEC's recent changes in this area—requiring investment advisers to disclose additional information on professional designations and certifications they list—should prove beneficial. Another opportunity lies in SEC's mandated review of financial literacy among investors. Incorporating issues of consumer confusion about financial planners' titles and designations into that review could assist the agency in assessing whether any further changes are needed in disclosure requirements or other related areas.

Finally, SEC has limited information about the nature and extent of problems specifically related to financial planners because it does not track complaints, examination results, and enforcement activities associated with financial planners specifically, and distinct from investment advisers as a whole. However, a regulatory system should have data sufficient to identify risks and problem areas and support decisionmaking. SEC staff have noted that additional tracking could require additional resources, but other opportunities may also exist to gather additional information on financial planners. Because financial planning is a growing industry and has raised certain consumer protection issues, regulators could potentially benefit from better information on the extent of problems specifically involving financial planners and financial planning services.

Recommendations

We recommend that the National Association of Insurance Commissioners, in concert with state insurance regulators, take steps to assess consumers' understanding of the standards of care with regard to the sale of insurance products, such as annuities, and take actions as appropriate to address problems revealed in this assessment.

We also recommend that the Chairman of the Securities and Exchange Commission direct the Office of Investor Education and Advocacy, Office of Compliance Inspections and Examinations, Division of Enforcement, and other offices, as appropriate, to:

- Incorporate into SEC's ongoing review of financial literacy among investors an assessment of the extent to which investors understand the titles and designations used by financial planners and any implications a lack of understanding may have for consumers' investment decisions; and
- Collaborate with state securities regulators in identifying methods to better understand the extent of problems specifically involving financial planners and financial planning services, and take actions to address any problems that are identified.

Agency Comments

We provided a draft of this report for review and comment to FINRA, NAIC, NASAA, and SEC. These organizations provided technical comments, which we incorporated, as appropriate. In addition, NAIC provided a written response, which is reprinted in appendix II. NAIC said it generally agreed with the contents of the draft report and would give consideration to our recommendation regarding consumers' understanding of the standards of care with regard to the sale of insurance products.

NASAA also provided a written response, which is reprinted in appendix III. In its response, NASAA said it agreed that a specific layer of regulation for financial planners was unnecessary and provided additional information on some aspects of state oversight of investment advisers. NASAA also said that it welcomed the opportunity to continue to collaborate with SEC to identify methods to better understand and address problems specifically involving financial planners, as we recommended. In addition, NASAA expanded upon the reasons for its opposition to proposals that would augment oversight of investment advisers with an SRO.

We are sending copies of this report to interested congressional committees, the Chief Executive Officer of FINRA, Chief Executive Officer of NAIC, Executive Director of NASAA, and the Chairman of SEC. In addition, the report will be available at no charge on GAO's Web site at http://www.gao.gov.

If you or your staffs have any questions about this report, please contact me at (202) 512-8678 or cackleya@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs are on the last page of this report. GAO staff who made major contributions to this report are listed in appendix IV.

Alicia Puente Cackley

Alicia Puente Cackley
Director, Financial Markets
and Community Investment

List of Congressional Addressees

The Honorable Bob Corker
The Honorable Tim Johnson
The Honorable Herbert Kohl
The Honorable Richard C. Shelby
United States Senate

The Honorable Spencer Bachus
Chairman
The Honorable Barney Frank
Ranking Member
Committee on Financial Services
House of Representatives

Appendix I: Scope and Methodology

Our reporting objectives were to address (1) how financial planners are regulated and overseen at the federal and state levels, (2) what is known about the effectiveness of regulation of financial planners and what regulatory gaps or overlap may exist, and (3) alternative approaches for the regulation of financial planners and the advantages and disadvantages of these approaches.

For background information, we obtained estimates for 2000 and 2008, and projections for 2018, from the Bureau of Labor Statistics on the number of individuals who reported themselves as "personal financial advisers," a term that the agency said was interchangeable with "financial planner." The bureau derived these estimates from the Occupational Employment Statistics survey and the Current Population Survey.[1] According to the bureau, the Occupational Employment Statistics' estimates for financial planners have a relative standard error of 1.9 percent, and the median wage estimate for May 2009 has a relative standard error of 1.5 percent. Because the overall employment estimates used are developed from multiple surveys, it was not feasible for the bureau to provide the relative standard errors for these financial planner employment statistics. To estimate the number of households that used financial planners, we analyzed 2007 data from the Board of Governors of the Federal Reserve's Survey of Consumer Finances. This survey is conducted every three years to provide detailed information on the finances of U.S. households.[2] Because the survey is a probability sample based on random selections, the sample is only one of a large number of samples that might have been drawn. Since each sample could have provided different estimates, we express our confidence in the precision of our particular sample's results as a 95 percent confidence interval (e.g., plus or minus 2.5 percentage points). This is the interval that would contain the actual population value for 95 percent of the samples that could have been drawn. In this report, for this survey, all percentage

[1]As explained by the Bureau of Labor Statistics, the Occupational Employment Statistics program produces employment and wage estimates for over 800 occupations. These are estimates of the number of people employed in certain occupations, and estimates of the wages paid to them. Since self-employed persons are not included in the estimates, the bureau also considers information from the Current Population Survey, a monthly survey of households conducted by the Bureau of Census for the Bureau of Labor Statistics, to derive its occupation estimates.

[2]Additional information on the sample design and data collected by the Survey of Consumer Finances is available at http://www.federalreserve.gov/pubs/oss/oss2/about.html.

estimates have 95 percent confidence intervals that are within plus or minus 2.5 percentage points from the estimate itself.

To identify how financial planners are regulated and overseen at the federal and state levels, we identified and reviewed, on the federal level, federal laws, regulations, and guidance applicable to financial planners, the activities in which they engage, and their marketing materials, titles, and designations. We also reviewed relevant SEC interpretive releases, such as IA Rel. No. 1092, *Applicability of the Investment Advisers Act to Financial Planners, Pension Consultants, and Other Persons Who Provide Investment Advisory Services as a Component of Other Financial Services*. We also discussed the laws and regulations relevant to financial planners in meetings with staff of the Securities and Exchange Commission (SEC), Financial Industry Regulatory Authority (FINRA), Department of Labor, and Internal Revenue Service. We also interviewed two legal experts and reviewed a legal compendium on the regulation of financial planners. At the state level, we interviewed representatives from the North American Securities Administrators Association (NASAA) and the National Association of Insurance Commissioners (NAIC) and reviewed model regulations developed by these agencies. In addition, we selected five states—California, Illinois, North Carolina, Pennsylvania, and Texas—for a more detailed review. We chose these states because they had a large number of registered investment advisers and varying approaches to the regulation of financial planners, and represented geographic diversity. For each of these states, we reviewed selected laws and regulations related to financial planners, which included those related to senior-specific designations and insurance transactions, and we interviewed staff at each state's securities and insurance agencies.

To identify what is known about the effectiveness of the regulation of financial planners and what regulatory gaps or overlap may exist, we reviewed relevant federal and state laws, regulations and guidance. In addition, we spoke with representatives of the federal and state agencies cited above, as well as FINRA and organizations that represent or train financial planners, including the Financial Planning Coalition, The American College, and the CFA Institute; organizations that represent the financial services industry, including the Financial Services Institute, Financial Services Roundtable, Securities Industry and Financial Markets Association, Investment Advisers Association, American Society of Pension & Professional Actuaries, National Association of Insurance and Financial Advisors, American Council of Life Insurers, Association for Advanced Life Underwriting, American Institute of Certified Public Accountants, American Bankers Association; and organizations representing consumer interests, including the Consumer Federation of America and AARP. We also spoke with selected academic experts knowledgeable about these issues. In addition, we reviewed relevant studies and other documentary evidence, including a 2008 study of the RAND Corporation that was commissioned by SEC, “Investor and Industry Perspectives on Investment Advisers and Broker-Dealers”; “Results of Investor Focus Group Interviews About Proposed Brokerage Account Disclosures,” sponsored by SEC; results of the FPA Fiduciary Task Force, “Final Report on Financial Planner Standards of Conduct”; “U.S. Investors & The Fiduciary Standard: A National Opinion Survey,” sponsored by AARP, the Consumer Federation of America, the NASAA, the Investment Adviser Association, the Certified Financial Planner Board of Standards, the Financial Planning Association, and the National Association of Personal Financial Advisors; and the 2009 National Financial Capability Study, commissioned by FINRA. We determined that the reliability of these studies was sufficient for our purposes. In addition, we reviewed relevant information on the titles and designations used by financial planners, including FINRA’s Web site that provides the required qualifications and other information about the designations used by securities professionals.

We also obtained and reviewed available data on complaints and selected enforcement actions related to financial planners from the Federal Trade Commission, Better Business Bureau, and SEC. We collected from the Federal Trade Commission complaint data from its Consumer Sentinel Network database, using a keyword search of the term “financial planner” for complaints filed from 2005 to 2010. From the Better Business Bureau, we collected the number of complaints about the financial planning industry received in 2009. From SEC, we collected complaints from the agency’s Investor Response Information System that had been coded as relating to “financial planners” from November 2009 to October 2010. We also reviewed data from SEC’s Tips, Complaints, and Referrals database that resulted from a keyword search for the terms “financial planner,” “financial adviser,” “financial advisor,” “financial consultant,” and “financial counselor” from March 2010 to October 2010. In addition, at our request, SEC and NASAA provided us anecdotally with examples of enforcement actions related to individuals who held themselves out as financial planners. SEC identified 10 formal enforcement actions between August 2009 and August 2010 and NASAA provided us selected examples of state enforcement actions involving financial planners from 1986 to 2010 from 30 states. We gathered information on SEC- and state-registered investment advisers from SEC’s Investment Adviser Registration Database. FINRA did not provide us with data on complaints, examination results, or enforcement actions specific to financial planners; FINRA officials told us they do not track these data specific to financial planners.

To identify alternative approaches for the regulation of financial planners and their advantages and disadvantages, we conducted a search for legislative and regulatory proposals related to financial planners, which have been made by Members of Congress, consumer groups, and representatives of the financial planning, securities, and insurance industries. We identified and reviewed position papers, studies, public comment letters, congressional testimonies, and other documentary sources that address the advantages and disadvantages of these approaches. In addition, we solicited views on these approaches from representatives of the wide range of organizations listed above, including organizations that represent financial planners, financial services companies, and consumers, as well as state and federal government agencies and associations and selected academic experts.

We conducted this performance audit from June 2010 through January 2011 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix II: Comments from the National Association of Insurance Commissioners

NAIC
National Association of Insurance Commissioners
& The Center for Insurance Policy and Research

January 10, 2011

Alicia Puente Cackley
Director, Financial Markets and Community Investment
United States Government Accountability Office
441 G Street NW
Washington, D.C. 20548

Dear Ms. Cackley:

Thank you for the opportunity to review the Government Accountability Office's draft report, "Consumer Finance: Regulatory Coverage Generally Exists for Financial Planners, but Consumer Protection Issues Remain" (GAO-11-235). The NAIC appreciates the important role the GAO plays in maintaining consumer protections and ensuring appropriate implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (P.L. 111-203). Consumer protection is at the heart of the NAIC's and state insurance regulators' activities involving regulating markets, ensuring company solvency and protecting the public interest.

We generally agree with the contents of this draft report and we do not have any substantive comments to submit at this time. Furthermore, our association will give further consideration to the recommendation of your office regarding an assessment of consumers' understanding of standards of care with regard to insurance products. Under the leadership of our current president, Susan E. Voss, Commissioner of Insurance for the State of Iowa, state insurance regulators will include this matter as a topic for discussion during our 2011 deliberations.

Thank you again for this opportunity. If you are in need of further information, please be in touch with Eric Nordman, Director of Regulatory Services, at (816) 783-8005, or Ethan Sonnichsen, Director of Government Relations, at (202) 471-3990.

Sincerely,

Andrew J. Beal
Chief Operating Officer and
Chief Legal Officer

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Appendix III: Comments from the North American Securities Administrators Association

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NASAA

January 6, 2011

Ms. Alicia Puente Cackley
Director
Financial Markets and Community Investment
Government Accountability Office
441 G Street, NW
Washington, DC 20548

Dear Ms. Cackley:

Thank you for the opportunity to comment on the Government Accountability Office (GAO) draft report entitled *Consumer Finance: Regulatory Coverage Generally Exists for Financial Planners, but Consumer Protection Issues Remain* (GAO-11-235) ("report"). We also appreciate the opportunity to respond to inquiries from GAO staff and to provide information needed for the completion of this report. The report covers important matters to investors and regulators, and we commend the GAO staff for its thoroughness in preparing this report.

NASAA concurs with the report that a specific layer of regulation for financial planners is unnecessary. NASAA offers the following comments in order to convey our position on several issues discussed in the report and to provide additional information on state regulation of investment advisers and financial planners.

Augmenting Oversight of Investment Advisers with an SRO

As noted in the report, regulation of financial planners is primarily covered under state and federal laws governing investment advisers. State securities regulators and the Securities and Exchange Commission ("SEC") share responsibility for regulating investment advisers based primarily on the assets an investment adviser has under management. Since 1996, investment advisers with $30 million or less in assets under management have been regulated by the states, while those with assets under management in excess of $30 million have been regulated by the SEC. However, the Dodd-Frank Wall Street Reform and Consumer Protection Act increased this regulatory dividing line to $100 million. As a result, we estimate that approximately 4,000 investment advisers will switch from SEC to state registration, leaving the SEC to focus on the larger more systemically significant advisers.

Ms. Alicia Puente Cackley
January 6, 2011
Page 2 of 4

Regulation of investment advisers is a topic of considerable debate, and the report covers various proposals on how the oversight of financial planners and investment advisers should be handled. One of the proposals discussed in the report is the formation of a self-regulatory organization ("SRO") for investment advisers. The report considers potential advantages and disadvantages of this approach, and NASAA believes there are significant concerns with this concept beyond those noted in the report that must be considered.

NASAA's position is that investment adviser regulation is a governmental function that should not be outsourced to a private, third-party organization that does not have expertise or experience with investment adviser regulation. One can readily conclude that the designation of an SRO for the oversight of investment advisers, with its attendant direct and indirect costs, its opaque structure and attendant lack of accountability and transparency, would outweigh any perceived benefits to the investing public.

The chief concerns the states have with the designation of an SRO for the oversight of investment advisers are the collaboration, transparency, accountability, and conflict issues that have always been inherent to the SRO model. While industry SROs had historically worked as a partner with the SEC and the states (creating what was referred to as the "three-legged stool" of regulation), this model recently changed based on an over-broad construction of the "government actor doctrine." It has been our experience that, to avoid a classification as a "government actor", the relevant SRO has restricted the release of information to the government and has affirmatively taken the position that it is prohibited from active collaboration with governmental regulators, including the governmental entity responsible for its oversight. As such, previous synergies with the SRO have been lost, and it has become increasingly difficult for the governmental regulators to meaningfully control oversight or investigations over registrants subject to the current SRO model.

Collaboration issues aside, the regulatory work performed by SROs lacks transparency. Although SROs have been performing governmental functions for decades, they are not subject to similar Freedom Of Information Act (FOIA) and public records requirements as are the SEC and state securities regulators. Even where there is public disclosure by SROs regarding members, as in the case of BrokerCheck, the SRO has placed limitations and filters on regulatory records that far exceed FOIA provisions. The end result is that vital information is withheld from the investing public. Without greater transparency, investors cannot obtain the information they need to make informed decisions.

Finally, the current SRO model raises accountability and conflict concerns. Even where there is an independent Board of Directors, SROs remain organizations built on the premise of self-rule and are, as a matter of first principle, accountable to their members rather than the investing public. Ultimately, no matter how many safeguards are instituted, an SRO has substantial conflicts of interest that governmental regulators do not. This is particularly true in situations where industry and investor interests conflict, as in the case of mandatory pre-dispute arbitration clauses and the disclosure or expungement of historical settlements, judgments, and investor claims. Ultimately, SROs simply cannot match the accountability of government

Ms. Alicia Puente Cackley
January 6, 2011
Page 3 of 4

regulators, nor the proximity and familiarity of state regulators, in particular, when considering investor protection and regulatory thoroughness.

State Regulation of Investment Advisers and Investment Adviser Representatives

The report discusses both state and SEC regulation of investment advisers, including the registration forms required by the SEC and the disclosure of that information to investors. We believe it is important to note that these forms, the ADV Parts 1 and 2, are also required by the state securities regulators.

In addition to these forms, state-registered advisers are also required to submit additional forms and supplemental information such as client contracts or financial statements. State regulators also require investment advisers to complete additional disclosure questions. Specifically, in Part 2 of the ADV, commonly referred to as the firm brochure, an investment adviser registering with a state securities regulator must disclose additional information about outside business activities, certain fee arrangements, and arbitration claims against the adviser or a management person. The information contained in these registration forms is available to the investing public from the adviser, state securities regulators, or online at www.adviserinfo.sec.gov. As explained in the report, most states register investment adviser representatives and important information about the backgrounds of these individuals is also available on the same website.

Conclusions and Recommendations

The report's conclusions include a reference to the lack of complaint information available to state and federal regulators. While states track complaint and enforcement information on investment advisers as noted in the report, that information generally does not distinguish between complaints or enforcement actions lodged against an investment adviser versus a financial planner. NASAA understands the GAO's concern with potential complaints against financial planners given the increase of individuals and firms providing financial planning services. NASAA is taking steps to gauge whether there are in fact significant numbers of complaints against investment adviser firms providing financial planning services and, if so, how better to track this information and address potential problems.

Finally, the report includes a recommendation that the SEC "collaborate with state securities regulators in identifying methods to better understand the extent of problems specifically involving financial planners and financial planning services, and take actions to address any problems that are identified." Over the years, NASAA has worked closely with the SEC on matters specific to the regulation of investment advisers, including revisions to registration forms, the development of the electronic system for registration used by investment advisers, and the upcoming implementation of the increased assets under management threshold. NASAA welcomes the opportunity to continue to work with the SEC and to address potential issues involving financial planners as recommended in the report.

Ms. Alicia Puente Cackley
January 6, 2011
Page 4 of 4

Thank you again for the opportunity to review and comment on the draft report. We look forward to working with the GAO on future studies.

Sincerely,

David Massey,
NASAA President and
North Carolina Deputy Securities Administrator

Appendix IV: GAO Contact and Staff Acknowledgments

GAO Contact

Alicia Puente Cackley (202) 512-8678 or cackleya@gao.gov

Staff Acknowledgments

In addition to the contact named above, Jason Bromberg (Assistant Director), Sonja J. Bensen, Jessica Bull, Emily Chalmers, Patrick Dynes, Ronald Ito, Sarah Kaczmarek, Marc Molino, Linda Rego, and Andrew Stavisky made key contributions to this report.

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