

Executive Summary

Regulation of Financial Planners

April 2002

The following is an executive summary of an extensive report on the financial planning profession that examines current regulation of financial planners, regulatory trends affecting the profession, past reform efforts, and possible options for future regulation. To review the full Report in .pdf format, please [click here](#).

I. Introduction

The financial planning profession is in a curious regulatory posture. While the financial services industry is one of the most heavily regulated sectors in the United States, the financial planning profession itself lacks a stand-alone regulatory scheme. The importance of financial planning is reviewed, as well as the challenges facing financial planners, based on the premise that it is indeed an established profession in its own right.

II. Financial Planning in the Financial Services Industry

What is financial planning? Although there is no universally accepted definition, the six steps of the financial planning process, as defined by two of the organizations involved in financial planning, are examined, as well as how regulators and others view the process and planners. The question of whether there is a need for regulation, based on criticism of the profession in the 1980s, is reviewed.

III. Current Regulation of Financial Planning

- A. **Overview.** Although federal and state governments do not regulate financial planners as a professional group, their activities and conduct are intensively regulated in their capacity as investment advisers, insurance agents, stock brokers, accountants, and attorneys. This section reviews the substantive regulation of planners in each of these functional areas of oversight of financial planning.
- B. **Federal Regulation.** The primary federal statute regulating financial planners is the Investment Advisers Act of 1940. The key components of the Advisers Act, including the definition and exclusions for an adviser, registration requirements, anti-fraud provisions, their explicit fiduciary duty to clients, and other requirements, are carefully examined. It is difficult to "escape" the definition of investment adviser for anyone offering comprehensive financial planning, unless they meet the exclusion by working for banks, offering certain fee-based advisory programs as stock brokers, or on an incidental basis as accountants or attorneys. A significant number of planners are also licensed to sell securities, and thus are subject to oversight by the National Association of Securities Dealers.
- C. **State Regulation.** Many financial planners are regulated solely on the state level by state securities or insurance departments, frequently both, and sometimes indirectly by the Securities and Exchange Commission (SEC) if affiliated with a federally registered investment adviser. Since many financial planners come from the accounting and legal professions, and still practice in these areas as well as in financial planning, these other regulatory frameworks are briefly examined.
- D. **Private Regulation.** The motivation for individuals to be certified by private sector organizations is reviewed, as well as the long-term market dilemma for financial planners whose advisory services are reduced in value if consumers are unable to distinguish between "high quality" and "low quality" advisers. Certifying organizations and the steps they have taken within the private sector to define the competency and ethical standards for financial planners are examined. In addition, financial planners may be "regulated" through private litigation. The

causes for litigation, including breach of contract, fiduciary duty, and negligence, are discussed.

IV. **Regulatory Trends in the Financial Services Industry**

A variety of trends affecting financial planners are examined, including the recent repeal of Depression-era laws that prohibited cross-ownership of banks, securities firms, and insurance companies. These large conglomerates increasingly compete with financial planners by offering the same services traditionally offered by financial planners. Utilization of retention letters by financial planners describing the scope of services is reviewed, as is the controversial proposed exclusion from the Advisers Act for broker-dealers. Current enforcement efforts by the SEC are also examined.

V. **Possible Reform of Financial Planner Regulation**

- A. **Past Reform Efforts.** A surprising number of attempts have been made to change the regulatory scheme for investment advisers and financial planners over the past quarter-century. This section briefly discusses efforts by the SEC to set competency standards for investment advisers in 1976 and a statutory right of action by consumers. Increasing numbers of planners registering with the SEC in the 1980s led to corresponding pressures on agency resources, leading to a number of proposals for self-regulatory organizations (SROs). The International Association for Financial Planning was one of the first to suggest an SRO for financial planners in the mid-1980s, and the SEC and Congress also attempted to establish SROs for advisers and planners a few years later. A 1992 effort to establish a combined financial planner/adviser SRO in Colorado, and a draft federal proposal from 1995 that was actively discussed by various planner organizations but never pursued with Congress, are also briefly examined.
- B. **Canadian Reform.** A unique regulatory proposal to comprehensively define and regulate financial planning in most Canadian provinces is reviewed.
- C. **Options for Future Regulation of Financial Planners.** Although major regulatory reform usually happens during crises, the Report examines possible options for regulating financial planners in the future, as well as the challenges of developing a regulatory framework for a multidisciplinary profession already heavily regulated. Preliminary considerations include how to define financial planning, and factors to consider such as an overinclusive or underinclusive definition that accurately captures "real" financial planners or those purporting to be planners. Whether financial planning is now an established profession - and whether it even matters in contemplating future regulation -- is also discussed.

This section suggests six alternatives that financial planners may want to consider in future regulation, including advantages and disadvantages of each:

1. status quo;
2. consumer protection litigation model;
3. stricter qualifications for investment adviser representatives;
4. professional licensing on state level;
5. interstate compact; and
6. federal SRO.

Finally, this section briefly explores the challenges of regulating the intangible characteristics of professionalism, and concludes that current functional regulation falls short of the institutional competence needed to regulate ethical behavior and the comprehensive financial planning process. Instead, regulators continue to focus largely on detecting fraud in the financial services industry.

VI. **Conclusion**

Significant changes in the market have led to an increasing demand for objective and competent financial planning advice. However, the tremendous growth in the number of individuals offering such services has made it even more difficult to regulate an emerging financial planning profession.

A number of critical questions need to be addressed. Should financial planning be viewed as a separate profession? Is there a need for change? Should the principal goal be to change existing anti-fraud regulations, or should there be more of a focus on regulating professionalism? And what would be the appropriate regulatory body in charge of creating and enforcing professional regulations, as well as an oversight body to review its operation? Whether such changes happen, generally accepted standards for financial planning are nonetheless needed to clearly define and provide for fair and efficient regulation of the financial planning profession.