



CERTIFIED FINANCIAL PLANNER BOARD OF STANDARDS, INC.

August 26, 2011

Ms. Elizabeth M. Murphy  
Secretary  
Securities and Exchange Commission  
100 F Street NE  
Washington, DC 20549-1090

**Re: File Number S7-23-11, Broker-Dealer Reports**

Dear Ms. Murphy:

Certified Financial Planner Board of Standards, Inc. (CFP Board)<sup>1</sup> appreciates the opportunity to comment on the proposal by the Securities and Exchange Commission (the Commission) to amend Exchange Act Rule 17a-5.<sup>2</sup> The Broker-Dealer Reports Proposal is a welcome effort to close regulatory gaps demonstrated by the Bernard Madoff Ponzi scheme scandal. It follows the Commission's adoption of amendments to the Investment Adviser Custody Rule, Rule 206(4)-2, and the Investment Adviser Recordkeeping Rule, Rule 204-2, which were adopted for the same fraud-prevention reasons.<sup>3</sup> CFP Board strongly supported adoption of the Investment Adviser Custody Rule amendments.<sup>4</sup> However, we recognize that the Investment Adviser Custody Rule as amended would not have prevented Madoff's Ponzi scheme because his firm was registered solely as a broker-dealer for decades. We believe the Broker-Dealer Reports Proposal is a much-needed companion rule to the Investment Adviser Custody Rule that will close this regulatory gap and enhance the Commission's ability to oversee the custody activities of broker-dealers. For these reasons and the reasons below, we support adoption of this proposal.

Significant factors permitted the Madoff Ponzi scheme to continue for as long as it did. First, Madoff's independent accounting firm apparently did not conduct meaningful audits of the firm, including audits of the assets Madoff claimed to be managing. Second, no securities regulator ever verified the existence of the assets that Madoff claimed to be managing. If any independent party, either an auditor or a regulator, had reviewed the existence and value of the assets Madoff claimed to be managing, then in all likelihood the Ponzi scheme would have been discovered and halted.

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<sup>1</sup> CFP Board is a 501(c)(3) non-profit organization that acts in the public interest by fostering professional standards in personal financial planning through setting and enforcing education, examination, experience, and ethics standards for financial planner professionals who hold the CFP® certification. CFP Board's mission is to benefit the public by granting the CFP® certification and upholding it as the recognized standard of excellence for personal financial planning. We currently oversee more than 63,000 CFP® professionals who agree to comply with our competency and ethics standards and subject themselves to the disciplinary oversight of CFP Board.

<sup>2</sup> Broker-Dealer Reports, Exchange Act Release No. 64,676 (June 15, 2011), 76 Fed. Reg. 37,572 (June 27, 2011) (to be codified at 17 C.F.R. pts. 240, 249).

<sup>3</sup> See Custody of Funds or Securities of Clients of Investment Advisers, Investment Advisers Act Rel. No. 2968 (Dec. 30, 2009), 75 Fed. Reg. 1456 (Jan. 11, 2010).

<sup>4</sup> See Letter of Kevin R. Keller, Chief Executive Officer, Certified Financial Planner Board of Standards, Inc., to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission (July 28, 2009), available at <http://www.sec.gov/comments/s7-09-09/s70909-759.pdf>.

Thousands of subsequent investors could have avoided hundreds of millions of dollars in additional losses.

The Broker-Dealer Reports Proposal is designed to address these regulatory gaps. The proposed amendments would require carrying broker-dealers to file reports regarding their compliance with the Financial Responsibility Rules.<sup>5</sup> The amendments would require broker-dealers that either clear transactions or carry customer accounts to allow the Commission and self-regulatory organizations (SROs), such as FINRA, to review the work-papers of the broker-dealers' independent public accountants and discuss the findings with the accountants. The amendments also would require broker-dealers to prepare and file a new Form Custody.

Audit Reports and Auditing Standards: The proposed rule would require carrying broker-dealers to file with the Commission a report asserting compliance with the Financial Responsibility Rules (the Compliance Report) and a report of their independent public accountant (the Examination Report) regarding the assertions in the Compliance Report.<sup>6</sup> They would allow the Public Company Accounting Oversight Board (PCAOB) to implement oversight of independent public accountants of broker-dealers as required by Section 982 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act), and establish standards for review of broker-dealers that are dually registered as, or affiliated with, investment advisers. When Congress created the PCAOB as part of the Sarbanes-Oxley Act, it created a rigorous oversight authority for accounting firms that conduct audits of public companies. However, the PCAOB lacked jurisdiction over accounting firms that audited broker-dealers and investment advisers that were not affiliates of public companies, and the Commission arguably lacked the ability to require broker-dealers and investment advisers to use PCAOB-member accounting firms. Section 982 of the Dodd-Frank Act closed this inadvertent regulatory gap.

Under the proposed rule, a PCAOB-registered accounting firm would be required to audit every broker-dealer's financial statement and net capital calculations. For firms that custody customer funds or securities, the accounting firm would also audit the broker-dealer's customer reserve calculation as well its accounting system, internal accounting controls, and policies and procedures for complying with the Financial Responsibility Rules.<sup>7</sup> For these issues, under the current rules the accounting firm only prepares a study. Under the proposed rule, these issues would be part of the audit on which the accounting firm must issue an opinion—a higher standard and one that provides greater assurance. Requiring that the financial statements of every broker-dealer be audited by a PCAOB-member accounting firm will go a long way to preventing the recurrence of schemes such as Madoff's at registered broker-dealers. These are exactly the steps necessary to provide investors with confidence that their assets are safe.

The Proposal provides that, in the case of firms dually registered as broker-dealers and investment

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<sup>5</sup> Rule 15c3-1, Rule 15c3-3, Rule 17a-13, and the Account Statement Rules.

<sup>6</sup> Broker-dealers that do not carry customer securities would be required to file a report asserting their exemption from the requirements of Rule 15c3-3 (the Exemption Report) and a report of their independent public accountant regarding the assertions in the Exemption Report.

<sup>7</sup> The accounting firm's audit also would be required to address certain other issues, such as collection of SIPC assessments and, for firms that use a model-based approach to calculating net capital, the internal risk management system established in connection with this calculation.

advisers, or for broker-dealers with affiliated investment advisers, the audit required of the broker-dealer will satisfy the firm's responsibilities under the Investment Adviser Custody Rule. We believe this is a critical point. The Broker-Dealer Reports Proposal presents this as a matter of avoiding duplication, but we believe it is more. A major factor that allowed the Madoff scheme to continue after registration of the firm with the Commission as an investment adviser was the fact that, on some occasions, securities regulators looked at the brokerage operations of Madoff in isolation from the investment advisory operations.

We believe it is critically important that there be a single audit of the custody function at both the broker-dealer and investment adviser operations of any dually registered entity (or of affiliated broker-dealers and investment advisers), and that this audit use a single, consistent standard for evaluating custody at both the broker-dealer and investment adviser operations. We believe this will limit the possibility of issues falling between the cracks because of different broker-dealer and investment adviser custody standards. CFP Board, as part of the Financial Planning Coalition, has been a vocal advocate of a strong and uniform fiduciary standard of care for both broker-dealers and investment advisers.<sup>8</sup> A single, uniform custody standard for both broker-dealer and investment adviser operations of dually registered firms (and affiliated broker-dealers and investment advisers) will best support equal protection of both broker-dealer and investment adviser clients, and prevent issues from being missed because no one was required to look at the "big picture."

Access to Audit Documentation Amendments: The proposed rule would require the independent accountants who prepare broker-dealer audits to make themselves and their work papers available both to the Commission and any SRO responsible for examining that broker-dealer.<sup>9</sup> While we do not have comments on the precise details of the relationship between the securities regulators and the accounting firms, we believe it is reasonable for the securities regulators to be able to validate any concerns promptly with a broker-dealer's independent accounting firm.

Form Custody Amendments: Finally, the proposed rule would require broker-dealers to file a quarterly Form Custody with the Commission describing their custody arrangements. Form Custody would be supported by a Compliance Report that the broker-dealer would file with its financial statements attesting that it was in compliance with and did not have any material weaknesses in internal controls relating to the Financial Responsibility Rules in the previous year. The Broker-Dealer Reports Proposal explains that the intent of these requirements is to allow the Commission and the SROs to identify potential "red flags" concerning custody that may warrant further investigation. For example, if a broker-dealer claimed to have custody of a particular type of security at a particular clearing broker-dealer, a custody bank, or a clearing utility (such as The Depository Trust & Clearing Corporation), but that other entity had no record of such a relationship, that discrepancy would allow the securities regulators to investigate quickly.<sup>10</sup> While we do not expect that future Bernie Madoffs

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<sup>8</sup> See Letter from Kevin R. Keller, CEO, Certified Financial Planner Board of Standards, et al., to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission (Aug. 30, 2010), available at <http://www.sec.gov/comments/4-606/4606-2593.pdf>.

<sup>9</sup> Pursuant to Exchange Act Section 15(b)(8), other than a small number of proprietary broker-dealers and exchange specialists, all broker-dealers are required to be a member of FINRA, which is the designated examining authority responsible for inspecting its member firms.

<sup>10</sup> We do not express an opinion whether the particular questions on the proposed Form Custody are all necessary or appropriate. However, we suggest that rather than seeking general information about types of entities at which a broker-

will self-report their Ponzi schemes on Form Custody or in the Compliance Report, we do believe Form Custody and the Compliance Report will serve as a useful adjunct to the provisions in the Broker-Dealer Reports Proposal relating to improved audits and better access to information for securities regulators.

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CFP Board appreciates the opportunity to comment on the Commission's proposed amendments to Exchange Act Rule 17a-5 relating to broker-dealer custody and audits. If you should have any questions regarding this comment letter, CFP Board, the financial planners it certifies, or the CFP® marks, please contact Marilyn Mohrman-Gillis, Managing Director, Public Policy and Communications, at (202) 379-2235, or visit CFP Board's Web site at [www.CFP.net](http://www.CFP.net).

Sincerely,

A handwritten signature in black ink that reads "Kevin R. Keller". The signature is written in a cursive style with a large initial "K".

Kevin R. Keller, CAE  
Chief Executive Officer

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dealer custodies securities (see Proposed Form Custody Item 3), it would be more helpful to require the broker-dealer to disclose the specific entities at which it custodies securities. As discussed in the text, such a disclosure would allow the securities regulators to note potential discrepancies raised by the disclosures more easily, as well as changes in custody relationships that may warrant further investigation.