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ARTICLES

ESCAPING ENTITY-CENTRISM IN FINANCIAL SERVICES REGULATION

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In the ongoing discussions about financial services regulation, one critically important topic has not been recognized, let alone addressed. That topic is what this Article calls the "entity-centrism" of financial services regulation. Laws and rules are entity-centric when they assume that a financial services firm is a stand-alone entity, operating separately from and independently of any other entity. They are entity-centric, therefore, when the specific requirements and obligations they comprise are addressed only to an abstract and solitary "firm," with little or no contemplation of affiliates, parent companies, subsidiaries, or multi-entity enterprises. Regulatory entity-centrism is not an isolated phenomenon, as it permeates the laws and rules governing many facets of a firm's operations. Moreover, it can be discerned in laws and rules covering many types of financial services activities. In other words, entity-centrism in financial services regulation is pervasive. It is also deeply problematic.

This Article calls attention to entity-centrism as manifested in financial services regulation, shows why entity-centrism counters regulatory objectives, and assesses possible explanations for the phenomenon. It does so primarily by evaluating two recent regulatory failures that reveal how entity-focused laws and rules privilege entity boundaries over the various ways in which multiple entities (or entities and individuals) work together as a common enterprise. Accordingly, the Article contends that financial services regulation should look past entity boundaries and that lawmakers and regulators should think more broadly, critically,

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and creatively to address the persistent and significant regulatory difficulties that entity-centrism has spawned.

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INTRODUCTION

Financial services regulation is complex. Among other difficulties, lawmakers and regulators do not always understand *what*, exactly, has to be regulated—what market failure or inefficiency, in other words, gave rise to the need for regulation. The complicated financial products that fueled, if not precipitated, the 2008 financial crisis are poster children for this point.[1] In addition, regardless of whether the "what" is understood adequately, the "how" often presents intractable difficulties, for it

1. See, e.g., Permanent Subcomm. on Investigations, U.S. Senate Comm. on Homeland Sec. & Governmental Affairs, Wall Street and the Financial Crisis: Anatomy of a Financial Collapse 1 (2011), available at http://www.hsgac.senate.gov/download/report-psi-staff-report-wall-street-and-the-financial-crisis-anatomy-of-a-financial-collapse (on file with the *Columbia Law Review*) (noting financial crisis was "result of high risk, complex financial products; undisclosed conflicts of interest; and the failure of regulators, the credit rating agencies, and the market itself to rein in the excesses of Wall Street").

requires achieving a careful balance: How might regulations address the problems discerned without unduly raising the costs borne by market participants and stifling productive market activities? Too much or too little regulation, or the wrong kind, can produce disastrous results.[2] Enforcement, lastly, presents its own challenges, limited, as it necessarily is, by regulators' resources and investigative skills and focus, not to mention an often too-close relationship with those subject to regulation, as the term "revolving door" aptly connotes.[3]

In the ongoing discussions about regulation and its proper goals, implementation, and enforcement—encompassing considerations of how best to protect clients and customers and the circumstances under which markets function most effectively—one critically important topic has not been recognized, let alone addressed. That topic is what this Article calls the "entity-centrism" of financial services regulation—regulation of providers of financial services, such as broker-dealers,[4] investment

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2. See Cass R. Sunstein, Paradoxes of the Regulatory State, 57 U. Chi. L. Rev. 407, 411 (1990) ("Sometimes [regulation] has imposed enormously high costs for speculative benefits; sometimes it has accomplished little or nothing; and sometimes it has aggravated the very problem it was designed to solve.").

3. See, e.g., John C. Coffee, Jr., The Political Economy of Dodd-Frank: Why Financial Reform Tends to Be Frustrated and Systemic Risk Perpetuated, 97 Cornell L. Rev. 1019, 1043 (2012) (noting SEC staff members, hoping to obtain jobs on Wall Street or with private law firms upon leaving SEC, may "not want to confront the private bar's elite law firms"); David S. Hilzenrath, SEC Staff's "Revolving Door" Prompts Concerns About Agency's Independence, Wash. Post (May 13, 2011), http://articles.washingtonpost.com/2011-05-13/business/35232119_1_sec-employees-sec-inspector-sec-enforcement-actions (on file with the *Columbia Law Review*) (noting, according to study by Project on Government Oversight, "[o]ver the past five years, 219 former SEC employees filed disclosures with the SEC saying that they planned to represent clients or employers in dealings with the agency"); Eric Lichtblau, Lawmakers Regulate Banks, Then Flock to Them, N.Y. Times (Apr. 13, 2010), http://www.nytimes.com/2010/04/14/business/14lobby.html?_r=0 (on file with the *Columbia Law Review*) (citing finding that in 2009, "at least 70 former members of Congress were lobbying for Wall Street and the financial services sector").

4. A broker-dealer is a natural person or entity that is engaged in the business of buying and selling securities either on behalf of the person's customers (a broker) or for the person's own account (a dealer) and is subject to regulation as such under the Securities Exchange Act of 1934 ("Exchange Act"). See 15 U.S.C. § 78c(a)(4)(A) (2012) (defining "broker"); id. § 78c(a)(5)(A) (defining "dealer"); id. § 78i(j) (prohibiting broker's or dealer's use of mails or other instrumentalities of interstate commerce "to effect any transactions in, or to induce or attempt to induce the purchase or sale of, any" security unless broker or dealer is registered with SEC as "broker-dealer" under Exchange Act). Put another way, a broker acts as an agent for its customer and, for each transaction effected, generally receives a commission as compensation. See Anita K. Krug, The Modern Corporation Magnified: Managerial Accountability in Financial-Services Holding Companies, 36 Seattle U. L. Rev. 821, 833 (2013) (describing role of brokers in securities transactions). By contrast, a dealer buys and sells securities to customers or others, acting as a principal in the transaction (and, therefore, bearing the risk associated with the securities in which it transacts), and is compensated through an extra amount added to the prices of securities sold and paying a discounted price for securities bought. See id. (describing role of dealers in securities transactions).

advisers, and mutual funds.[5] Laws and rules are entity-centric when they assume that financial services firms are stand-alone entities, operating separately from, and independently of, any other entity. They are entity-centric, therefore, when the specific requirements and obligations they comprise are addressed only to an abstract and solitary unit of business association, otherwise known as an entity—a single corporation, limited liability company (LLC), limited partnership, or business trust, for example—with no contemplation of affiliates, parent companies, subsidiaries, or multi-entity enterprises.

In many respects, law is built around the entity. It is not difficult either to appreciate why that is or to conclude that it makes sense. After all, a substantial portion of the laws and rules that exist today, and doubtless an even larger portion of those to be created in the future, relate to matters of economics, markets, and productivity. As a result, these laws and rules concern themselves with such things as incentives, agency costs, and externalities.[6] The primary actors in the marketplace are, of course, entities—corporations largely, but also limited liability companies, business trusts, and limited partnerships, to name a few. Entities merge with other entities. Entities may go bankrupt. Entities invest in other entities. Entities create and sell goods, or provide services, to their customers. If the entity is the marketplace actor, then, logically, the entity should be the regulatory subject.

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5. This Article does not address financial services functions that fall within the ambit of banking regulation and, therefore, does not address the Bank Holding Company Act of 1956, Pub. L. No. 84-511, 70 Stat. 133 (codified as amended at 12 U.S.C. §§ 1841–1852 (2012) and in scattered sections of 26 U.S.C.), or other laws and rules governing U.S. banks. Although banking services might seem to be some of the most fundamental of financial services, this Article's exclusion of banking regulation reflects the fact that the objectives of that regulation are largely dissimilar to those of other types of financial services regulation. See Heidi Mandanis Schooner, Regulating Risk Not Function, 66 U. Cin. L. Rev. 441, 467–68, 478 (1998) (observing "primary purpose of bank regulation is the maintenance of the safety and soundness of banking institutions," which serves "end of stemming the risk to the bank insurance fund and systemic risk," whereas "primary purpose of regulation of securities activities is investor protection"). This Article also does not discuss regulation of insurance policies and products because insurance regulation generally remains within the purview of the states and, therefore, reflects disparate approaches. See Daniel Schwarcz, Regulating Insurance Sales or Selling Insurance Regulation?: Against Regulatory Competition in Insurance, 94 Minn. L. Rev. 1707, 1708 (2010) (noting "[f]or the last two centuries, individual states and U.S. territories have been entrusted with primary responsibility for regulating property, casualty, and life insurance markets" and "each jurisdiction has its own insurance regulator and set of insurance laws").

6. See Henry N. Butler & Larry E. Ribstein, Opting out of Fiduciary Duties: A Response to the Anti-Contractarians, 65 Wash. L. Rev. 1, 44–45 & n.186 (1990) (arguing existence of agency costs in corporate context does not justify legal rules mandating particular fiduciary standards); Alan R. Palmiter, Toward Disclosure Choice in Securities Offerings, 1999 Colum. Bus. L. Rev. 1, 7–29 (describing and questioning "regulatory tenets" that ground U.S. regulation of securities offerings).

However, entities very often are not self-contained. They frequently are components of groups of affiliated entities that, together, pursue related or mutually beneficial activities as a larger enterprise—as an association of entities, in other words.[7] Indeed, this is evident from society's collective and concerted focus in recent years on addressing the systemic implications of "too big to fail" institutions—firms that often comprise scores of entities but that society regards (and perhaps fears) as unitary actors. We have no difficulty—and, if anything, it seems only natural—to disregard the myriad entities that constitute a multinational enterprise or other conglomerate and, instead, to think of the enterprise as a unitary being. For example, we tend to refer to Goldman Sachs as an "it," even though, as a web of parent companies, subsidiaries, and affiliates, Goldman Sachs could as easily be considered a "they."[8] It may, therefore, come as a surprise that financial services regulation tends to take the opposite approach and, in particular, to pay all too much attention to the enterprise's building blocks—namely, the entities of which it consists. To use an old idiom, regulation does not see the forest for the trees.

Regulatory entity-centrism is not an isolated phenomenon in the financial services realm. It pervades most types of laws and rules, from those governing a firm's[9] initial registration with the relevant regulatory body (for example, a brokerage firm's registration with the Securities and Exchange Commission (SEC) as a broker-dealer),[10] to the substantive requirements to which the regulated firm must adhere,[11] to the firm's ultimate insolvency or liquidation.[12] In addition, entity-centrism does not discriminate among financial services activities, as it can be readily found in laws and rules covering securities broker-dealers, mutual funds and other registered investment companies, investment advisers, and futures commission merchants and other intermediaries for commodity futures transactions. Entity-centrism in financial services regulation is pervasive. It is, furthermore, deeply problematic.

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7. See, e.g., Virginia Harper Ho, Theories of Corporate Groups: Corporate Identity Reconceived, 42 Seton Hall L. Rev. 879, 885 (2012) ("Most major public corporations are in fact part of corporate groups that contain hundreds or even thousands of affiliated companies around the world.").

8. See Goldman Sachs Grp., Inc., Annual Report (Form 10-K) exh. 21.1 (Mar. 1, 2013), available at http://www.goldmansachs.com/investor-relations/financial/current/10k/2012-10-K.pdf (on file with the *Columbia Law Review*) (listing over eighty "significant subsidiaries of The Goldman Sachs Group, Inc. as of December 31, 2012").

9. This Article uses "firm" to refer to an economic association, whether it consists of one entity or multiple entities.

10. See infra Part I.A (explaining different types of financial services regulation designate entity as regulatory subject).

11. See infra Part I.B.1–2 (describing ways in which regulation of investment advisers and mutual funds centers on entity).

12. See infra Part I.B.3 (explaining laws and rules governing bankruptcy are entity-centric).

This Article's goal is to show how entity-centrism, as manifested in financial services regulation, defeats regulatory objectives. To put it succinctly, entity-centrism counters regulatory goals by privileging entity boundaries over the various ways in which entities, or entities and individuals, work together as part of a common enterprise. Entity-centrism insists that the subject and/or beneficiary of regulatory obligations is cohesive and complete in and of itself and thereby ignores how those whom regulation generally exists to protect—clients and customers—may be situated outside the entity, leaving their interests vulnerable, or how actors outside the entity may use the entity to manipulate or escape regulatory obligations, again leaving the relevant interests without the protections that the regulations themselves contemplate.

Of course, one might reasonably believe that entity-centrism furthers important regulatory goals. After all, as suggested above, the corporate person and other forms of business association are deemed critical to a thriving capitalist economy. When an investor invests in a business organized as one of these entity forms, the entity structure limits the possible liability the investor might incur as a result of her partial ownership of the business to the amount of her investment, thereby encouraging investment activity and, beyond that, "capital formation."[13] Perhaps, then, the entity is similarly critical to a thriving financial services regulatory regime. Even without more, however, that proposition is dubious based simply on a consideration of the economic role of corporations (and other entity forms). The corporation's primary function, stated most broadly, is to encourage the coming together of business managers, on the one hand, and suppliers of capital, otherwise known as investors, on the other.[14] From a practical perspective, the corporate form ensures (albeit with a few exceptions) that investors will not be made responsible for the corporation's debts and liabilities.[15] From a more theoretical per-

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13. David Millon, Piercing the Corporate Veil, Financial Responsibility, and the Limits of Limited Liability, 56 Emory L.J. 1305, 1309, 1312 (2007) (noting "limited liability protects . . . shareholders from personal responsibility for corporate obligations," which encourages investment from those who would be reluctant to invest if doing so put their personal wealth at risk). Capital formation is the process of increasing an economy's capital stock (such as buildings, equipment, and other productive goods). Capital Formation, Investopedia, http://www.investopedia.com/terms/c/capital-formation.asp (on file with the *Columbia Law Review*) (last visited Oct. 7, 2013). Capital stock, combined with labor, is a necessary condition for an economy's production of goods and services and income growth. See id.

14. Limited liability furthers this purpose by attracting investors to businesses. See D. Gordon Smith & Cynthia A. Williams, Business Organizations: Cases, Problems, and Case Studies 221 (3d ed. 2012) (recounting how, in eighteenth century, limited liability for investors "was a major factor in the decision to seek incorporation for many businesses").

15. See Austin v. Mich. State Chamber of Commerce, 494 U.S. 652, 658–59 (1990) ("State law grants corporations special advantages—such as limited liability, perpetual life, and favorable treatment of the accumulation and distribution of assets—that enhance their ability to attract capital and to deploy their resources in ways that maximize the

spective, the corporate form is a formal, legal embodiment and representation of the most efficient mode of economic production—namely, the firm.[16]

Achieving efficiency in productive relationships (such as between entrepreneurs and capital suppliers) and limiting liability are not primary objectives of financial services regulation, although, to be sure, one goal of that regulation is to promote efficiency and productivity.[17] Financial services regulation, as this Article conceives it, is the regulation of those—whether entities or individuals—who supply finance- and investment-related services to third parties. Examples include securities brokers, futures brokers, and investment advisers. Further, financial services regulation governs both the ongoing provision of those services and the process of their cessation, as evidenced by laws and rules covering financial firm liquidations and bankruptcies.[18] In financial services regulation, there is no need to use the entity as the unit of analysis, as there is nothing about what financial services regulation does—protecting the "users" of financial services and promoting the integrity of the financial services and capital markets—that cannot extend beyond entity boundaries.

Indeed, that conclusion is at least implied by instances in which regulation's entity focus has given way to superentity doctrines or, at least, confusion and debate about the regulatory weight to be placed on the entity. For example, in various contexts, the SEC has embraced an entity-boundary-be-damned approach to regulatory interpretation and

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return on their shareholders' investments."), overruled by Citizens United v. FEC, 130 S. Ct. 876 (2010).

16. A firm is an aggregation of economic transactions that occur beyond the framework of the market and thus avoid the transaction costs that accompany market relationships. See R.H. Coase, The Nature of the Firm, 4 Economica 386, 391–92 (1937) (explaining how costs associated with obtaining necessary resources through transacting in open market impel entrepreneurs to form firms, in which they can better control and direct those resources); see also Charles R.T. O'Kelley & Robert B. Thompson, Corporations and Other Business Associations: Cases and Materials 3 (6th ed. 2010) (describing "essence of the firm" as "entrepreneur's management and conscious direction of resource allocation decisions" to perform tasks "that cannot as efficiently be handled via market transactions"); Matthew T. Bodie, The Post-Revolutionary Period in Corporate Law: Returning to the Theory of the Firm, 35 Seattle U. L. Rev. 1033, 1040–41 (2012) (summarizing Coase's well-known theory of organization of economic activity in firms). Of course, because the firm refers to an economic enterprise, rather than a legal form, any particular firm, in the Coasean sense, might comprise more than one corporation or other legal entity. See Douglas G. Baird & Anthony J. Casey, No Exit? Withdrawal Rights and the Law of Corporate Reorganizations, 113 Colum. L. Rev. 1, 4 n.12 (2013) ("An economic enterprise directed by a single entrepreneur can be split into several legal entities, or conversely, several disconnected enterprises can be brought under one legal umbrella.").

17. See Steven L. Schwarcz, Private Ordering, 97 Nw. U. L. Rev. 319, 330–32 (2002) (acknowledging efficiency as one goal of regulation but questioning premise, prevalent in legal doctrine and scholarship, that it is only goal).

18. See, e.g., 11 U.S.C. §§ 741–753 (2012) (setting forth rules for liquidation of broker-dealers).

enforcement. That approach is the apparent inspiration behind the SEC's mantra that, under the securities laws, one is not permitted to do indirectly what she is not permitted to do directly.[19] Rephrased: One cannot break into multiple steps what one is not permitted to do in one step; one cannot pursue through multiple entities an activity that one is not permitted to do using one entity; and so on. In addition, under the securities laws, a regulated entity's unlawful actions may also subject the entity's parent company or affiliates to liability, such as through the doctrine of "control person" liability.[20]

Similarly, in the realm of banking regulation, Supreme Court and federal court cases from the 1970s and 1980s regarding what activities banks were permitted to conduct under the now-repealed Glass-Steagall Act[21] often turned on whether banks' offerings, to customers and others, of interests in "pooled" investment entities—i.e., investment funds—created by the banks constituted transactions in "securities."[22] If, by offering shares of the investment funds, the banks were deemed to be offering securities, then the banks would be violating Glass-Steagall's prohibition on a bank's engagement in the activity of offering securities.[23] That the question arose was not surprising: Ownership interests in investment

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19. This doctrine appears both in the SEC's regulatory interpretations and "no-action" letters and in its rulemaking under the securities statutes. See, e.g., 17 C.F.R. § 270.2a51-3 (2013) (prohibiting company from being deemed "qualified purchaser" under Investment Company Act of 1940 ("Investment Company Act") if company was "formed for the specific purpose" of making particular private fund investment, "unless each beneficial owner of the company's securities is a qualified purchaser"). The doctrine is, moreover, consistent with Congress's mandate in the securities laws. See, e.g., 15 U.S.C. § 80b-8(d) (2012) ("It shall be unlawful for any person indirectly, or through or by any other person, to do any act or thing which it would be unlawful for such person to do directly under the provisions of this subchapter or any rule or regulation thereunder.").

20. In particular, section 20(a) of the Exchange Act provides that "control persons" might incur liability based on the actions of those under their control. See 15 U.S.C. § 78t(a) (mandating, with limited exceptions, that "[e]very person who, directly or indirectly, controls any person liable under any provision of this chapter or of any rule or regulation thereunder shall also be liable jointly and severally . . . to any person to whom such controlled person is liable").

21. Banking Act of 1933, ch. 89, 48 Stat. 162 (codified as amended at 12 U.S.C. §§ 24, 78, 377–78 (1994)) (repealed 1999).

22. See Inv. Co. Inst. v. Camp, 401 U.S. 617, 624 (1971) (describing question presented as whether "creation and operation of an investment fund by a bank which offers to its customers the opportunity to purchase an interest in the fund's assets constitutes the issuing, underwriting, selling, or distributing of securities or stocks in violation of" Glass-Steagall Act); Inv. Co. Inst. v. Conover, 790 F.2d 925, 926–27 (D.C. Cir. 1986) (framing question as whether to uphold Comptroller of the Currency's determination that Citibank's organization and operation of "collective investment trust" complied with requirements of Glass-Steagall Act).

23. See *Camp*, 401 U.S. at 625 (observing "[o]n their face, [sections] 16 and 21 of the Glass-Steagall Act appear clearly to prohibit" bank's "issuing and selling stock or other securities evidencing an undivided and redeemable interest in the assets of the fund" (internal quotation marks omitted)); *Conover*, 790 F.2d at 927–28 (noting "Glass-Steagall Act prohibits national banks from engaging in the securities business").

funds were (and still are) generally thought to be securities, much like ownership interests in entities that pursue noninvestment activities.[24] The interpretation urged by the banks, on the other hand, was, in essence, that they were not offering securities. In their view, although the pooled investment structure necessarily exists in the form of an entity (one that, yes, offers and sells ownership interests), the structure exists solely to enable the banks to perform permissible banking services for multiple customers simultaneously.[25] In other words, the offerings should be evaluated solely based on the substance of the services provided, rather than the circumstance that a separate entity is involved. By countenancing that interpretation, as the courts sometimes did,[26] the courts also countenanced the inappropriateness of entity-centrism.

These exceptions show that approaches to regulation can be more flexible and more malleable than entity-centrism permits, and that entity-centrism is not a regulatory necessity. The exceptions are, however, exactly that—exceptional and sporadic—and, in any event, fail to engage a broader analysis of entity-centrism as an animating regulatory principle. Yet, if entity-centrism is not necessary and, indeed, may be counter-productive or harmful, what explains its existence and persistence? Addressing that question is an additional challenge of this Article, one that it can only begin to tackle. However, when one considers the history of many types of financial services regulation, a few themes begin to emerge. One is that much of financial services regulation arose as a complement to "core" securities regulation, which very much has the entity as its focus, and appropriately so.[27] Other bases of entity-centrism are more obscure but can be seen in an evaluation of how financial services have changed over the past century, combined with the circumstance that many laws and rules have remained largely dormant over that time.[28] Because those laws and rules have not (until recently, in some cases) been put to the test, their entity-centric shortcomings have not been discerned or challenged and, therefore, remain uncorrected.[29]

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24. See *Conover*, 790 F.2d at 928 (observing SEC "ha[d] in the past opined that ownership interests in collective trust funds are 'securities' for purposes of the federal securities laws").

25. See *Camp*, 401 U.S. at 634 ("It is argued that a bank investment fund simply makes available to the small investor the benefit of investment management by a bank trust department . . . and that . . . an investment fund creates no problems that are not present whenever a bank invests in securities for the account of customers.").

26. See *Conover*, 790 F.2d at 938 (affirming Comptroller's conclusion that collective investment trust at issue did not violate Glass-Steagall Act).

27. See infra Part III.A (suggesting entity-centrism may have arisen as extension of entity focus of other components of securities laws).

28. See infra Part III.B (suggesting entity-centrism may be in part attributable to policymakers' failure to reevaluate decades-old laws and rules).

29. See infra Part III.B (describing this oversight and labeling it "regulatory atrophy").

This Article contends that financial services regulation needs to look past entity boundaries. Lawmakers and regulators need to think more broadly to address the significant regulatory difficulties—such as regulators' ineffective responses to customer harm, including the theft or misplacement of customer assets—that have arisen over the past several years and that show no sign of abating. Addressing entity-centrism is one way of doing that. Of course, with that argument a number of further challenges present themselves. No longer regarding the entity as the center of the regulatory universe would seem to mean introducing tremendous additional complexity to a sphere of regulation that is already all too complex. However, postponing the necessary reorientation of policy assumptions will not render that reorientation more manageable later. It is time to begin replacing entity-centrism with a greater focus on the practical effects and deficiencies of entity-centric laws and rules.

This Article begins, in Part I, by describing the ways in which regulation of financial services firms is entity-centric. Focusing on provisions of the securities laws and related rules pertaining to financial services, it shows how entity-centrism is manifested in myriad aspects of that regulation, including registration requirements, discrete substantive obligations, and liquidation procedures. Using two recent regulatory failures as case studies, Part II shows how the incongruence between regulation's entity-centrism, on the one hand, and the reality of how financial services are provided, on the other, contradicts the primary objective of financial services regulation: client and customer protection. This Part examines the recent bankruptcy of MF Global, a futures brokerage firm that became insolvent in 2011,[30] and the Ponzi scheme orchestrated by the Stanford Financial Group, which came to light in 2009.[31] It contends that, in both cases, the entity focus of relevant laws and rules deprived victimized customers of the extensive protections those laws and rules would otherwise have provided.

As a first step toward moving beyond entity-centrism in financial services regulation, Part III delves into the bases of regulation's fixation on the stand-alone entity. It focuses on the influence of corporate governance norms on the earliest forms of financial services laws and rules and, further, suggests that some laws and rules have become weak through disuse and insufficient critical evaluation of their core deficiencies. Finally, in Part IV, the Article posits that, to achieve more workable and effective financial services regulation, new approaches to its formulation must emerge—approaches that not only acknowledge and search for tendencies toward entity-centrism but that also address the problem comprehensively. This Part points to circumstances in which

30. See infra Part II.A (describing entity-centrism of MF Global bankruptcy).

31. See infra Part II.B (describing entity-centrism of regulation of Stanford Financial Group).

lawmakers and regulators should be especially alert to an unwarranted elevation of the entity over the ways in which financial services firms actually operate and, in broad strokes, suggests proposals for overcoming entity-centrism in specific regulatory contexts.

I. ENTITY-CENTRISM

Financial services regulation embodies entity-centrism, in that it is largely premised on the notion that the entity is the appropriate unit of regulation. "Entity" in this rubric encompasses any of the fundamental organizational building blocks of a business enterprise, including, among others, corporations, partnerships, limited liability companies, and variations thereof (such as limited liability partnerships, limited liability limited partnerships, S-corporations, and more).[32] In focusing on entities, financial services regulation tends to neglect how interentity relationships and activities may further or impede regulatory objectives. Instead, regulation is informed by corporate governance norms, which characteristically have centered on the entity and, in particular, its internal relationships and functions, usually without reference to persons (individuals or other entities) outside the entity.[33] Because corporate governance norms structure the relationships between a firm's management, on the one hand, and its shareholders, on the other, those norms are, almost by definition, entity-focused. Indeed, corporate governance principles have traditionally involved extra-entity persons only in connection with shareholders' failures to maintain entity integrity or formalities.[34] The most prominent example in this regard is a liability doctrine commonly known as "veil piercing." Under this doctrine, a corporation's controlling shareholder might be deemed responsible for the firm's financial liabilities, to the extent the shareholder effectively was the corporation's alter ego, using the corporation as a vehicle through which the shareholder pursued her own activities and objectives.[35]

To be sure, even in the corporate governance context, the law's inward focus has not been immune to challenge or criticism. In recent years, for example, scholars and commentators have begun to question the standard corporate focus on shareholders and, in particular, increasing shareholder value.[36] Perhaps as a result of such challenges, various

32. See Smith & Williams, supra note 14, at 93–95 (discussing differences between entity forms).

33. See id. at 197–204 (describing respective rights and roles of directors and shareholders as participants in corporate management).

34. See id. at 222–23 (discussing circumstances in which corporation's liabilities might be imposed directly against shareholder based on shareholder's conduct).

35. See, e.g., Robert B. Thompson, Piercing the Corporate Veil: An Empirical Study, 76 Cornell L. Rev. 1036, 1039–43 (1991) (describing corporate veil piercing doctrine).

36. See Lynn Stout, The Shareholder Value Myth: How Putting Shareholders First Harms Investors, Corporations, and the Public, at vi (2012) (questioning and criticizing

states have adopted so-called "other constituency" statutes.[37] These statutes authorize corporate directors, in their decisionmaking, to consider factors beyond shareholders' interests, such as how a decision might affect employees, the environment, or the community as a whole.[38] In addition, because the very role of the board of directors as entity decisionmakers embodies an inward, entity-based focus, some scholars have come to question the notion of placing ultimate corporate management authority in the corporate board.[39] These analyses at least implicitly question the entity-centrism of corporate governance principles, notwithstanding that the subject of corporate governance is undeniably the single, solitary corporate entity. If one can reasonably question entity-centrism in the realm of corporate governance, then surely it deserves a critical analysis in financial services regulation. Yet until now that analysis has not occurred in any meaningful way.

As the case studies in Part II elaborate, this regulatory myopia has meant that financial services regulation is less effective than it might

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"conventional shareholder value thinking"); Matthew T. Bodie, AOL Time Warner and the False God of Shareholder Primacy, 31 J. Corp. L. 975, 1001 (2006) (questioning, based on AOL Time Warner merger, "whether shareholder wealth maximization should really be the ultimate arbiter of corporate value"); Robert Sprague, Beyond Shareholder Value: Normative Standards for Sustainable Corporate Governance, 1 William & Mary Bus. L. Rev. 47, 72–81 (2010) (arguing against "shareholder primacy approach to corporate governance"); Gordon Pearson, The Truth About Shareholder Primacy, Guardian (Apr. 27, 2012, 12:18 PM), http://www.guardian.co.uk/sustainable-business/short-termism-shareholder-long-term-leadership (on file with the *Columbia Law Review*) ("The world—business leaders, politicians, academics, and even the people in the street—have come to believe that it is the legal duty of those who run businesses to maximise the wealth of shareholders, and to hell with everything else. But it is simply not the case.").

37. See, e.g., Iowa Code § 491.101B (1999) ("A director, in determining what is in the best interest of the corporation when considering a tender offer or proposal of acquisition, merger, consolidation, or similar proposal, may consider [a number of] community interest factors . . . ."); Mass. Gen. Laws ch. 156B, § 65 (2013) (providing directors, in determining corporation's best interests, may consider, among other things, "the interests of the corporation's employees, suppliers, creditors and customers, the economy of the state, region and nation, [and] community and societal considerations"); 15 Pa. Cons. Stat. Ann. § 1715 (West 2013) (providing directors, in carrying out duties, may consider how any action might affect "employees, suppliers, customers[,] . . . creditors[,]" and local communities, in addition to shareholders).

38. Charles Hansen, Other Constituency Statutes: A Search for Perspective, 46 Bus. Law. 1355, 1355 (1991) ("The typical [other constituency] statute provides that in acting in the best interests of the corporation, the directors may take into account the interests of a variety of constituencies other than shareholders, including employees, the communities in which facilities of the corporation are located, customers, and suppliers."); Amir N. Licht, The Maximands of Corporate Governance: A Theory of Values and Cognitive Style, 29 Del. J. Corp. L. 649, 700–05 (2004) (summarizing history, content, and efficacy of other constituency statutes).

39. See, e.g., Kelli A. Alces, Beyond the Board of Directors, 46 Wake Forest L. Rev. 783, 785–86 (2011) ("Corporate officers and the investors and parties in interest that are essential to the firm's daily operation and capital structure—the *real* corporate decision makers—should perform the functions assigned to the board, so that the now-vestigial board of directors can completely wither away.").

otherwise be. With a view toward providing context for that discussion, this Part describes, in general terms, how entity-centrism has manifested itself in financial services regulation. It does so by focusing primarily, though not exclusively, on regulation of firms providing securities-related financial services. Although financial services regulation subsumes not only securities regulation (some aspects of it, at least[40]) but also commodity futures regulation, banking regulation, and insurance regulation,[41] securities regulation is perhaps the most prominent and controversial component of financial services regulation. It encompasses not only regulation of securities broker-dealers, which serve as intermediaries for securities transactions, but also regulation of mutual funds (and other registered investment companies) and investment advisers, which manage accounts on behalf of securities investors, from mutual funds to hedge funds to individuals.[42] Part I.A discusses how, as to a variety of securities-related financial services, entity-centric principles determine the regulatory subject. Part I.B describes ways in which entity-centrism counters regulatory goals, focusing on the investment advisory and mutual fund contexts and introducing the entity-centric concerns that arise in connection with resolving or liquidating insolvent financial services firms.

A. *The Subject of Regulation*

Entity-centrism is evident in the fundamental matter of designating the regulatory subject. A firm's financial services activities may require the firm to register under the appropriate regulatory regime and, thereafter, to satisfy applicable regulatory requirements and become subject to examinations and possible enforcement proceedings by the relevant regulator. A firm that desires to perform investment advisory services, for example, must satisfy investment adviser registration requirements and thereby become regulated by either the SEC[43] or the appropriate state securities regulator(s).[44] If, as is often the case, the "firm" consists of

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40. See infra notes 249–255 and accompanying text (describing components of securities regulation also regarded as financial services regulation).

41. That "financial services regulation" encompasses all of these categories of regulation is evident in the fact that each was a subject of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"), Pub. L. No. 111-203, 124 Stat. 1376 (2010), and that this statute is characterized as a "substantial overhaul of the regulation of all providers of financial services." Sarah Jane Hughes, Developments in the Laws Governing Electronic Payments, 67 Bus. Law. 259, 259 (2011).

42. See James D. Cox, Robert W. Hillman & Donald C. Langevoort, Securities Regulation: Cases and Materials 1075–79, 1093–99 (6th ed. 2009) (summarizing regulation of investment advisers and registered investment companies under Investment Advisers Act of 1940 ("Advisers Act") and Investment Company Act).

43. The relevant federal statute is the Advisers Act, 15 U.S.C. §§ 80b-1 to 80b-21 (2012).

44. See Staff of the Inv. Adviser Regulation Office, Div. of Inv. Mgmt., SEC, Regulation of Investment Advisers by the U.S. Securities and Exchange Commission 8–9

multiple entities, it must cause certain of those entities, depending on their functions, to become so registered. Accordingly, the particular entities that become registered as investment advisers are also, not surprisingly, the units that are required to comply with regulatory requirements and the units through which the firm must provide its investment advisory services to clients.[45] Moreover, the investment adviser registration and regulation of any particular entity typically occurs separately from, and independently of, the registration and regulation of any other entity.[46]

The same goes for firms aiming to act as securities broker-dealers, which buy and sell securities either as intermediary agents (meaning they bear no risk and receive commissions as compensation) or as principals (meaning they transact for their own account and, accordingly, bear the associated risk).[47] A firm's becoming registered as a broker-dealer involves its registering the relevant entity or entities with the SEC under the Securities Exchange Act of 1934 ("Exchange Act")[48] and subjecting those entities to the SEC's ongoing regulatory supervision.[49] Similarly, a firm seeking to sponsor[50] mutual funds or other publicly offered investment companies must, in order to do so, register the "company" (that is, the fund, an entity) with the SEC under the Investment Company Act of

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(2013) [hereinafter SEC, Regulation of Investment Advisers], available at http://www.sec.gov/about/offices/oia/oia_investman/rplaze-042012.pdf (on file with the *Columbia Law Review*) (noting role of states in regulating investment advisers). Investment adviser regulation governs investment advisers to investment vehicles, such as mutual funds and hedge funds, as well as to other types of advisory clients, such as individuals and endowments. See id. at 8–17 (listing types of investment advisers required to become registered under Advisers Act).

45. To be sure, in the registration process, the registering entity may be required to disclose to the regulator the existence of affiliated entities, yet the affiliates are not themselves directly subject to the regulatory requirements that accompany registration. See id. at 18–19.

46. Cf. American Bar Association, Business Law Section, SEC No-Action Letter, 2012 WL 160552, at *4 (Jan. 18, 2012) (noting investment adviser registration form "was not designed to combine information about separately formed advisers that conduct different advisory businesses, even if those advisers are related to each other because of a control relationship").

47. See SEC, Form BD, Uniform Application for Broker-Dealer Registration 2, available at http://www.sec.gov/about/forms/formbd.pdf (on file with the *Columbia Law Review*) (last visited Oct. 7, 2013) (requiring any broker-dealer applicant to indicate whether it is corporation, partnership, limited liability company, sole proprietorship, or "other" and to state where "applicant entity" was incorporated, filed its partnership agreement, or was formed).

48. 15 U.S.C. §§ 78a–78kk.

49. See Div. of Trading & Mkts., SEC, Guide to Broker-Dealer Registration, U.S. Sec. & Exch. Comm'n (Apr. 2008), http://www.sec.gov/divisions/marketreg/bdguide.htm (on file with the *Columbia Law Review*) (summarizing broker-dealer regulation).

50. "Sponsoring" a fund generally encompasses orchestrating the fund's formation, coordinating the fund's arrangements with its investment adviser(s) and other service providers, and overseeing the commencement of the fund's activities and the fund's ongoing operations.

1940 ("Investment Company Act")[51] and comply with the associated obligations.[52]

The imposition of registration requirements and substantive obligations on entities, as opposed to super- or supra-entity units, holds also in nonsecurities contexts. For example, firms desiring to act as futures commission merchants, which serve as brokers for transactions involving commodity futures, similarly must submit to regulation as such by registering an entity with the Commodity Futures Trading Commission (CFTC) under the Commodity Exchange Act of 1936 ("Commodity Exchange Act")[53] and, thereafter, must cause that entity to adhere to the associated regulatory strictures.[54] Firms that intend to act as commodity trading advisors (the investment-adviser counterparts to accounts that pursue commodity futures trading activities rather than securities-focused activities) or commodity pool operators, which sponsor funds that pursue commodity futures trading, must similarly register an entity with the CFTC, with that entity becoming subject to regulatory oversight.[55]

Despite the prevalence of this entity-based approach to regulatory registration and compliance, it may strike one as odd (at best) to hone in on the phenomenon as an example of entity-centrism. After all, not only are entity-registration requirements customary and uncontroversial, they perhaps seem eminently sensible. If a firm wishes to perform financial services, then the "who" or the "what" that will actually do the work needs to be defined. To the extent the services-providing activity can be confined within an entity, then should not that entity be the regulatory subject? Entity-centrism, in other words, makes things easy and likely conforms to how consumers of financial services have come to conceive of the suppliers of those services.[56]

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51. 15 U.S.C. §§ 80a-1 to 80a-64. The Investment Company Act governs not only mutual funds but also other publicly offered investment vehicles, such as exchange-traded funds.

52. See Investment Company Registration and Regulation Package, U.S. Sec. & Exch. Comm'n, http://www.sec.gov/divisions/investment/invcoreg121504.htm (on file with the *Columbia Law Review*) (last modified Dec. 21, 2004) (summarizing investment company regulation).

53. See 7 U.S.C. § 6d(a)(1) (2012) ("It shall be unlawful for any person to be a futures commission merchant unless . . . such person shall have registered . . . with the [Commodity Futures Trading] Commission . . . .").

54. See Futures Commission Merchants (FCMs) & Introducing Brokers (IBs), U.S. Commodity Futures Trading Comm'n, http://www.cftc.gov/IndustryOversight/Intermediaries/FCMs/index.htm (on file with the *Columbia Law Review*) (last visited Oct. 7, 2013) (summarizing regulatory requirements applicable to FCMs).

55. See Commodity Pool Operators (CPOs) & Commodity Trading Advisors (CTAs), U.S. Commodity Futures Trading Comm'n, http://www.cftc.gov/IndustryOversight/Intermediaries/CPOs/index.htm (on file with the *Columbia Law Review*) (last visited Oct. 7, 2013) (summarizing regulatory requirements applicable to CTAs and CPOs).

56. For example, an investor who wishes for a portfolio manager employed by Citigroup Alternative Investments to manage her retirement account assets need only

For present purposes, the point is simply that, even for the seemingly pedestrian matter of defining the regulatory subject, designating the entity as the regulatory unit is not the only possible option. For example, in the mutual fund context, rather than the fund being the "registrant" subject to investment company regulation, the regulatory subject could instead be those who have been engaged to provide investment advice to the mutual fund and, indirectly, to its shareholders.[57] That approach would be more desirable, for example, based on the recognition that a mutual fund may be viewed merely as a facilitating structure, one that allows the fund's investment adviser to provide advisory services to the fund's shareholders.[58] From that perspective, directing regulatory obligations toward those who control the fund and are responsible for its existence and ongoing operations may better promote regulatory goals.[59]

Similarly, in theory, the subject of broker-dealer or investment adviser regulation could, instead, be the (multi-entity) enterprise itself or even subentity divisions within the enterprise.[60] Such an approach might be more desirable to the extent that the activities of any particular entity within the enterprise are determined based on factors other than the performance of a particular kind of financial service. For example, if a division (involving only a portion of the employees) of a U.K. Morgan Stanley entity and a division (involving only a portion of the employees) of a U.S. Morgan Stanley entity provide investment advisory services only to U.S. institutional investors, then, in the name of achieving more efficient and streamlined regulation, it may make sense for those two divisions to be jointly subject to U.S. investment adviser regulation—and only that regulation. Under the entity-based approach, however, in addition to the U.S. entity being separately registered and regulated in

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enter into an agreement with that entity, which, as one might imagine, is registered and regulated as an investment adviser. Investment Adviser Public Disclosure: Citigroup Alternative Investments LLC, U.S. Sec. & Exch. Comm'n, http://www.adviserinfo.sec.gov/IAPD/Content/Search/iapd_landing.aspx?SearchGroup=Firm&FirmKey=119537&BrokerKey=-1 (on file with the *Columbia Law Review*) (last visited Oct. 7, 2013). If, instead, the investor would like to open a brokerage account with Citigroup, she will enter into an agreement with a Citigroup entity that is registered and regulated as a broker-dealer.

57. See Anita K. Krug, Investment Company as Instrument: The Limitations of the Corporate Governance Regulatory Paradigm, 86 S. Cal. L. Rev. 263, 305–11 (2013) [hereinafter Krug, Investment Company as Instrument] (arguing investment company regulation would better further its goals by focusing on investment company's investment adviser, rather than on company and its board of directors).

58. See id. at 265–66 (observing mutual funds exist "solely to facilitate the provision of investment advice to [mutual fund] shareholders").

59. See id. at 311 (arguing mutual fund regulation focusing on fund's investment adviser would be "more coherent[] and ultimately . . . more effective" than regulation focusing on mutual fund itself).

60. The latter approach might make sense to the extent that it is more coherent, from a functional perspective, for divisions within different entities to be involved in the provision of the relevant financial services.

the United States (and, quite possibly, the United Kingdom), based on each type of financial services it provides and where those services are provided, the U.K. entity likewise would be registered and regulated in both the United Kingdom and the United States.[61]

Finally, consider an arrangement in which portfolio managers or other personnel within a financial services firm provide a number of distinct types of investment advisory services through separate entities. The group may, through one entity, provide discretionary investment advisory services focusing on positions in equities and instruments derivative of equities. The group might, at the same time, and through a different entity, carry out investment advisory services focusing on real estate and real estate securities. In these circumstances, the separation of the investment advisory services into two separate entities may promote organizational efficiency and serve the goal of associating liabilities arising from a particular type of advisory activity with the assets underlying that activity.[62] Yet, in light of the common ownership and personnel, allowing both entities to become jointly registered and treated as a single unit may create substantial regulatory efficiencies, in the sense of permitting lower compliance costs (for the firm) and lower oversight costs (for the SEC or other relevant regulators).

This discussion suggests that making the entity the discrete regulatory subject, as opposed to entity subcomponents or supercomponents, does not necessarily achieve anything that one of these alternative approaches could not achieve, except that the entity-based approach may be a more bright line specification of what is to be regulated.[63] There is

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61. See, e.g., SEC, Regulation of Investment Advisers, supra note 44, at 7 ("Non-U.S. persons advising U.S. persons are subject to the [Investment Advisers] Act and must register under the Act . . . ."); see also 15 U.S.C. § 80b-3(a) (2012) (requiring any investment adviser to register pursuant to Advisers Act before lawfully making use of instrumentalities of interstate commerce); Banco Espirito Santo S.A., Securities Act Release No. 9270, Exchange Act Release No. 65,608, Investment Advisers Act Release No. 3304, 2011 WL 5039037 (Oct. 24, 2011) (issuing cease-and-desist order and determining Portugal-based bank that was not registered with SEC and offered brokerage services to U.S. customers violated sections of Securities Act of 1933, Exchange Act, and Advisers Act); cf. Remarks by Governor Susan Schmidt Bies, 37 Conn. L. Rev. 715, 716 (2005) (observing "[a]s large U.S. banks have expanded their international operations, they have . . . become subject to supervision in their host countries," and "as foreign banking organizations . . . have established [branches in the United States] . . . they, too[,] have become subject to additional supervision").

62. In a variation of this structure, a single management group might oversee two or more groups of personnel that carry out different types of financial services through separate entities under the parent company's umbrella.

63. It is also worth considering, however, whether the entity-based approach actually delineates the regulatory object more clearly. To the extent that, for example, components of different entities perform financial services activities as part of the larger enterprise, regulation of those activities under the existing approach means registration of multiple entities, with each one independently satisfying the relevant regulatory requirements. See supra notes 43–55 and accompanying text (describing how, in various financial services contexts, entity is regulatory subject). By recognizing that different entities may be

no need to reach a definitive conclusion on that possibility. The discussion, however, frames a deeper evaluation of financial services regulation and, in particular, an examination of other contexts in which entity-centrism grounds legal rules and analysis but in which that circumstance is less obvious and its rationale less intuitive. Indeed, as the next section highlights, in multiple respects regulation's entity-centrism is inconsistent with the ways in which financial services firms actually operate. Moreover, as shown by the financial regulatory failures described in Part II, entity-centrism in these other contexts more decidedly fails to further the financial services regulatory objectives of protecting clients and customers and promoting market integrity.

B. *The Dysfunctions of Regulation*

The activities of many financial services entities are but components of a single, larger financial services enterprise represented by a parent or holding company.[64] Put another way, financial services "firms" are not so much firms at all, if that term is defined narrowly to refer to discrete legal persons.[65] However, as the previous section indicated, the propensity of regulation to focus on discrete entities within an enterprise may run counter to regulatory efficiency.[66] The fragmentation that arises from regulatory fixation on the entity may obscure the nature of relationships between entities, including possible conflicts of interest that may arise by virtue of those relationships. Whereas the previous section's discussion of the entity-based regulatory approach was largely theoretical, intended to suggest the plausibility of alternative approaches, this section turns to other contexts in which entity-centrism is evident and in which the desirability of considering alternative approaches is more apparent.

1. *Investment Advisers.* — Returning to the world of investment adviser regulation, entity-centrism can be found in regulatory doctrine governing advisory activities for privately offered funds, including hedge

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involved with the enterprise's broader financial services activities, presumably registration and regulation could become more streamlined and efficient for both the regulated and the regulator.

64. See James A. Fanto, "Breaking Up Is Hard to Do": Should Financial Conglomerates Be Dismantled?, 79 U. Cin. L. Rev. 553, 553 (2010) (noting many broker-dealers "operate within the [financial] conglomerate structure"); Martin J. Gruenberg, Acting Chairman, Fed. Deposit Ins. Corp., Remarks at the Federal Reserve Bank of Chicago Bank Structure Conference (May 10, 2012), http://www.fdic.gov/news/news/speeches/chairman/spmay1012.html (on file with the *Columbia Law Review*) ("Large financial companies conduct business through multiple subsidiary legal entities with many interconnections owned by a parent holding company.").

65. See Howell E. Jackson, The Expanding Obligations of Financial Holding Companies, 107 Harv. L. Rev. 507, 509 (1994) (describing how modern financial services institutions "operate . . . typically through a network of subsidiaries specializing in deposit-taking, insurance underwriting, securities activities, and various other financial services").

66. See supra notes 57–62 and accompanying text (suggesting possible reasons to focus regulation on units other than entity).

funds and private equity funds. For most purposes under the investment adviser regulatory framework, the fund itself—the entity—rather than those who hold ownership interests in it—the investors—is regarded as the "client" of the investment adviser that manages the fund's assets.[67] By virtue of its client status, the fund is entitled to the regulatory protections of, as the case may be, the Investment Advisers Act of 1940 ("Advisers Act")[68] or applicable state securities laws.[69] The investors, however, generally are not given those protections.

At first glance, this arrangement might not seem particularly problematic, given that the fund—and not its investors—is the direct recipient of the adviser's investment advice.[70] After all, as a legal matter, it is the fund's assets that are deployed to buy and sell securities and other investment instruments. The distinction between an individual's investing directly and investing through a fund is, however, only superficial. When an investor enters into a direct relationship with an investment adviser, the investment adviser manages the investor's assets, which are usually held in a separate account under the investor's name, apart from anyone else's assets.[71] By contrast, when an investor invests in a hedge fund, for example, the investor does not execute a contract with the adviser but instead enters into a subscription agreement with the fund, pursuant to which the investor places her assets in the fund. In those circumstances, although the fund is the legal owner of the securities in its portfolio, the investor (indirectly) has a proportionate interest in each of those securities by virtue of her holding a proportionate interest in the fund.[72]

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67. See, e.g., 17 C.F.R. § 275.202(a)(30)-1 (2013) (noting, for purposes of identifying "client" of "foreign private adviser," "partnership, limited liability company, trust . . . , or other legal organization . . . to which [the adviser] provide[s] investment advice based on its investment objectives rather than the individual investment objectives of its [investors]" may be deemed single client).

68. 15 U.S.C. §§ 80b-1 to 80b-21 (2012).

69. See supra note 44 and accompanying text (observing investment advisers may be governed by state regulatory authorities rather than by SEC).

70. See Status of Investment Advisory Programs Under the Investment Company Act of 1940, 62 Fed. Reg. 15,098, 15,102 (Mar. 31, 1997) (noting, although "client of an investment adviser typically is provided with individualized advice[,] . . . [an adviser of an investment company] has no obligation to ensure that each security purchased for the company's portfolio is an appropriate investment for each shareholder").

71. Ian Salisbury, SMAs Beat Funds in 2008, Wall St. J. (Mar. 12, 2009), http://online.wsj.com/article/SB123679669243098151.html (on file with the *Columbia Law Review*) (noting separately managed accounts (SMAs) "are a type of fee-based account" whose assets are invested by investment adviser on account holder's behalf, and SMAs differ from mutual funds in that investors in latter "own shares in a single pool of assets," whereas SMA holders "own their stocks directly").

72. See Permanent Subcomm. on Investigations, U.S. Senate Comm. on Homeland Sec. & Governmental Affairs, Tax Haven Abuses: The Enablers, the Tools and Secrecy 250 (2006) (observing hedge funds "pool investor contributions to trade in securities" and

The fund structure—one might also call it a pooled investment structure—is, at its foundation, a convenience mechanism. It is a method for an investment adviser to aggregate the assets of institutions and individuals that, at one time, would have been direct clients of the adviser.[73] That is, those who might otherwise have engaged investment advisers to manage their assets directly—and who would, in those circumstances, be considered advisory clients—now increasingly place their assets with their advisers of choice through investments in hedge funds, private equity funds, and other pooled investment entities that the advisers manage.[74] In this structure, an adviser's formal, contractual relationship is with the fund rather than with any investor in the fund.

This restructuring of investment relationships is, by and large, a product of advisers' determination that pooling investor assets in a fund structure creates management efficiencies, at least when an adviser manages most or all of the assets under its management in accordance with a single investment strategy, as opposed to tailoring its management services on a client-by-client basis.[75] The ultimate services an investor receives are virtually the same, regardless of whether the advisory relationship is direct or occurs through a pooled structure.[76] Yet, in terms of how regulation "covers" the investor—the person whose assets ultimately are at stake—the distinction is critical. To reformulate the point, an investor's investment in a private fund does not make that person a "client" of the fund's investment adviser, even though, had the investor engaged the adviser directly, the investor would have client status and the regulatory protections that come with it.[77] Those regulatory protections

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hedge fund investor "generally sign[s] a 'subscription agreement' specifying the investor's ownership interest in the fund").

73. See Anita K. Krug, Moving Beyond the Clamor for "Hedge Fund Regulation": A Reconsideration of "Client" Under the Investment Advisers Act of 1940, 55 Vill. L. Rev. 661, 690–91 (2010) [hereinafter Krug, A Reconsideration of Client] (describing efficiency rationale for "pooled asset structure").

74. See Registration Under the Advisers Act of Certain Hedge Fund Advisers, 69 Fed. Reg. 45,172, 45,173 (July 28, 2004) ("Instead of managing client money directly, [a growing number of investment] advisers pool client assets by creating limited partnerships, business trusts or corporations in which clients invest."); Steven M. Davidoff, Paradigm Shift: Federal Securities Regulation in the New Millennium, 2 Brooklyn J. Corp. Fin. & Com. L. 339, 349 (2008) (observing "sophisticated investors" increasingly place investment assets in hedge funds and other private funds).

75. See Anita K. Krug, Institutionalization, Investment Adviser Regulation, and the Hedge Fund Problem, 63 Hastings L.J. 1, 25 (2011) ("Investment funds . . . are ideal investment-management vehicles for those advisers who effectively offer strategies rather than more personal advisory services.").

76. See id. at 24–26 (describing evolution of structure of investment advisory relationships).

77. See id. at 27–30 (describing who is deemed advisory client for regulatory purposes). Although investment advisers are deemed to owe fiduciary duties to both the fund and its investors, SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 191–92 (1963), those duties are not defined, either by statute or rule, and may be (and typically are)

include the right to receive required disclosures regarding the adviser's business activities and conflicts of interest[78] and the right to provide consent (or not) to certain transactions the adviser may propose for the investor, such as securities transactions as to which the adviser has a conflict of interest.[79]

To be sure, an investor's losing the client status she would otherwise enjoy simply because she obtains advisory services in an intermediated format might cause scant concern if regarding the fund as the client achieved countervailing protections for investors. That might be the case if, for example, an independent fiduciary represented the fund on investors' behalf. That is not the typical arrangement, however. To the contrary, since the fund is usually a creature of the adviser's creation, it is typically under the adviser's control, and the fund's decisions are thus typically dictated, directly or indirectly, by the adviser.[80] Accordingly, the fund has no "voice" independent of the adviser's, and its words and actions should in no way be regarded as reflective or representative of the interests of its beneficial owners,[81] the investors.[82]

The definition of "client" is only one instance of entity-centrism in the investment advisory context. Another involves the composition of investment advisory firms. Entrepreneurs often form two separate entities

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limited by contract. Accordingly, fiduciary obligations arguably do not provide meaningful protections to fund investors.

78. See 17 C.F.R. § 275.204-3 (2013) (requiring SEC-registered investment adviser, on at least annual basis, to deliver to clients disclosure document containing "all information required by Part 2 of Form ADV"). Part 2 of Form ADV is a disclosure document that each adviser must submit to the SEC on an annual basis and that contains information regarding all aspects of the adviser's business, including conflicts of interest and other risks that may affect the adviser's management of client accounts. See SEC, Instructions for Part 2A of Form ADV: Preparing Your Firm *Brochure* 1, available at http://www.sec.gov/about/forms/formadv-part2.pdf (on file with the *Columbia Law Review*) (last visited Oct. 7, 2013) ("As a fiduciary, [an adviser] ha[s] an ongoing obligation to inform [its] *clients* of any material information that could affect the advisory relationship.").

79. See 15 U.S.C. § 80b-5(a)(2) (2012) (providing SEC-registered adviser may not enter into advisory contract that "fails to provide . . . that no assignment of such contract shall be made by the investment adviser without the consent of the other party to the contract"); id. § 80b-6(3) (prohibiting adviser from buying security from, or selling security to, client account unless adviser first obtains client's consent to transaction).

80. See Krug, A Reconsideration of Client, supra note 73, at 673 ("In the world of hedge funds and other private funds, . . . a prevalent model is for the adviser . . . to have control of the fund, either as its 'sponsor' . . . or as its general partner or manager.").

81. "Beneficial owners" as to any particular fund refers to those whose assets are at risk in the fund or, put another way, those who have the "benefits" of ownership of the fund. Black's Law Dictionary 1214 (9th ed. 2009) (defining "beneficial owner" as "[o]ne recognized in equity as the owner of something because use and title belong to that person, even though legal title may belong to someone else").

82. See Krug, A Reconsideration of Client, supra note 73, at 672–77 (describing investor protection concerns arising from circumstance that fund's investment adviser typically controls fund and speaks on its behalf).

for the purpose of operating one or more hedge funds or other private funds. To avoid certain adverse tax consequences, the entrepreneurs may form one entity to manage the fund's portfolio investments and a second entity to be its general partner or managing member.[83] Both entities play roles in the management and administration of the fund. Yet, pursuant to federal regulation, only the entity that formally acts as the investment adviser is required to become registered and regulated as such.[84] By contrast, some state regulators have reached a different conclusion and have required both entities to be separately registered and regulated,[85] thereby producing duplicative compliance costs for registrants and an inefficient use of regulatory resources. Regardless of whether one or both entities are ultimately subject to regulation, however, the circumstance that regulation centers on discrete entities means that form trumps substance.

Additionally, the entity-centrism that weakens investment adviser regulation also pervades investors' and others' understanding of that regulation and hinders their reliance on it, worsening entity-centrism's effects. For example, entity-centrism is apparent in the "due diligence" questionnaires that many investors require their prospective investment advisers to complete so that the investors may obtain additional information about the advisers' business activities.[86] Questionnaires often ask about regulatory matters, such as whether any enforcement actions have been brought against a prospective adviser.[87] Reflecting regulation's entity-centrism, the questionnaires sometimes inquire only about the

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83. See, e.g., American Bar Association Section of Business Law, SEC No-Action Letter, 2005 WL 3334980, at *28 (Dec. 8, 2005) ("[An] adviser to a private fund often establishes a special purpose vehicle . . . to act as the fund's general partner or managing member."); SEC, Regulation of Investment Advisers, supra note 44, at 18–19 (describing regulatory implications of adviser's use of special purpose general partner entities).

84. See SEC, Regulation of Investment Advisers, supra note 44, at 18–19 (describing requirements to be met for special purpose general partner entity set up by registered investment adviser so as not to have to register separately as investment adviser).

85. For example, until 2010, California followed that approach. See Cal. Corps. Comm'r Op. 7132, Commissioner's Opinion 10/1 C, at 6 (2010), available at http://www.dbo.ca.gov/Commissioner/Opinions/pdf/OP7132.pdf (on file with the *Columbia Law Review*) (concurring that California Corporations Commission would not take regulatory action against general partner entity in multi-entity investment advisory firm, provided firm complies with certain requirements).

86. See What Is a Due Diligence Questionnaire?, wiseGEEK, http://www.wisegeek.com/what-is-a-due-diligence-questionnaire.htm (on file with the *Columbia Law Review*) (last visited Oct. 7, 2013) ("A due diligence questionnaire is a thorough checklist to help a prospective investor collect information about a potential investment . . . .").

87. See, e.g., Managed Funds Ass'n, Model Due Diligence Questionnaire for Hedge Fund Investors, at I.G.1–2 (2011), available at http://www.managedfunds.org/wp-content/uploads/2011/06/Due-Dilligence-Questionnaire.pdf (on file with the *Columbia Law Review*) (exemplifying due diligence questionnaire inquiring whether investment adviser answering questionnaire has been subject to criminal or administrative proceedings).

entity that is the adviser, overlooking the commonplace prospect that an adviser's principals may own a number of other advisory entities—entities that, though not the subject of the questionnaire, may have been the subject of regulatory actions about which most investors would wish to know.

Prevailing doctrine, then, privileges the formalism of the entity. In the process, it curtails regulatory protections and may also impede the efficient use of regulatory resources. More coherent, and less entity-centric, approaches would aim to give force to regulatory objectives. Such approaches might, for example, "look through" the entity to bestow at least some protections on the entity's investors or regard a multi-entity advisory firm as a single regulatory unit.

2. *Mutual Funds.* — Entity-centrism also plagues the regulation of mutual funds and other publicly offered funds (formally known as investment companies). Because mutual funds are available to retail investors, they are, in contrast to private funds, subject to comprehensive regulation, which is set forth in the Investment Company Act[88] and the associated SEC rules.[89] That regulation is primarily aimed at mutual funds' boards of directors and relies on the directors' status as fiduciaries to the fund and its shareholders.[90] Like other corporate boards, a mutual fund's board has formal decisionmaking authority and, therefore, performs such tasks as formally approving the appointment of the fund's service providers, formally establishing the fund's valuation policies and procedures, and formally determining whether to authorize new classes of shares.[91] Also like other corporate boards, the fund's board has an oversight function and must stay apprised of the fund's activities and operations.[92]

By focusing on the persons nominally governing the fund, regulation centers on the entity with which shareholders formally have a relationship. Regulation centers on the fund, in other words. Like a private fund, however, that entity is but a means, or a mechanism, through which the investment adviser provides its services[93] and, in many respects,

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88. 15 U.S.C. §§ 80a-1 to 80a-64 (2012).

89. 17 C.F.R. §§ 270.0-1 to 270.60a-1 (2013).

90. See Indep. Dirs. Council, Fundamentals for Newer Directors 10 (2011), available at http://www.idc.org/pdf/idc_11_fundamentals.pdf (on file with the *Columbia Law Review*) ("[Mutual fund] [d]irectors have a fiduciary duty to represent the interests of the fund's shareholders . . . .").

91. A. Joseph Warburton, Should Mutual Funds Be Corporations? A Legal & Econometric Analysis, 33 J. Corp. L. 745, 750 (2008) (detailing boards of directors' responsibilities under Investment Company Act).

92. See id. at 750–51 (observing mutual fund boards have "watchdog" role and perform "monitoring function").

93. See Ben L. Fernandez, The Duties of Mutual Fund Independent Trustees with Respect to the Investment Advisory Fee, Bos. B.J., Mar.–Apr. 1997, at 12, 12–13 (observing that, by investing in mutual funds, investors select investment advisers).

is under the adviser's control.[94] And, much like an investment adviser to private funds, an adviser managing a mutual fund is typically the reason the fund exists.[95] That is, the adviser decides to create the fund as a mechanism to provide advisory services in an aggregated, pooled fashion.[96] The adviser, moreover, is often primarily responsible for selecting not only the fund's service providers, such as its administrator, its distributors, and its auditor,[97] but also the members of the fund's initial board of directors.[98] Finally, it is usually the adviser's own employees who serve as the mutual fund's chief compliance officer and any other officers the fund might have.[99] Accordingly, in this context, too, the fund can be seen as a mere facilitator of the adviser's provision of advisory services.[100]

The investment adviser's fundamental role vis-à-vis a mutual fund that it manages means that the fund's board is to some extent beholden

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94. See Tannenbaum v. Zeller, 552 F.2d 402, 405 (2d Cir. 1977) ("Control of a mutual fund . . . lies largely in the hands of the investment adviser . . . .").

95. See S. Rep. No. 91-184, at 5 (1969), reprinted in 1970 U.S.C.C.A.N. 4897, 4901 (noting separately owned and controlled investment adviser creates, markets, and manages most mutual funds).

96. See Burks v. Lasker, 441 U.S. 471, 480–81 (1979) ("A mutual fund is a pool of assets, consisting primarily of portfolio securities, and belonging to the individual investors holding shares in the fund." (citing *Tannenbaum*, 552 F.2d at 405)).

97. Cf. *Tannenbaum*, 552 F.2d at 405 (observing investment adviser has responsibility for mutual fund's operations).

98. John Morley & Quinn Curtis, Taking Exit Rights Seriously: Why Governance and Fee Litigation Don't Work in Mutual Funds, 120 Yale L.J. 84, 92 (2010) (noting mutual funds "are typically organized by their advisers, and their boards of directors are initially selected by advisers").

99. See Indep. Dirs. Council, supra note 90, at 4 (noting mutual fund's officers are typically employees of fund's investment adviser). Under the Investment Company Act rules, each investment company is required to have a chief compliance officer. 17 C.F.R. § 270.38a-1(a)(4) (2013).

100. Not surprisingly, and consistent with the regulatory approach to private funds, it is the mutual fund itself, rather than its shareholders, that is the advisory client and therefore entitled to the relevant regulatory protections. See Janus Capital Grp., Inc. v. First Derivative Traders, 131 S. Ct. 2296, 2299 (2011) (deciding whether investment adviser "can be held liable . . . for false statements" contained in prospectuses of adviser's "client mutual funds[]"). In contrast to the private fund context, however, mutual fund shareholders would likely not be direct clients of the adviser. Mutual funds are designed and regulated to be suitable for investments by so-called retail investors—in other words, investors "who lack investing experience and sophistication" or who do not have substantial investment assets. Donald C. Langevoort, The SEC, Retail Investors, and the Institutionalization of the Securities Markets, 95 Va. L. Rev. 1025, 1025 (2009). Such investors generally do not fit the profile of a direct advisory client, simply because of the associated inefficiencies. That is, for an investment adviser, managing numerous small accounts may not be worthwhile, considering the associated costs and anticipated financial benefits. See Inv. Co. Inst. v. Conover, 790 F.2d 925, 928 (D.C. Cir. 1986) (noting common trust funds permit banks to manage individuals' trust accounts where those accounts "are too small to be managed individually"). Accordingly, in contrast to the private fund context, an investor's placing assets in a mutual fund does not entail her losing the client status she might otherwise have.

to the adviser and, therefore, not truly independent of it.[101] That, in turn, means that the board may be ineffective in its role as a fiduciary to the fund and its shareholders, including in such matters as negotiating the fees the adviser will charge the fund and evaluating the adviser's activities on the fund's behalf.[102] Moreover, the difficulties arising from regulation's failure to acknowledge mutual funds' multi-entity structure are compounded by courts' following suit, embracing entity-focused principles in adjudicating claims involving mutual funds. As just one example,[103] in dismissing a fraud claim against a mutual fund's investment adviser premised on the inclusion of misleading statements in the fund's offering documents, the Supreme Court reasoned that the adviser could not be deemed the "maker" of the statements, notwithstanding that the adviser effectively controlled the fund, because the fund was the entity that had formally issued the documents, and the adviser was a separate entity from the fund.[104]

In short, given the typically close relationship between the adviser and the board, the board's associated conflicts of interest, and courts' concomitant reliance on corporate governance principles, it is doubtful that regulation's formal focus on the entity and, specifically, its governing body serves the professed objectives of mutual fund regulation. More effective and less entity-centric regulation might, instead, center on the person or organization that is, in fact, primarily responsible for the fund's existence and its success or failure. That is, regulation would focus on the investment adviser: It would recognize the adviser as providing services to the mutual fund's shareholders (albeit in an intermediated format); specify what the adviser must and cannot do in carrying out its activities on the fund's behalf, such as in connection with determining fees payable by the fund; and dispense with a meaningful regulatory role for the fund's board of directors.

3. *Insolvency and Bankruptcy.* — Entity-centrism is also apparent in the laws and rules governing the liquidation of financial services firms in

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101. Krug, Investment Company as Instrument, supra note 57, at 283 (arguing mutual fund's board members are not independent of investment adviser in part because of desire for future board appointments).

102. See Lyman Johnson, A Fresh Look at Director "Independence": Mutual Fund Fee Litigation and *Gartenberg* at Twenty-Five, 61 Vand. L. Rev. 497, 530–31 (2008) (recommending different standards of fiduciary duty in cases involving fees to counter concern that mutual fund directors are not sufficiently independent from fund's investment adviser).

103. For other examples, see Krug, Investment Company as Instrument, supra note 57, at 289–99 (describing various ways in which courts, in cases involving mutual funds, elevate entity-centric corporate governance norms over investor protection objectives of securities regulation).

104. The Supreme Court reached that conclusion in 2011 in *Janus Capital Group*, 131 S. Ct. 2296. In doing so, it rejected the plaintiff's compelling contention that "an investment adviser should generally be understood to be the 'maker' of statements by its client mutual fund, like a playwright whose lines are delivered by an actor." Id. at 2304.

connection with their insolvencies or bankruptcies. Although a financial services firm may consist of a number of separate entities, those entities often operate cohesively, united in pursuing jointly shared business goals. Indeed, that fact should not be particularly surprising, given the typical structure of the financial services firm, in which one entity—the parent company—directly or indirectly owns and controls the other entities in an often complex parent-subsidiary structure.[105] The enterprise is able to act as a single firm because the various subsidiaries effectively have the status of assets of the parent company, subject to the parent company's use and manipulation.[106] That structure, moreover, is simply a product of corporate law principles. The parent company, as the subsidiaries' controlling shareholder, has the power to elect and replace the members of the subsidiaries' respective boards of directors and, in that capacity, may be said to control the boards and their decisions.[107] Therefore, the structure stands in contrast to a group of entities that, lacking common control or ownership, are able to act independently of one another.

However, as described more concretely in the case studies presented in Part II, the laws and rules governing financial services firms' insolvencies or bankruptcies evince problematic entity-centrism. For one thing, in the event the parent company, or even one of the subsidiary entities, becomes insolvent, it need not be the case that the other entities within the enterprise will meet a similar fate.[108] This is entity-centrism at

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105. See Williamson v. Cox Commc'ns, Inc., No. Civ.A. 1663-N, 2006 WL 1586375, at *4 (Del. Ch. June 5, 2006) ("The fact that an allegedly controlling shareholder appointed its affiliates to the board of directors is one of many factors Delaware courts have considered in analyzing whether a shareholder is controlling."); Gruenberg, supra note 64 (observing "corporate structure" of large financial firms with multiple lines of business that operate globally "is likely to be a holding company [structure] with a parent at the top and multiple layers of subsidiaries").

106. Cf. Gruenberg, supra note 64 (noting, in large financial holding company structures, "intra-company risk transfers and financial relationships will not be transparent"). Among other things, parent companies have been known to conduct their proprietary trading or other business activities through their subsidiaries or by using subsidiary assets. See, e.g., Disclosure Statement for the Plan of Liquidation for MF Global Holdings Ltd., MF Global Finance USA Inc., and Their Debtor Affiliates at 13–17, In re MF Global Holdings Ltd., 481 B.R. 268 (Bankr. S.D.N.Y. 2012) (No. 11-15059 (MG)) [hereinafter MF Global Plan Disclosure Statement], 2013 WL 485943, available at http://mfglobalcaseinfo.com/pdflib/995_15059.pdf (on file with the *Columbia Law Review*) (describing how MF Global's parent company used various subsidiaries to carry out firm's proprietary investment strategy).

107. See, e.g., Nina A. Mendelson, A Control-Based Approach to Shareholder Liability for Corporate Torts, 102 Colum. L. Rev. 1203, 1263 (2002) ("Controlling shareholders can ensure that their interests are fully represented on the subsidiary's board of directors, or by commonly employed officers, as well as that they have influence over both large and small corporate decisions, either directly, for some decisions, or through the board.").

108. Nonetheless, "[a] resolution of the individual subsidiaries of the financial company would increase the likelihood of disruption and loss of franchise value by

work, albeit in a largely benign manner: Given the adverse consequences of bankruptcy for creditors, it is difficult to quibble with any entity's survival, even in the midst of its affiliates' demise.

Beyond that, however, given the close ownership ties among the entities in the group, it is likely that the insolvency of one entity, particularly the parent company, will cause at least some others to follow suit.[109] The 2008 bankruptcy of Lehman Brothers, a large financial services conglomerate, is illustrative of that phenomenon.[110] In bankruptcy, moreover, the role of the parent company as the repository of, and authority over, the "assets" that are the subsidiaries is often replaced—rather jarringly—by bankruptcy trustees, administrators, liquidators, and, sometimes, receivers.[111] Whereas prior to bankruptcy each of the entities was, in some form or another, operated by the parent company for the furtherance (however defined) of the enterprise as a whole, in bankruptcy the connections between entities are broken and the affiliations severed.[112] The entities are taken over by independent parties whose objectives are to recover for "their" particular entity and corresponding

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disrupting the interrelationships among the subsidiary companies." Gruenberg, supra note 64.

109. See Standard & Poor's, RatingsDirect: Corporate Criteria—Parent/Subsidiary Links; General Principles; Subsidiaries/Joint Ventures/Nonrecourse Projects; Finance Subsidiaries; Rating Link to Parent 2–3 (2004), available at http://www.maalot.co.il/data/uploads/pdfs/1.Parent_Subsidiary.pdf (on file with the *Columbia Law Review*) (noting "'strong' subsidiary is no further from bankruptcy than its parent" and subsidiaries' credit ratings are generally no higher than that of parent company, in light of "likelihood that a parent's bankruptcy would cause the subsidiary's bankruptcy, regardless of its stand-alone strength").

110. See Yalman Onaran & Christopher Scinta, Lehman Files Biggest Bankruptcy Case as Suitors Balk (Update4), Bloomberg (Sept. 15, 2008, 9:43 AM), http://www.bloomberg.com/apps/news?pid=newsarchive&sid=awh5hRyXkvs4&refer=japan (on file with the *Columbia Law Review*) ("Lehman Brothers Holdings Inc., the fourth-largest U.S. investment bank, succumbed to the subprime mortgage crisis it helped create in the biggest bankruptcy filing in history.").

111. To be sure, the approach differs depending on whether the bankruptcy is filed under Chapter 11 or under Chapter 7 of the Bankruptcy Code. In particular, in Chapter 11 bankruptcies, it is not necessarily the case that a trustee will be appointed to replace the debtor's management. See 11 U.S.C. § 1104(a)(1)–(2) (2012) (allowing court to appoint trustee "for cause" or "if such appointment is in the interests of creditors, any equity security holders, and other interests of the estate"). Despite the Bankruptcy Code's more flexible approach in Chapter 11 bankruptcies, courts have appointed trustees in some Chapter 11 bankruptcies, including the bankruptcy of MF Global Holdings Ltd. See Ben Berkowitz, Former FBI Director Appointed MF Global Trustee, Reuters (Nov. 25, 2011, 9:13 PM), http://www.reuters.com/article/2011/11/26/us-mfglobal-trustee-idUSTRE7AP02Q20111126 (on file with the *Columbia Law Review*) (reporting appointment of trustee to oversee MF Global's bankruptcy).

112. See, e.g., Daniel P. Collins, MF Global Trustee Reports Show Folly of Bankruptcy Process, Futures (June 8, 2012), http://www.futuresmag.com/2012/06/08/mf-global-trustee-reports-show-folly-of-bankruptcy (on file with the *Columbia Law Review*) (observing trustees for different MF Global entities "are tossing around accusations against various entities that while a going concern, worked as one business with one leader").

group of creditors as much of the bankrupt entity's property as possible.[113] Even where an insolvent entity's directors remain in control, the directors must now carry out their duties for the benefit of those creditors.[114] As one might surmise, each of these professionals is likely to claim to have rights to the same limited property.[115]

At the point of insolvency, then, it becomes amply clear that entity-centrism is alive and well. The entities comprising the enterprise become the independent, self-contained legal beings that regulation has tended to assume they are. The fluid and cohesive, in other words, is supplanted by the ossified and (often) warring, all because the enterprise happened to be structured as a collection of separate entities rather than as a single, albeit complex, one.[116] Because of the hindsight that bankruptcy invites, if not requires, and the spotlight it shines on regulatory shortcomings, Part II pursues these considerations, discussing two recent financial services firm bankruptcies. The discussion shows, in concrete terms, how entity-centrism in financial services regulation, encompassing regulation that applies in both pre- and postbankruptcy contexts, is not merely an academic concern.

II. CASUALTIES OF ENTITY-CENTRISM

As Part I describes, financial services regulation is the regulation of financial services firms, not only over the span of their operations, but also during their liquidations. Financial services regulation, in other words, governs both the life and the death of the firm, and, indeed, some laws and rules that help define the firm's activities also govern its cessation of them. The preceding Part highlights a few of the ways in

113. See Bankr. Judges Div., Admin. Office of the U.S. Courts, Bankruptcy Basics 76 (rev. 3d ed. 2011), available at http://www.uscourts.gov/uscourts/FederalCourts/BankruptcyResources/bankbasics2011.pdf (on file with the *Columbia Law Review*) (noting bankruptcy trustee has responsibility to act "principally for the benefit of the unsecured creditors" and to "recover property" of estate).

114. See A. Mechele Dickerson, A Behavioral Approach to Analyzing Corporate Failures, 38 Wake Forest L. Rev. 1, 15 n.50 (2003) ("Directors of insolvent firms are deemed to have fiduciary duties to creditors because shareholders' residual interests in an insolvent firm are worthless and cannot be paid until creditors' claims are paid in full.").

115. See Daniel P. Collins, MF Global Trustees Square Off, Futures (May 1, 2012), http://www.futuresmag.com/2012/05/01/mf-global-trustees-square-off (on file with the *Columbia Law Review*) ("As the MF Global debacle has dragged on, [it] has become apparent . . . that the two trustees are on a collision course as they battle for what's left of the bankrupt firm.").

116. In the apt words of an official of the U.K. Financial Services Authority, discussing the bankruptcy of Lehman Brothers, "[F]inancial institutions may be global in life, but they are national in death—they become a series of local legal entities when they become subject to administration and/or liquidation." Thomas Huertas, Dir., Banking Sector, Fin. Servs. Auth., The Rationale for and Limits of Bank Supervision (Jan. 19, 2009), available at http://www.fsa.gov.uk/library/communication/speeches/2009/0119_th.shtml (on file with the *Columbia Law Review*).

which laws and rules governing financial services firms are entity-centric. Firms are regulated through particular entities, with each entity that performs particular services registering with the appropriate authority and complying with the associated obligations separately from any other entity. Applicable doctrine affords client protections to hedge funds and other private funds, rather than to their investors, even though the entity that is the fund, created and controlled by its investment adviser, is but a mechanism to aggregate would-be clients.[117] Regulation of mutual funds and other public funds centers on the entity that is the fund, even though something beyond the fund—namely, its investment adviser—is responsible for what the fund is and does.[118] In bankruptcy and liquidation, law treats a financial services firm as a compilation of discrete and independent entities, even though, prior to bankruptcy, those entities operated as a cohesive unit.[119]

This Part focuses on two recent bankruptcies that reveal not only the significant shortcomings of financial services regulation, but also that those shortcomings are the product of regulation's entity-centered formulation. Their facts are particularly interesting and, more importantly, show entity-centrism's pathologies in a particularly stark manner. Each firm's demise occurred under circumstances very different from those of the other's. Although Lehman Brothers and Bernard Madoff may readily come to mind (and although both likewise evince problematic entity-centrism), the firms discussed in this Part have received far less attention, as have the regulatory failures they have made apparent. Moreover, each firm's collapse occurred after the financial crisis had mostly run its course. The firms are MF Global and the group of companies owned by R. Allen Stanford. These two episodes, discussed in Part II.A and II.B, respectively, are instructive not because the laws and rules governing bankruptcies in the financial services context are any more entity-centric or problematic than the laws and rules governing financial services firms' day-to-day activities. Indeed, some of the most troublesome aspects of these episodes and, in particular, the rules and norms governing them do not involve the Bankruptcy Code. Rather, the case studies are instructive for the simple reason that financial services catastrophes are litmus tests for the efficacy of financial services regulation. We might think of such events as the ultraviolet lights that illuminate how failures of financial services regulation may be traced to entity-centrism.

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117. See supra notes 67–82 and accompanying text (discussing investment adviser regulation as example of entity-centrism).

118. See supra Part I.B.2 (highlighting how mutual fund regulation inappropriately centers on entity that is fund and fails to acknowledge multi-entity structures).

119. See supra Part I.B.3 (describing bankruptcy doctrine's entity-centric assumptions).

A. *MF Global*

1. *The Enterprise Structure*. — MF Global was a broker-dealer registered with the SEC under the Exchange Act and a futures commission merchant registered with the CFTC under the Commodity Exchange Act. In one form or another, it had been around for almost 230 years, originating in 1783 England as James Man's sugar trading business.[120] The firm, which became known as E.D.&F. Man in 1869,[121] ultimately became an asset management firm named Man Group PLC, pursuing its global brokerage business under the name Man Financial.[122] In 2007, Man Group spun off Man Financial, in the process changing the latter's name to MF Global.[123] Soon thereafter, MF Global commenced an initial public offering.[124] Jon Corzine became MF Global's CEO in March 2010 and resigned from that position nineteen months later, on November 4, 2011, four days after the firm filed for bankruptcy.[125]

Referring to MF Global as an "it," however, is a bit misleading because the firm was a multi-entity, multinational enterprise, consisting of at least fifty separate entities.[126] The MF Global entity that went bank-

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120. Staff Report Prepared for Rep. Randy Neugebauer, Chairman, Subcommittee on Oversight & Investigations, Committee on Financial Services 5 (2012) [hereinafter Staff Report], available at http://financialservices.house.gov/uploadedfiles/256882456288524.pdf (on file with the *Columbia Law Review*) ("MF Global traces its origin back 229 years to a sugar brokerage business founded by James Man in London in 1783."); Jill Treanor, MF Group's Trading Roots Stretch Back Two Centuries, Guardian (Oct. 31, 2012, 10:32 AM), http://www.guardian.co.uk/business/2011/oct/31/mf-global-trading-history (on file with the *Columbia Law Review*) (noting "MF Global group can still trace its roots back to" James Man's sugar brokerage business).

121. See Staff Report, supra note 120, at 5 ("In 1869, the business became known as E.D.&F. Man.").

122. See id. (observing E.D.&F. Man "had $1 billion in funds under management" by 1994 and Man Financial had been "Man Group's global brokerage business[]").

123. See Jacob Bunge, MF Global: History from IPO to Bankruptcy, Wall St. J.: Deal J. (Oct. 31, 2011, 11:33 AM), http://blogs.wsj.com/deals/2011/10/31/mf-global-history-from-ipo-to-bankruptcy/ (on file with the *Columbia Law Review*) (noting MF Global began in 2007 "as a spinoff of U.K. hedge-fund firm Man Financial").

124. See Staff Report, supra note 120, at 7 ("On July 18, 2007, MF Global announced an initial public offering . . . .").

125. See Aaron Lucchetti & Mike Spector, The Unraveling of MF Global, Wall St. J. (Dec. 31, 2011) [hereinafter Lucchetti & Spector, Unraveling of MF Global], http://online.wsj.com/article/SB10001424052970203686204577117114075444418.html (on file with the *Columbia Law Review*) (noting "Mr. Corzine's tenure began in March 2010"); Ben Protess & Kevin Roose, Corzine Resigns from MF Global, N.Y. Times: Dealbook (Nov. 4, 2011, 7:50 AM), http://dealbook.nytimes.com/2011/11/04/corzine-resigns-from-mf-global/ (on file with the *Columbia Law Review*) (reporting Jon Corzine's resignation).

126. See Motion Pursuant to Federal Rule of Bankruptcy Procedure 9019 for Entry of Order Approving Settlement Agreement Between the Debtor, the Trustee, MF Global UK Ltd. (in Special Administration) and MFGUK Joint Special Administrators at 4, In re MF Global Inc., 481 B.R. 268 (Bankr. S.D.N.Y. 2012) (No. 11-2790 (MG) SIPA), available at http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/mfgimfguksette

rupt and that "caused" the bankruptcies of most of the other entities was the parent company, MF Global Holdings Ltd. ("Holdings").[127] The ultimate cause of the bankruptcy—a fascinating topic but of lesser importance for present purposes—was its CEO's inappropriate trading and investment activities on the firm's behalf.[128] Mr. Corzine had made an enormous bet on European sovereign debt, one that relied on leverage such that, when European countries' credit ratings were substantially downgraded in the fall of 2011, MF Global's lenders (or, more accurately, its "repo" counterparties[129]) sought additional collateral that the firm was unable to supply.[130] The drain on assets caused by the default risk associated with European debt and by MF Global's own credit-rating downgrade—combined with the termination of negotiations

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ment122112.pdf (on file with the *Columbia Law Review*) ("MFG Holdings . . . was the parent of nearly fifty direct or indirect subsidiaries . . . ."). The large number of entities comprising "MF Global" is evident from its organizational chart. See MF Global Plan Disclosure Statement, supra note 106, at 90 (graphically depicting MF Global's organizational structure).

127. Michael J. de la Merced & Ben Protess, MF Global Files for Bankruptcy, N.Y. Times: Dealbook (Oct. 31, 2011, 10:21 AM), http://dealbook.nytimes.com/2011/10/31/mf-global-files-for-bankruptcy/?ref=mfgloballtd (on file with the *Columbia Law Review*) (reporting Holdings's bankruptcy filing).

128. See Complaint at 56–57, Freeh v. Corzine (In re MF Global Holdings Ltd.), No. 11-15059 (MG) (Bankr. S.D.N.Y. filed Apr. 22, 2013) [hereinafter Holdings Complaint], 2013 WL 2472173 (contending Jon Corzine and other Holdings officers breached fiduciary duty of care based on, among other things, trading strategies they pursued on Holdings's behalf); Report of Investigation of Louis J. Freeh, Chapter 11 Trustee of MF Global Holdings Ltd., et al. at 97, In re MF Global Holdings Ltd., No. 11-15059 (MG) (Bankr. S.D.N.Y. filed Apr. 4, 2013) [hereinafter Report of Investigation of Louis J. Freeh], available at http://www.mfglobalcaseinfo.com/pdflib/1279_15059.pdf (on file with the *Columbia Law Review*) ("Corzine's bet on the Euro RTMs exposed [MF Global] to an excessive level of risk.").

129. "Repos"—short for "repurchase agreements"—are financial instruments that constitute "a method of short-term borrowing." Alan N. Rechtschaffen, Capital Markets, Derivatives and the Law 149–50 (2009). In particular, "repos" involve the "borrower's" sale of securities to the "lender," with the sale price constituting the loan. See id. (comparing security sales in repos to use of collateral in loans). The borrower subsequently repurchases the securities from the lender at a price that includes an extra amount equivalent to interest. See What Is a Repo?, Int'l Capital Mkt. Ass'n, http://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/short-term-markets/Repo-Markets/frequently-asked-questions-on-repo/1-what-is-a-repo/ (on file with the *Columbia Law Review*) (last visited Oct. 7, 2013) ("The difference between the price paid by the buyer at the start of a repo and the price he receives at the end is his return on the cash that he is effectively lending to the seller."). From an economic perspective, repos function like secured loans, in that the securities serve as collateral. Rechtschaffen, supra, at 150.

130. See Matthew Leising, MF Global's $310 Million Margin Call on Last Day Exceeded Its Market Value, Bloomberg (Feb. 6, 2012, 7:36 PM), http://www.bloomberg.com/news/2012-02-06/mf-global-faced-a-310-million-margin-call-on-futures-broker-s-final-day.html (on file with the *Columbia Law Review*) (describing MF Global's liquidity crisis in its final days).

with the firm's only plausible buyer[131]—left bankruptcy as MF Global's only option.[132]

In life, MF Global operated as securities and futures brokerage firms typically do these days. The parent company, Holdings, did not itself provide brokerage or other financial services to customers.[133] Accordingly, it was neither registered with nor regulated by any financial regulatory authority in any capacity.[134] It did, however, pursue business activities of a sort, namely, proprietary trading activities, in which it traded and invested in securities (and possibly other instruments) for its own account.[135] Although Holdings could potentially have carried out these

131. The prospective buyer, Interactive Brokers LLC, was primarily interested in buying MF Global Inc. (the U.S. brokerage subsidiary) or substantially all of that entity's assets. See John L. Roe & James L. Koutoulas, Commodity Customer Coal., White Paper: Background, Impacts & Solutions to MF Global's Bankruptcy 7 (2012), available at http://commoditycustomercoalition.org/wp-content/uploads/2012/05/CCC-White-Paper-MF-Global-Bankruptcy-Revised-5-9-121.pdf (on file with the *Columbia Law Review*) ("The MFGH parent firm sought Chapter 11 bankruptcy protection on October 31, 2011 after an acquisition of MFGI's commodities accounts by rival firm Interactive Brokers fell through."); cf. Ben Protess et al., Regulators Investigating MF Global for Missing Money, N.Y. Times: Dealbook (Oct. 31, 2011, 9:55 PM), http://dealbook. nytimes.com/2011/10/31/regulators-investigating-mf-global/ (on file with the *Columbia Law Review*) ("[Interactive Brokers] coveted only MF Global's futures and securities customers."). "When MF Global informed Interactive Brokers of the shortfall of customer funds, the company withdrew from negotiations." Staff Report, supra note 120, at 73.

132. See Staff Report, supra note 120, at 54–73 (describing MF Global's collapse and observing "MF Global faced a liquidity drain of crisis proportions"); see also Report of Investigation of Louis J. Freeh, supra note 128, at 103–04 (describing margin calls MF Global received immediately prior to bankruptcy); Lucchetti & Spector, Unraveling of MF Global, supra note 125 (summarizing events leading to MF Global's bankruptcy); Kevin McCoy, Bankrupt Brokerage MF Global Showed Appetite for Risk, USA Today (Nov. 9, 2011, 8:25 PM), http://usatoday.com/money/industries/brokerage/story/2011-11-10/mf-global-warningsigns/51145024/1 (on file with the *Columbia Law Review*) ("MF Global filed for bankruptcy court protection on Oct. 31 when efforts to find a buyer for the company broke down amid signs that an estimated $600 million in customer funds could not be accounted for.").

133. Cf. The Collapse of MF Global: Lessons Learned and Policy Implications: Hearing Before the S. Comm. on Banking, Hous. & Urban Affairs, 112th Cong. 50 (2012) (statement of Robert Cook, Director, Division of Trading and Markets, U.S. Securities and Exchange Commission) [hereinafter Cook Testimony] ("MF Global Holdings Ltd. . . . was a publicly traded holding company that conducted financial activities through a number of subsidiaries located in various countries.").

134. Cf. id. (describing various regulatory regimes to which subsidiaries, as entities providing financial services, were subject).

135. See Staff Report, supra note 120, at 30 (describing how, under Corzine's leadership, MF Global increasingly "looked to proprietary trading . . . as a way to further boost revenues"); Editorial, MF Global Meltdown Shows the Wisdom of Prop-Trading Limits: View, Bloomberg (Oct. 31, 2011, 7:05 PM), http://www.bloomberg.com/news/2011-10-31/mf-global-meltdown-shows-the-wisdom-of-prop-trading-limits-view.html (on file with the *Columbia Law Review*) (recounting how, upon his arrival at MF Global, "Corzine pumped up the firm's proprietary trading desk, using its small base of capital to buy European sovereign debt").

activities directly, in a manner that did not involve any of its subsidiaries, it instead conducted them largely through several of its subsidiaries or units or divisions of those subsidiaries.[136] Holdings's European sovereign debt investments were at the core of the firm's trading strategy, which, as Mr. Corzine originally conceived it, would not cause the firm to bear any risk.[137] For their part, the MF Global subsidiaries were the entities that actually provided financial services and were regulated as such, depending on what any particular subsidiary did and the jurisdiction in which it was located.[138]

The firm maintained operations in the United Kingdom, Canada, Australia, and Singapore, in addition to the United States. In the United States, MF Global Inc. was the entity performing brokerage services, whereas, in the U.K., it was MF Global UK Ltd.; in Singapore, it was MF Global Singapore Pte. Ltd.; and so on.[139] Brokerage customers "signed

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136. See Staff Report, supra note 120, at 35 (describing how, in furtherance of MF Global's proprietary trading strategy, MF Global UK bought European bonds, which it then sold to MF Global Inc., which used bonds "as collateral in intercompany [repo-to-maturity (RTM)] transactions with MFGUK [which] . . . then entered into further RTM transactions"); Report of Investigation of Louis J. Freeh, supra note 128, at 26–27 ("MFG UK entered into the trades because it, and not MFGI, was a member of the relevant clearinghouses . . . .").

137. See Staff Report, supra note 120, at 35 (noting Corzine's belief that his trading strategy "could book instant profits for MF Global without affecting its balance sheet"); John Carney, The Trade That Killed MF Global, CNBC (Nov. 2, 2011, 12:02 PM), http://www.cnbc.com/id/45132384/The_Trade_That_Killed_MF_Global (on file with the *Columbia Law Review*) (observing MF Global had been pursuing "what it viewed as a nearly risk-free trade, hoping to make money in a very old fashioned way—skimming the spread as a middle man"). This strategy is known as repo-to-maturity. See Staff Report, supra note 120, at 31–36 (discussing mechanics of repo-to-maturity agreement). The notion was that the loans—or, more precisely, repurchase agreements, see supra note 129 (explaining repurchase agreements)—that MF Global obtained to purchase bonds on European sovereign debt generally had the same maturity as the bonds themselves. See Report of Investigation of Louis J. Freeh, supra note 128, at 27 ("The maturity of the securities underlying the Euro RTMs matched the maturity of the financing provided under MFG UK's repos . . . with one difference."). Assuming, as Mr. Corzine mistakenly did, that the bonds would retain their value until maturity, then, by using the bonds as collateral for the loans (or, more precisely, by selling them to the lenders on the condition that MF Global would repurchase them at maturity) the strategy presented no risk to MF Global. See Staff Report, supra note 120, at 31–36 (describing proprietary trading strategy Corzine implemented on behalf of MF Global). At the end of the bonds' term, MF Global would have earned the interest on those bonds, which was marginally higher than the interest MF Global was obligated to pay for the loans (or, more precisely, the difference between the price at which the lenders purchased the bonds and the price at which MF Global was obligated to repurchase them). See id. (indicating key technical assumptions of Corzine's trading strategy).

138. See Cook Testimony, supra note 133, at 1–2 (summarizing regulation to which certain subsidiaries were subject); Staff Report, supra note 120, at 21–22 (observing MF Global had "six regulated subsidiaries, five of which were located outside of the United States").

139. See Staff Report, supra note 120, at 22 (listing regulated subsidiaries and regulatory regime to which each was subject); see also ICE Clear Eur., MF Global Client

up" with whatever subsidiary was appropriate in light of their brokerage needs and geographic location. Nonetheless, with Holdings and, more specifically, Mr. Corzine at the helm, the various entities were operated as a single enterprise. Decisionmaking was centralized in Holdings, and each subsidiary's assets and resources were deployed in furtherance of enterprise objectives—again, typical of other large financial services firms.[140] In light of Holdings's control relationship (whether direct or indirect) over each of the subsidiaries, Mr. Corzine and other officers formally employed by that entity could cause the movement of assets among the entities for various purposes.[141] That they did so, moreover, need not have given rise to any regulatory or corporate governance concerns.[142] Indeed, so long as the regulated entities complied with their obligations and the subsidiaries maintained (and Holdings respected) corporate formalities, the entities' working together as a single unit may have been both efficient and productive.

2. *The Plunge into Bankruptcy.* — Until the music stopped. By September 2011, it had become apparent to reasonably close observers that Holdings was in precarious financial health as a result of the worsening European debt crisis and the circumstance that MF Global held substantial "long" positions in that continent's sovereign debt.[143] As the firm's financial condition continued to deteriorate through October 2011, its lenders sought to protect themselves by demanding additional collateral, while those MF Global shareholders and bondholders who were aware of the firm's plight similarly sought to abandon their

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Information Update 1 (2011), available at https://www.theice.com/publicdocs/clear_europe/circulars/C11181.pdf (on file with the *Columbia Law Review*) ("MF Global conducted its business through a number of subsidiaries worldwide, including MF Global Inc., MF Global UK Ltd, MF Global Singapore Pte. Limited, MF Global Hong Kong Ltd, MF Global Australia Limited and MF Global Canada Co.").

140. See Cook Testimony, supra note 133, at 50–52 (noting Holdings conducted its activities through number of subsidiaries); Elaine Knuth, MF Global's Original Sin, Futures (Nov. 1, 2012), http://www.futuresmag.com/2012/11/01/mf-globals-original-sin (on file with the *Columbia Law Review*) (noting various MF Global entities "operated as one entity").

141. See, e.g., Staff Report, supra note 120, at 57, 64 (describing how Holdings needed to "inject" capital into MF Global Inc. and transferred funds from MF Global Inc. to MF Global UK); Holdings Complaint, supra note 128, at 25 ("Corzine caused MFGI to enter into the Euro RTM trades.").

142. Although the congressional report on MF Global flags numerous regulatory concerns, the apparently commonplace transfer of funds among the various MF Global entities was not among those concerns. See Staff Report, supra note 120, at 50–72 (listing regulatory concerns prior to MF Global's bankruptcy but not referencing funds transfers).

143. See Staff Report, supra note 120, at 46 (noting Holdings disclosed in its May 2011 10-K report that "its net position in European RTM trades was $6.3 billion"); Azam Ahmed & Ben Protess, To Avoid Raising Capital, MF Global Moved Around Sovereign Debt, N.Y. Times: Dealbook (June 5, 2012, 10:45 AM), http://dealbook.nytimes.com/2012/06/05/to-avoid-regulatory-scrutiny-mf-global-moved-around-sovereign-debt (on file with the *Columbia Law Review*) (discussing MF Global's "$6 billion bet on European sovereign debt").

positions.[144] The firm's regulators, including the CFTC and the firm's "designated self-regulatory organization,"[145] the Commodity Mercantile Exchange Group (CME), stepped onto the scene, quite literally.[146] Each established a "physical presence" in the firm's Chicago office, meaning one of the offices of MF Global Inc., the U.S. brokerage subsidiary.[147]

Regulators' primary role at such times of stress is to monitor the firm's continued compliance with its regulatory obligations.[148] For MF Global, perhaps the most important regulatory requirement was ensuring the integrity of the funds and assets that brokerage customers had placed in custody with the firm for purposes of their futures trading activities.[149] An additional aim for regulators was to work with MF Global's management to secure a buyer for the firm, with the hopes of effecting a seam-

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144. See Staff Report, supra note 120, at 59 (describing how in MF Global's final days, lenders, customers, and shareholders sought to cut ties with firm); Peter Elkind with Doris Burke, The Last Days of MF Global, CNNMoney (June 4, 2012, 3:17 PM), http://finance.fortune.cnn.com/2012/06/04/the-last-days-of-mf-global/ (on file with the *Columbia Law Review*) (observing by close of trading on October 25, 2011, "MF Global shares had dropped 48%, to $1.86"; "[c]ustomers were demanding their money and closing accounts; [and] counterparties and lenders were cutting off credit").

145. Staff Report, supra note 120, at 23 (internal quotation marks omitted).

146. See Bryan Durkin, Chief Operating Officer, Commodity Mercantile Exch. Grp., Address Before the National Grain and Feed Association 40th Annual Country Elevator Conference (Dec. 12, 2011), *in* Jackie Roembke, CME Group Discusses MF Global Bankruptcy, Feed & Grain (Dec. 14, 2011), http://www.feedandgrain.com/article/10525740/cme-group-discusses-mf-global-bankruptcy (on file with the *Columbia Law Review*) (detailing CME's presence in MF Global's offices at end of October 2011); Elkind with Burke, supra note 144 (noting CFTC personnel had been "on the ground" at MF Global before bankruptcy).

147. See Staff Report, supra note 120, at 69 (referring to "CFTC staff in MF Global's Chicago office"); Durkin, supra note 146 (noting CME auditors were in "MF Global's Chicago offices" on October 27 and 28, 2011).

148. Cf. Staff Report, supra note 120, at 61 (observing in MF Global's final week "[t]he SEC advised [MF Global Inc.] that it wanted to meet with the company's managers . . . to discuss liquidity, funding, financial statement condition, and regulatory computations, and that the CFTC would also participate"); Durkin, supra note 146 (describing CME's focus on MF Global's regulatory compliance as latter became insolvent).

149. See Staff Report, supra note 120, at 67–70 (describing regulators' efforts in MF Global's final days to verify customer account balances); Elkind with Burke, supra note 144 ("[MF Global's] primary business was handling trades that allowed hedging and speculation in such things as pork bellies, metals, and foreign currencies."). Some of MF Global's customers pursued trading and investments in securities. However, out of the customer accounts at MF Global Inc. at the time it declared bankruptcy, about 36,000 were held by futures customers, whereas fewer than 350 were held by securities customers. See Staff Report, supra note 120, at 1 ("At the time of MF Global's bankruptcy, the company served approximately 36,000 futures customers and 318 securities customers."); Linda Sandler, MF Global Judge Tells Trustee to Disclose More JPMorgan Work, Bloomberg Businessweek (Dec. 7, 2011), http://www.businessweek.com/news/2011-12-07/mf-global-judge-tells-trustee-to-disclose-more-jpmorgan-work.html (on file with the *Columbia Law Review*) (noting transfer of "about 38,000 commodity accounts to other firms" and "plans to sell 330 securities accounts").

less continuation of the firm's brokerage operations.[150] Although MF Global initially believed that it had found a willing buyer in Interactive Brokers, an online brokerage firm,[151] the desired deal did not materialize,[152] leading Holdings to file for bankruptcy, with proceedings carried out under Chapter 11 of the Bankruptcy Code.[153]

As for MF Global Inc., the SEC, after discussions with CFTC representatives, placed the entity into a liquidation proceeding under the Securities Investor Protection Act (SIPA),[154] a statute enacted in 1970 to protect securities brokerage customers in the event of a broker-dealer's insolvency.[155] It quickly became apparent that the deal with Interactive Brokers had failed and that bankruptcy was the only remaining option because MF Global had discovered a very large discrepancy between the amount of funds the firm—in particular, MF Global Inc.—should have held in its custodial accounts for brokerage customers and the amount of funds that it actually held in those accounts.[156] There was, in other words, a substantial "shortfall."[157] The trustee that the bankruptcy court appointed to liquidate MF Global Inc. ultimately determined that the shortfall, originally estimated to be approximately $900 million, was instead approximately $1.6 billion.[158]

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150. See Mike Spector, Aaron Lucchetti & Liam Plevin, Corzine Firm's Final Struggles, Wall St. J. (Nov. 5, 2011), http://online.wsj.com/article/SB10001424052970203716204577018113636278598.html (on file with the *Columbia Law Review*) (observing in MF Global's final days "regulators were worried about the run on the firm and hoped a rescuer would swoop in").

151. Staff Report, supra note 120, at 67 ("Corzine had identified Interactive Brokers, LLC as a potential buyer, and executives for both companies worked through the weekend to negotiate the terms of a deal.").

152. See de la Merced & Protess, supra note 127 (reporting Interactive Brokers's concerns about MF Global's "capital levels" led prospective buyer "to call off the deal").

153. See Staff Report, supra note 120, at 73 ("MF Global filed for reorganization under Chapter 11 of the Bankruptcy Code . . . .").

154. See id. ("[T]he Securities Investor Protection Corporation commenced a proceeding to liquidate [MF Global Inc.] under [SIPA]."); Mike Spector & Aaron Lucchetti, SIPC Expected to Name Trustee for MF Global Brokerage, Wall St. J. (Oct. 31, 2011, 4:45 PM) [hereinafter Spector & Lucchetti, SIPC Expected to Name Trustee], http://online.wsj.com/article/SB10001424052970204528204577010240782392380.html#articleTabs%3Darticle (on file with the *Columbia Law Review*) ("[SIPC] is poised to appoint a trustee to take over MF Global Holdings Ltd.'s brokerage . . . .").

155. 15 U.S.C. §§ 78aaa–78*lll* (2012).

156. See Holdings Complaint, supra note 128, at 56 ("On October 30, 2011, . . . a sale to a third party collapsed when [MF Global] informed the would-be buyer that it had identified a potential significant shortfall in customer segregated funds.").

157. Staff Report, supra note 120, at 1.

158. See id. ("[I]t is now known that MF Global's collapse resulted in a $1.6 billion shortfall in customer funds."); Ben Protess, MF Global Trustee Sees $1.6 Billion Customer Shortfall, N.Y. Times: Dealbook (Feb. 10, 2012, 8:01 PM), http://dealbook.nytimes.com/2012/02/10/mf-global-trustee-sees-1-6-billion-customer-shortfall/ (on file with the *Columbia Law Review*) (reporting $1.6 billion as revised estimate of shortfall amount).

3. *Entity-Based Battles for Assets.* — Consistent with the discussion in Part I.B, in MF Global's death, the operation of MF Global as a multipart enterprise was supplanted, all too abruptly, by an entity-centric entrenchment and conflict among the MF Global subsidiaries.[159] Once in the throes of bankruptcy, each MF Global entity was treated as a separate unit, independent of the other entities within the MF Global enterprise.[160] Put another way, at the time the entity came to owe its corporate governance obligations to its creditors, rather than to its equity owners—a natural consequence of being in bankruptcy[161]—regarding the enterprise and its myriad entity components as a cohesive whole became impossible, almost by definition. After all, the functioning of entities as part of a larger business depended on common ownership of, or some other ownership-based affiliation among, those entities. For MF Global, recall, Holdings owned each other MF Global entity, whether directly or through another MF Global entity.[162] However, ownership is almost irrelevant in bankruptcy, a status of drained equity and a resulting governance focus on creditors.[163] More precisely, because an entity's equity owners (shareholders or partners, for example) have lowest priority in bankruptcy payouts, the trustees or directors controlling a bankrupt entity are generally obliged to further the interests—and abide by the wishes—of the entity's creditors, as the top-priority constituency.[164] Accordingly, after Holdings ceased to be a component of each entity's governance structure, the connections among the affiliated entities could be expected to dissipate.

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159. See supra Part I.B.3 (describing how, in bankruptcy, entities in multi-entity enterprises pursue entity-based interests, often in opposition to affiliate entities' interests).

160. See Nick Brown, MF Global Trustees Resolve Fight over $130 Mln CME Settlement, Chi. Trib. (July 27, 2012), http://articles.chicagotribune.com/2012-07-27/news/sns-rt-mfglobal-cmel2e8irb2y-20120727_1_mf-global-customers-james-giddens-shortfall-in-customer-accounts (on file with the *Columbia Law Review*) ("With both sides facing shortfalls, the trustees are liable to butt heads over entitlement to various pots of money . . . ."); Ben Protess, Freeh Calls for Peace in Fight over MF Global Money, N.Y. Times: Dealbook (Aug. 29, 2012, 7:18 PM), http://dealbook.nytimes.com/2012/08/29/freeh-calls-for-peace-in-fight-over-mf-global-money/ (on file with the *Columbia Law Review*) (describing how trustees of various MF Global entities "spent months feuding" in efforts to collect funds to pay entities' respective creditors and customers).

161. See supra notes 109–115 and accompanying text (describing how entity's bankruptcy modifies obligations owed by entity's management).

162. See supra notes 126–127 and accompanying text (describing MF Global's organizational structure).

163. See supra notes 112–114 and accompanying text (explaining bankrupt entity's management has obligations to entity's creditors).

164. See Kenneth M. Ayotte & Edward R. Morrison, Creditor Control and Conflict in Chapter 11, 1 J. Legal Analysis 511, 538 (2009) (finding, based on empirical analyses, "among large privately and publicly held businesses, creditor control is pervasive" and "[e]quity holders and managers exercise little or no leverage during the reorganization process").

In theory, at least, under the current bankruptcy legal regime, a bankruptcy of related entities could involve a consolidation in which, for purposes of the bankruptcy liquidation proceedings, the entities are regarded as one, with their assets and liabilities regarded as the assets and liabilities of a single debtor.[165] "Substantive consolidation," as the equitable doctrine is formally called,[166] may be appropriate when, for example, a creditor has been duped into extending credit, which might be the case if the debtor led the creditor to believe that the debtor owned assets that were, in fact, owned by the debtor's affiliates.[167] It has also been used in circumstances in which the debtor's and its affiliates' assets are intertwined to the extent that attempting to sort them out would injure all creditors.[168] However, courts have traditionally viewed substantive consolidation as an extraordinary remedy.[169] Beyond that, it is not a strong prospect in bankruptcies of financial services firms because of the differing bankruptcy regulatory regimes to which different entities are necessarily subject. As an initial matter, a subsidiary based in a foreign jurisdiction will be liquidated in accordance with the laws and

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165. See J. Stephen Gilbert, Note, Substantive Consolidation in Bankruptcy: A Primer, 43 Vand. L. Rev. 207, 208 (1990) ("Substantive consolidation is a powerful vehicle in bankruptcy by which the assets and liabilities of one or more entities are combined and treated for bankruptcy purposes as belonging to a single enterprise."); see also Timothy E. Graulich, Substantive Consolidation—A Post-Modern Trend, 14 Am. Bankr. Inst. L. Rev. 527, 527 (2006) ("Essentially, for purposes of distribution in bankruptcy, substantive consolidation treats multiple entities as if they were one."); Peter J. Lahny IV, Asset Securitization: A Discussion of the Traditional Bankruptcy Attacks and an Analysis of the Next Potential Attack, Substantive Consolidation, 9 Am. Bankr. Inst. L. Rev. 815, 859 (2001) (observing upon substantive consolidation "court treats the assets and liabilities of at least two separate, but affiliated entities as if they were the assets and liabilities of a single bankruptcy debtor"). The Bankruptcy Code does not expressly contemplate substantive consolidation. Rather, courts have crafted the doctrine from the power conferred under § 105(a) of the Code, which authorizes courts to "issue any order, process, or judgment that is necessary or appropriate to carry out" the Code's provisions. 11 U.S.C. § 105(a) (2012).

166. See Gilbert, supra note 165, at 208 (characterizing substantive consolidation as "equitable remedy").

167. See Graulich, supra note 165, at 539–42 (summarizing cases in which courts have required substantive consolidation to address debtors' fraudulent or misleading conduct vis-à-vis creditors).

168. See id. at 543–44 (describing use of substantive consolidation in circumstances where debtors are "*unable* to 'unscramble' their assets and liabilities (at least without depleting the estate in the process and thereby reducing or eliminating creditor recoveries)"). However, there is no uniform test courts apply to determine whether substantive consolidation is appropriate for any particular bankruptcy. See In re Bonham, 229 F.3d 750, 765 (9th Cir. 2000) (observing "[n]o uniform guideline for determining when to order substantive consolidation has emerged" and "only through a searching review of the record, on a case-by-case basis, can a court ensure that substantive consolidation effects its sole aim: fairness to all creditors" (quoting FDIC v. Colonial Realty Co., 966 F.2d 57, 61 (2d Cir. 1992)) (internal quotation marks omitted)).

169. See Graulich, supra note 165, at 528 n.8 (listing cases articulating that substantive consolidation should be invoked sparingly).

rules of that jurisdiction.[170] More importantly, even for entities based in the same country, such as Holdings and MF Global Inc., the entity or entities that are regulated securities brokerages generally must be liquidated in accordance with SIPA, whereas the entities that are not so regulated will be wound up under Chapter 7 or Chapter 11 of the Bankruptcy Code.[171] At the very least, then, under current U.S. laws and rules, substantive consolidation cannot be counted on to stave off the entity-based liquidation of the enterprise.[172]

Accordingly, in the case of MF Global, the court appointed a trustee or administrator for each insolvent entity, and, for the most part, each entity claimed, through its trustee or administrator, that one or more other MF Global entities owed it money.[173] The irony of that circumstance becomes evident when one considers the fate of the customer funds that went missing from MF Global Inc.'s custodial accounts. As expected, MF Global Inc.'s trustee determined that Holdings had used a considerable portion of the missing funds to meet its lenders' demands for additional collateral.[174] Or, more precisely, he determined that Holdings's and MF Global Inc.'s *management* caused the customer funds to be used to meet the former entity's funding needs.[175] That use, even if unlawful, was possible by virtue of the entities' affiliations and functioning as an operationally coordinated enterprise.

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170. See, e.g., First Report of Louis J. Freeh, Chapter 11 Trustee of MF Global Holdings Ltd., et al., for the Period October 31, 2011 Through June 4, 2012, at 53–72, In re MF Global Holdings Ltd., No. 11-15059 (MG) (Bankr. S.D.N.Y. filed June 4, 2012), 2012 WL 2002765, available at http://mfglobalcaseinfo.com/pdflib/711_15059.pdf (on file with the *Columbia Law Review*) (summarizing liquidation status of various non-U.S. MF Global entities); cf. Staff Report, supra note 120, at 95–96 (observing "disposition of funds" held by MF Global UK "was subject to British law when MFGUK entered into administration following the collapse of its U.S. affiliates and parent").

171. Although a SIPA proceeding is a form of Chapter 7 proceeding, it nonetheless is a substantively different type of proceeding and, therefore, is not a candidate for consolidation with a "plain vanilla" Chapter 7 proceeding.

172. Cf. Ryan W. Johnson, The Preservation of Substantive Consolidation, Am. Bankr. Inst. J., July–Aug. 2005, at 44, 44 & n.9 (distinguishing substantive consolidation of Chapter 7 cases from substantive consolidation of Chapter 11 cases).

173. See Trustee's Second Six Month Interim Report for the Period June 5, 2012 Through December 4, 2012, at 14–18, In re MF Global Inc., No. 11-2790 (MG) SIPA (Bankr. S.D.N.Y. filed Dec. 4, 2012), available at http://dm.epiq11.com/MFG/document/GetDocument.aspx?DocumentId=2176933 (on file with the *Columbia Law Review*) (describing claims made by various MF Global entities against one another).

174. See Jason M. Breslow, MF Global Trustee Hints at Negligence Suit Against Jon Corzine, PBS Frontline (June 4, 2012, 2:00 PM), http://www.pbs.org/wgbh/pages/frontline/business-economy-financial-crisis/mf-global-six-billion-dollar-bet/mf-global-trustee-hints-at-negligece-suit-against-jon-corzine/ (on file with the *Columbia Law Review*) (reciting conclusions of MF Global Inc.'s trustee, including that customer funds had been used for "margin calls on European sovereign debt positions").

175. See id. (reporting trustee's conclusion that "Jon Corzine and other former executives of MF Global Holdings Ltd." were responsible for loss of customer funds).

Yet, in the entity-centric liquidation phase, with each entity seeking to maximize its own estate,[176] Holdings's trustee not only filed substantive claims against MF Global Inc., on the basis that Holdings's funds had been contributed to or were otherwise held by MF Global Inc.,[177] but also asserted the attorney-client privilege in response to a subpoena from MF Global Inc.'s trustee,[178] who was charged with locating the missing customer funds,[179] and challenged the validity of CFTC rules that would entitle MF Global Inc.'s futures customers to the entity's proprietary assets in the event that customers' funds could not be found and returned.[180] Additionally, Holdings's trustee disputed the applicability of those customer-protective rules to a brokerage firm liquidation brought under SIPA (a statute intended to govern *securities* brokerage firm liquidations but not *futures* brokerage firm liquidations), as the MF Global Inc. liquidation had been.[181] Needless to say, the entity-based battles meant that MF Global Inc. would face substantial challenges in retrieving its customers' assets.[182]

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176. See MF Global Plan Disclosure Statement, supra note 106, at 40–48 (listing claims made by various MF Global entities against other MF Global entities and noting Holdings and certain U.S. subsidiaries had "filed 68 claims against [MF Global Inc.] totaling in excess of $2.3 billion").

177. See Objection of the Chapter 11 Trustee to the SIPA Trustee's Motion for Entry of an Order Approving Agreement to Cooperate with and Assign Certain Claims to Class Action Plaintiffs in Pending Actions and to Distribute Funds Recovered to Customers at 15, In re MF Global Inc., 481 B.R. 268 (Bankr. S.D.N.Y. 2012) (No. 11-15059 (MG)), available at http://dm.epiq11.com/MFG/Document/GetDocument/1787440 (on file with the *Columbia Law Review*) (setting forth Holdings's claims against MF Global Inc., which totaled approximately $2.3 billion); see also MF Global Plan Disclosure Statement, supra note 106, at 34–35, 41 (summarizing Holdings's and other MF Global entities' claims against MF Global Inc.).

178. MF Global Plan Disclosure Statement, supra note 106, at 35 ("The Chapter 11 Trustee asserted attorney-client privilege . . . for some of the documents sought by the SIPA Trustee."). The two trustees ultimately reached an agreement involving Holdings's limited waiver of the privilege. See id. at 35–36.

179. See Spector & Lucchetti, SIPC Expected to Name Trustee, supra note 154 (describing MF Global Inc.'s "ultimate goal" as "maximizing value for customers").

180. See Trustee's Response to Briefing Regarding the Legal Principles and Framework for Allocation and Distribution of Customer Property at 4–5, In re MF Global Holdings Ltd., No. 11-15059 (MG) (Bankr. S.D.N.Y. filed Jan. 9, 2012) [hereinafter Trustee's Response to Briefing], available at http://dm.epiq11.com/MFG/Document/GetDocument/1555541 (on file with the *Columbia Law Review*) ("The Chapter 11 Trustee believes a plain reading of . . . the Bankruptcy Code requires a ratable distribution of . . . non-customer assets among [MF Global Inc.]'s general estate creditors . . . .").

181. See id. at 4 ("[T]he [CFTC's] Part 190 Regulations do not apply in a SIPA proceeding because a SIPA proceeding is not a case under chapter 7.").

182. See Staff Report, supra note 120, at 95–96 (describing challenges facing MF Global Inc.'s trustee in recovering U.S. customers' funds that Holdings had transferred to MF Global UK); Devlin Barrett & Aaron Lucchetti, Hope for MF Global Clients, Wall St. J. (July 31, 2012, 7:43 PM), http://online.wsj.com/article/SB10000872396390444058045

4. *Entity-Based Limitations on Customer Protections.* — In the squabbling among the MF Global trustees could be discerned a second problematic feature of the laws and rules governing futures brokers—one that is similarly the product of this Article's standard complaint: Those laws and rules do not anticipate that a brokerage firm may be entirely owned and controlled by another entity. In particular, with the goal of protecting customers,[183] the CFTC rules, as noted above, specify that a firm's own funds may be tapped to eliminate any shortfall of customer funds that might otherwise remain after customer assets have been marshaled.[184] Because the rules do not contemplate the existence of a parent company, however, to the extent the broker's own assets are insufficient to eliminate a shortfall, there is no apparent basis for recourse to the parent company's assets.[185] The parent is, after all, a separate entity.

However, it is precisely when there exists a parent company or other complex organizational structure that recourse to the parent company's (or other controlling entity's) assets becomes particularly important. In those situations, the parent company, pursuing its own proprietary trading or other business activities, may not have required the brokerage subsidiary to maintain capital beyond that necessary for it to satisfy its minimum net capital requirements under applicable CFTC and, possibly, SEC rules. Again, one might think of the broker and any other financial services subsidiaries under the parent company's umbrella as assets that the parent company may exploit to its best advantage, so long as the subsidiaries continue to satisfy their respective regulatory obligations.[186] This describes the state of affairs in the MF Global bankruptcy, and, not surprisingly, Holdings's trustee did not countenance the use of Holdings's assets for the benefit of MF Global Inc.'s brokerage customers.[187] Put another way, one of the trustee's apparent goals was to keep entity separateness intact—an endeavor that worked to the

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77561531001893726.html (on file with the *Columbia Law Review*) (reporting efforts by MF Global Inc.'s trustee to recover customer funds "face[d] daunting obstacles").

183. Unlike securities brokerage customers, futures brokerage customers, in the event their assets are missing from their accounts at the time of insolvency, are not entitled to compensation under SIPA or any other regulatory framework. See infra notes 193–195 and accompanying text for a discussion of the insurance provided under SIPA for securities brokerage customers.

184. See 17 C.F.R. § 190.08(a)(1)(ii)(J) (2013) (permitting customer recourse to "cash, securities or other property of the debtor's estate"); see also supra note 180 and accompanying text (noting Holdings's trustee challenged applicability of these rules).

185. See 17 C.F.R. § 190.08(a)(1) (describing assets comprising "customer property").

186. See supra notes 105–107 and accompanying text (describing how parent company may control and dominate subsidiaries' activities).

187. See Trustee's Response to Briefing, supra note 180, at 3–5 (claiming Holdings and other creditors of MF Global Inc., rather than brokerage customers, were entitled to MF Global Inc.'s assets under CFTC rules).

detriment of those persons the CFTC's liquidation regulations were designed to protect.

Although there have been claims that Holdings's trustee was overreaching, both in making claims against MF Global Inc. and in sequestering Holdings's assets,[188] he was merely pursuing the arguments that entity-centric laws and rules allowed, if not required, him to pursue. If the brokerage customers are ultimately made whole, as most observers speculate will happen,[189] it will be in spite of the financial services regulatory regime, not because of it. A more workable and fair regulatory approach would require a financial services firm's liquidation to proceed in the same manner as its operations were conducted—as a multipart, cohesive enterprise, with entity boundaries fluid, rather than ossified. There is no magic to entity boundaries in bankruptcy that did not exist prior to the bankruptcy filing. Financial services regulation, in other words, need not be based on corporate governance principles, which revolve around the relationship between an entity's owners (and possibly creditors), on the one hand, and its managers, on the other. Accordingly, it need not turn on determinations as to where one entity ends and another begins.

B. *Stanford Financial Group*

1. *The Ponzi Scheme.* — Like MF Global, Stanford Financial Group (SFG)—multiple entities whose activities were seamlessly coordinated—was a relatively well-established financial services firm,[190] whose customers

188. See, e.g., Ben Protess & Azam Ahmed, An MF Global Trustee Defends His Inquiry, N.Y. Times: Dealbook (Apr. 24, 2012, 8:37 PM), http://dealbook.nytimes.com/2012/04/24/an-mf-global-trustee-defends-his-inquiry/ (on file with the *Columbia Law Review*) (observing Louis Freeh, Holdings's trustee, had been criticized for his "handling of the case" and "prevent[ing] the brokerage [subsidiary's] customers . . . from recovering their money").

189. See, e.g., Trustee's Motion to (I) Approve the Trustee's Allocation of Property and (II) Approve the Terms of an Advance of General Estate Property for the Purpose of Making a Final 100% Distribution to Former Commodity Futures Customers of MF Global Inc. at 1, In re MF Global Inc., No. 11-2790 (MG) SIPA (Bankr. S.D.N.Y. filed Oct. 2, 2013), available at http://dm.epiq11.com/MFG/document/GetDocument.aspx?DocumentId=2423832 (asking court to approve distribution to MF Global brokerage customers of estate assets equal to remaining unpaid portion of prebankruptcy account balances); Nick Brown, Bankruptcy Judge Approves MF Global's Liquidation Plan, Reuters (Apr. 5, 2013, 1:06 PM), http://www.reuters.com/article/2013/04/05/us-mfglobal-bankruptcy-court-idUSBRE9340N420130405 (on file with the *Columbia Law Review*) (citing belief of Holdings's trustee that "customers in this case will be made whole" (internal quotation marks omitted)).

190. See Kristen Hays & Mary Flood, Billionaire Downplays Scrutiny of Stanford Financial, Hous. Chron. (Feb. 13, 2009), http://www.chron.com/business/article/Billionaire-downplays-scrutiny-of-Stanford-1742027.php (on file with the *Columbia Law Review*) (reciting company's claim it had "more than $50 billion in assets under management" and "more than 50 offices in North America, Latin America, the Caribbean and Europe").

likely took comfort in owner Allen Stanford's "great reputation."[191] Yet, by the time proceedings commenced to liquidate the Stanford entities, those customers had learned that they had been the victims of Mr. Stanford's mammoth Ponzi scheme, which involved over $7 billion.[192] Since then, their efforts have centered on attaining some measure of reimbursement, whether from SFG's estate or from the Securities Investor Protection Corporation (SIPC), a not-for-profit corporation that, pursuant to SIPA's mandate, operates an insurance scheme for securities brokerage customers.[193] Specifically, SIPC compensates customers in the event of a securities broker's insolvency at a time when customer accounts do not contain the funds or securities reflected on the customers' brokerage statements.[194] A securities broker that accepts customer deposits must be a SIPC member and, as such, must contribute to SIPC's insurance fund.[195]

The basic facts of the SFG Ponzi scheme are relatively straightforward. Mr. Stanford owned and controlled a multi-entity financial services enterprise. In particular, the enterprise comprised a U.S.-based entity—Stanford Group Company (SGC)—that was registered with, and regulated by, the SEC as a broker-dealer.[196] SGC was also a member of SIPC, even though it did not accept customer deposits and thus was under no obligation to become a member.[197] A second component of the enterprise was Stanford International Bank, Ltd. (SIBL), an Antiguan bank that, as a non-U.S. entity, was not subject to SIPA and,

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191. Ken Fisher with Lara Hoffmans, How to Smell a Rat: The Five Signs of Financial Fraud 94 (2009) (describing public perception of Allen Stanford while predicting he would end up in prison).

192. See Clifford Krauss et al., Texas Firm Accused of $8 Billion Fraud, N.Y. Times (Feb. 17, 2009), http://www.nytimes.com/2009/02/18/business/18stanford.html (on file with the *Columbia Law Review*) (reporting Allen Stanford's arrest for "massive ongoing fraud" involving potentially $8 billion in assets).

193. See Thomas W. Joo, Who Watches the Watchers? The Securities Investor Protection Act, Investor Confidence, and the Subsidization of Failure, 72 S. Cal. L. Rev. 1071, 1096 (1998) ("To the extent that the fund of customer property may be insufficient to satisfy all customer claims for net equity, the SIPC fund will cover the shortfall.").

194. See Securities Investor Protection Corporation, U.S. Sec. & Exch. Comm'n, http://www.sec.gov/answers/sipc.htm (on file with the *Columbia Law Review*) (last visited Sept. 29, 2013) ("If your brokerage firm goes out of business and is a member of [SIPC], then your cash and securities . . . may be protected up to $500,000 . . . ."). That might be the case when, for example, the firm has loaned out the securities for the purpose of allowing other brokerage customers to effect "short" sales, much as a commercial bank uses banking customers' cash deposits to make cash loans to other banking customers.

195. See 15 U.S.C. §§ 78ccc(a)(2), 78ddd(c) (2012) (setting forth SIPC's membership and assessment requirements).

196. See SEC v. Sec. Investor Prot. Corp., 872 F. Supp. 2d 1, 2 (D.D.C. 2012) (describing SGC as "now-defunct broker-dealer").

197. See id. at 5, 7–8 (noting SGC was SIPC member and customers deposited funds with Stanford International Bank, Ltd. rather than with SGC).

therefore, not a SIPC member.[198] SGC was a marketer, formally called an "introducing broker," that promoted SIBL and arranged the relationship between SIBL and its customers.[199] SGC's performance of that role was essential for SIBL's activities in the enterprise.[200] For its part, SIBL was the entity that accepted customer deposits.[201] In return, SIBL issued to depositors certificates of deposit (CDs) that, typical of CDs generally, had fixed terms and were to generate earnings based on specific rates of interest.[202] Moreover, and also typical of CDs generally, SIBL should have met its obligations to pay that interest through investing deposits legitimately and conservatively.[203]

In fact, through SIBL, Mr. Stanford expropriated customers' funds for his own personal purposes, satisfying obligations to pay customers who redeemed their CDs using new customers' deposits.[204] Regulators' revelation of the fraud, in February 2009, was followed by further revelations of regulatory failings that had kept the scheme operating longer than it might have otherwise.[205] Among other things, the episode embodied a veritable study in the problems created by the "revolving door" between regulators and the regulated.[206] But for the close relation-

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198. See id. at 5, 7 (observing SIBL was not SIPC member and reciting disclosure stating SIBL was not subject to any jurisdiction's "securities insurance laws").

199. See id. at 2 ("The [SIBL] CDs were marketed by [SGC].").

200. See id. at 3 (noting those who bought SIBL-issued CDs were SGC's customers).

201. See id. at 2, 7 (observing "CD investors" deposited funds with SIBL).

202. See James Quinn, FBI Believes Stanford Was Running Massive Ponzi Scheme, Telegraph (London) (Feb. 20, 2009, 8:51 PM), http://www.telegraph.co.uk/finance/financetopics/sir-allen-stanford/4737012/FBI-believes-Stanford-was-running-massive-Ponzi-scheme.html (on file with the *Columbia Law Review*) (describing CDs as "essentially medium-term savings products usually offering a fixed rate of interest"); cf. *Sec. Investor Prot. Corp.*, 872 F. Supp. 2d at 7 (noting SGC's marketing materials included caution that there was "no guarantee investors [would] receive interest distributions or the return of their principal" (internal quotation marks omitted)).

203. See Clifford Krauss, Indicted, Texas Financier Surrenders, N.Y. Times (June 18, 2009), http://www.nytimes.com/2009/06/19/business/19stanford.html (on file with the *Columbia Law Review*) (noting, according to SEC, Stanford's CDs "had been surreptitiously invested in real estate, other speculative investments and into Mr. Stanford's own operations even as his clients were told their funds had been invested in highly liquid and conservative assets").

204. See SEC, Analysis of Securities Investor Protection Act Coverage for Stanford Group Company 5 (2011), available at http://www.sec.gov/rules/other/2011/stanford-sipa-analysis.pdf (on file with the *Columbia Law Review*) (explaining Stanford used "CD sale proceeds" to fund redemptions "because sufficient assets, reserves and investments were not available").

205. See generally Office of Inspector Gen., SEC, Investigation of the SEC's Response to Concerns Regarding Robert Allen Stanford's Alleged Ponzi Scheme (2010) [hereinafter SEC Investigation Report], available at http://www.sec.gov/news/studies/2010/oig-526.pdf (on file with the *Columbia Law Review*) (detailing regulators' longstanding suspicions of Stanford's business and SEC's failures, over decade, to bring enforcement action against him or his firm).

206. See supra note 3 and accompanying text (noting how regulators' relationships with regulatory subjects challenge enforcement efforts); see also Murray Waas, Insight:

ship between Mr. Stanford and certain members of the SEC staff, the SEC may have more deeply scrutinized Mr. Stanford's activities and more doggedly pursued customer and third-party questions and complaints about those activities.[207]

2. *The Pursuit of SIPC Compensation.* — Regardless of how or whether regulators ignored or underperformed their obligations while the Stanford fraud was underway, the fact remained that SFG's customers had lost the principal value of their deposits, as well as any expectation of interest on those funds.[208] The question for them, particularly given the backdrop of a regulatory regime based on the goal of protecting investors, became whether they were entitled to any compensation for their losses.[209] The only realistic candidate for providing that compensation was SIPC, pursuant to its obligations under SIPA.[210] The SEC endorsed that prospect, a crucial condition given that, under SIPA, private parties have no right to seek SIPC compensation on their own.[211] Accordingly, acting pursuant to its authorization under SIPA, the SEC sought to compel SIPC to provide SIPA-based compensation to Stanford's victims, on the grounds that SGC—again, the U.S.-based introducing broker—had been an SEC-registered broker-dealer and a SIPC member.[212]

How Allen Stanford Kept the SEC at Bay, Reuters (Jan. 26, 2012, 5:46 PM), http://www.reuters.com/article/2012/01/26/us-sec-stanford-idUSTRE80P22R20120126 (on file with the *Columbia Law Review*) (describing how Stanford "paid at least eight former senior U.S. and foreign regulators and law-enforcement officials for legal advice or investigative services").

207. See Waas, supra note 206 (describing how Stanford's relationship with ex-regulators and officials may have "ke[pt] authorities at bay for so long"). But see SEC Investigation Report, supra note 205, at 149 (noting SEC's Office of Inspector General "did not find that [the SEC's] reluctance . . . to investigate or recommend an action against Stanford was related to any improper professional, social or financial relationship on the part of any former or current SEC employee").

208. See Peter J. Henning, Compensating Stanford's Investors, N.Y. Times: Dealbook (June 20, 2011, 3:04 PM), http://dealbook.nytimes.com/2011/06/20/compensating-stanfords-investors/ (on file with the *Columbia Law Review*) (noting SIBL's customers bought "$7.2 billion in allegedly bogus certificates of deposit").

209. See id. (observing "SIPC provides a measure of protection for customers when a broker becomes insolvent" but "authorities are still figuring out whether investors can get compensated for some of their losses").

210. Cf. id. (noting SEC was pushing for Stanford's customers to be "treated as brokerage customers by [SIPC]" because, if they were so treated, they "could get at least some of their money back").

211. See 15 U.S.C. § 78eee(a) (2012) (setting forth who may seek SIPC protection for broker-dealer's customers); Sec. Investor Prot. Corp. v. Barbour, 421 U.S. 412, 424–25 (1975) (holding customers of broker-dealer do not have implied right of action under SIPA to compel SIPC to exercise its authority to compensate them for losses).

212. See SEC v. Sec. Investor Prot. Corp., 872 F. Supp. 2d 1, 2 (D.D.C. 2012) (noting SGC was SEC-registered broker-dealer and SIPC member). More precisely, the SEC sought to compel SIPC to seek a protective decree from the U.S. District Court for the Northern

SIPC declined to comply with the SEC's request to commence a SIPA liquidation proceeding, the first time in SIPA's forty-two-year history that it had done so.[213] SIPC's reasoning, while upsetting to the Stanford victims, was simply based on the statute.[214] According to SIPC, the victims were not entitled to compensation under SIPA because the statute does not cover brokerage customers in their particular circumstances.[215] That was in part because, according to SIPC, the sole SIPC member in the Stanford group of entities, SGC, did not accept deposits from, or otherwise perform a custodial function for, Stanford customers.[216] Customers thus did not suffer losses at the hands of the entity whose actions would have given rise to SIPC insurance coverage.

SIPC's second argument, also surely correct, was that Stanford's victims had not suffered the sort of harms that SIPA exists to remedy: a broker-dealer's loss of cash or securities that a brokerage customer placed with it.[217] Specifically, it was not the case that the securities the victims had bought through their relationship with Stanford—the CDs—were missing from the victims' accounts with Stanford, since the CDs themselves were accounted for.[218] To be sure, they were worthless, but SIPC's point was that the victims had gotten, and still possessed, what

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District of Texas, which would have had jurisdiction over any liquidation proceeding conducted under SIPA. See id.

213. See id. ("[T]his proceeding is the first instance since SIPA was enacted . . . in which the SEC has sought . . . to compel the SIPC to file an application for a protective decree.").

214. See 15 U.S.C. § 78*lll*(2)(A)–(C) (noting "term 'customer' of a debtor means any person . . . who has a claim on account of securities received, acquired, or held by the debtor" but does not include person whose claim "arises out of transactions with a foreign subsidiary of a member of SIPC"); see also *Sec. Investor Prot. Corp.*, 872 F. Supp. 2d at 7–11 (describing SIPC's SIPA-based arguments); Letter from Stephen P. Harbeck, President, Sec. Investor Prot. Corp., to Ralph S. Janvey, Receiver, Stanford Fin. Grp. (Aug. 14, 2009) [hereinafter Harbeck Letter], available at http://www.stanfordfinancialreceivership.com/documents/SIPC_Letter.pdf (on file with the *Columbia Law Review*) (describing why, given facts of Stanford fraud, "there is no basis for SIPC to initiate a proceeding under SIPA").

215. See Securities Investor Protection Corporation's Brief in Opposition to SEC's Application for Order Under 15 U.S.C. § 78ggg(b) at 14–21, *Sec. Investor Prot. Corp.,* 872 F. Supp. 2d 1 (No. 11-mc-678 (RLW)) [hereinafter SIPC Brief] (explaining why, in SIPC's view, SEC had not adequately shown that Stanford's customers were entitled to SIPC compensation); Harbeck Letter, supra note 214, at 3 (describing why SIPC compensation is not available, under SIPA, for SIBL's customers).

216. See SIPC Brief, supra note 215, at 16–18 (explaining Stanford customers placed their funds with SIBL, not SGC, and bought SIBL CDs).

217. See *Sec. Investor Prot. Corp.*, 872 F. Supp. 2d at 6 ("[T]he SIPA statute 'attempts to protect customer interests in securities and cash *left with* broker-dealers . . . .'" (emphasis added by *Sec. Investor Prot. Corp.*) (quoting Louis Loss & Joel Seligman, Securities Regulation 3290 (3d ed. 2003))).

218. See SIPC Brief, supra note 215, at 18 ("[U]pon sending their funds to SIBL, investors or their designees received their actual CDs in return."); Harbeck Letter, supra note 214, at 3 (noting, although "SIPC protects the custody function performed by SIPC member firms for customers," because SIBL issued CDs to its customers, "those individuals [still] have their securities" (emphasis omitted)).

they had paid for.[219] Accordingly, Stanford's victims were not suffering the harm, and therefore were not in need of the protections, that SIPA contemplates. If those arguments seem to be based on formalism and blind to the realities of the Stanford company structure, that is a necessary consequence of SIPA's formalistic emphasis on entity boundaries and entity independence.

3. *Regulatory Disregard of Entity Relationships.* — After the revelation of the Stanford fraud, the entity-centrism of applicable laws and rules further disadvantaged those whom they were created to protect. To begin with SIPC's first argument, SIPA covers only brokerage "customers"—those who have "entrusted cash or securities to a broker-dealer who becomes insolvent."[220] No entrustment means no SIPC coverage. In theory, at least, the basis for that distinction is unassailable. If an investor has not placed any funds or securities with the insolvent broker-dealer, she has not lost anything as a result of the insolvency. Of course, myriad factors might complicate that picture. For example, is an investor a customer of a SIPC member if she entrusts funds or securities to a third party who then sends the assets to a SIPC member to hold in custody?[221] Is the investor covered if she deposits funds with a SIPC member who then sends the funds to the ultimate custodian,[222] who is not a SIPC member?[223] One particular factor complicates the Stanford matter: The firm with which customers placed their funds—SIBL, which, again, was not a SIPC member—was owned and controlled by the person who owned and controlled the firm that brought customers into the Stanford

219. See SIPC Brief, supra note 215, at 18–19 (contending CDs were either delivered to customer or held by IRA custodian).

220. Sec. Investor Prot. Corp. v. Pepperdine Univ. (In re Brentwood Sec., Inc.), 925 F.2d 325, 327 (9th Cir. 1991).

221. Although more information is needed to answer this question, based on the SEC's interpretation of "customer" under SIPA, that answer is arguably "yes," regardless of whether the customer knew that the third party would transfer the assets, so long as the arrangement satisfies certain conditions. See *Sec. Investor Prot. Corp.*, 872 F. Supp. 2d at 10 (reciting SEC's interpretation of "customer," whereby investor is not "customer" of introducing broker with whom investor placed assets, to extent introducing broker "promptly forwards all funds and securities to the clearing broker [who coordinates the investor's trading activities]," and clearing broker, among other requirements, acknowledges investor's customer status).

222. As used in the financial services context, a custodian is a firm—often a broker-dealer or a bank—that is responsible for holding and safeguarding brokerage customers' assets. See Custodian, Investopedia, http://www.investopedia.com/terms/c/custodian.asp (on file with the *Columbia Law Review*) (last visited Sept. 17, 2013) (defining "custodian" as "financial institution that holds customers' securities for safekeeping so as to minimize the risk of their theft or loss," which may also "offer a variety of other services including account administration, transaction settlements, collection of dividends and interest payments, tax support and foreign exchange").

223. Arguably, the answer to this question is "no," again based on the SEC's interpretation of "customer." See *Sec. Investor Prot. Corp.*, 872 F. Supp. 2d at 10 (reciting SEC's interpretation of "customer" for purposes of SIPA).

scheme—SGC, which, again, was a SIPC member.[224] SIPA simply does not speak to that fact pattern. SIPA and the legislative history behind it speak of broker-dealers in the singular and do not appear expressly to contemplate, or consider the implications of, covered firms' status as components of larger, multi-entity enterprises.[225]

That focus on broker-dealers as stand-alone, independently operated businesses is also evident in the notion that SIPC membership should be available voluntarily even to those firms that do not pursue the sorts of activities deemed to give rise to the risks about which Congress was concerned—that is, those firms that "neither hold free credit balances for customers nor hold securities for them which may be 'hypothecated.'"[226] The legislative history approvingly suggests that brokerage firms that do not place their customers' cash or securities at risk may nonetheless desire to become SIPC members on the basis that doing so might be good for business.[227] Some firms, it notes, may wish "to take advantage of SIPC membership as a general asset in the conduct of their business."[228] The notion behind the prospect of, say, an introducing (noncustodial) broker becoming a member is that everyone wins. Voluntary members may get a marginal reputational boost, while SIPC coffers get a marginal boost in the annual assessments it levies against member firms. From the perspective of achieving regulatory goals, moreover, it is simply a circumstance of no harm, no foul. Under this reasoning, since broker-dealers are stand-alone entities, voluntary SIPC membership, though doing nothing to further SIPA's purpose, also does nothing to harm brokerage customers.

However, once we introduce the notion that any given broker-dealer may not, in fact, operate separately from other broker-dealers or other custodians and, indeed, may be part of a larger, multi-entity financial services enterprise, voluntary membership is no longer akin to a tree fall-

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224. See id. at 2 (describing Stanford Financial Group entities and their relationships to one another).

225. In light of the House and the Senate committees' respective reports on the proposed statute at the time of its enactment, that is not surprising. The goal of the legislation, the House Committee on Interstate and Foreign Commerce pointed out, is to "provide protection to investors if the broker-dealer with whom they are doing business encounters financial troubles." H.R. Rep. No. 91-1613, at 1 (1970).

226. S. Rep. No. 91-1218, at 4 (1970). In other words, in enacting SIPA, Congress was concerned only about those broker-dealers who held customer assets and to whom customers might pledge those assets in the commonplace event that the customers borrowed cash or securities from the broker-dealers in furtherance of the customers' trading or investment activities. By contrast, Congress was not concerned about those broker-dealers who did not hold customer assets (and who, therefore, could not be the pledgees of customer assets) because Congress perceived that those broker-dealers would not be in a position to lose the assets.

227. See id. (noting for broker-dealers that do not hold customer cash or securities "membership in SIPC is voluntary").

228. Id.

ing in the deserted woods. It is the Stanford Financial Group. Mr. Stanford controlled two entities.[229] One did not accept customer funds but was a SIPC member (and advertised itself as such), while the other entity accepted customer deposits but, located offshore, was not a SIPC member or otherwise subject to a customer funds insurance regime.[230] Regardless of whether Stanford's victims had taken (unwarranted) comfort in SGC's status as a SIPC member at the time they bought their CDs or whether Mr. Stanford and his colleagues intended to (mis)lead them to think they would have the benefit of SIPC coverage in the event of SFG's insolvency, SIPC's entity-centrism meant that the statute did not address the commonplace circumstance of commonly controlled financial services entities, let alone the prospect of an enterprise's piecemeal use of SIPC membership as window dressing.

4. *Entities as Investment Instruments.* — Recall that a second component of SIPC's argument that Stanford's victims did not fall within SIPA's purview was the notion that nothing had happened to customers' holdings. The funds customers placed with SFG did, in fact, go to buying CDs, and those CDs—the certificates themselves—still exist and, in one way or another, are accounted for.[231] That circumstance contrasts with the scenario SIPA contemplates, in which assets are not available for the customer to withdraw as a result of a brokerage firm's insolvency at a time when a customer's assets are "in use" by the firm, leaving the firm obligated to the customer to that extent.[232] Entity-centrism can be readily seen in this aspect of the statute as well, in the form of a preference for nonpooled customer accounts.[233]

In any brokerage arrangement, customer funds should be properly deployed, meaning that they should be suitably invested or otherwise used so as to produce a return for customers. Beyond that defining concept, brokerage arrangements differ. In one common arrangement, the

229. See *Sec. Investor Prot. Corp.*, 872 F. Supp. 2d at 2 (noting Stanford "owned or controlled" Stanford Financial Group entities).

230. See id. at 2, 7–8 (describing functions of SGC and SIBL within Stanford Financial Group and noting whether each had been SIPC member).

231. See SIPC Brief, supra note 215, at 18–19 (arguing Stanford's customers had custody of their CDs and SGC did not have custody of any customer funds or securities).

232. See id. at 10–12 (observing "SIPA protects only the cash or securities that a brokerage is holding for a person when it fails" but does not insure value of any such securities (emphasis omitted)).

233. In other words, the Stanford CD arrangement may be viewed as a type of pooled investment arrangement. Its structure, moreover, had substantial similarities to that of other pooled investment entities. In both cases, an investor effectively buys a security that she thereafter holds until redemption. The funds the investor used to buy the security are pooled with the funds that other investors placed in the arrangement, which are then deployed for various investment activities. Depending on the success of those activities, the value of the security held by the investor will increase or decrease. Regardless, under SIPA, the investor cannot be said to have cash or securities "on deposit" in the fund or with the fund's operator.

customer grants the brokerage firm discretionary authority to trade and invest funds or other assets that the customer places in a brokerage account under her name.[234] In those circumstances, the customer has legal title to those assets and to each security or other instrument for which those assets are used.[235] If the broker misappropriates the customer's assets prior to, or in connection with, becoming insolvent, the customer, in addition to having fraud-based claims, is also protected under SIPA.[236] By contrast, where the customer has bought a CD from the brokerage firm, she has bought something resembling an interest in a pooled investment entity—a fund, in other words.[237] Regardless of what the broker, as the fund's manager, might do with the securities or other instruments the fund has bought, the customer still formally holds her shares or interests *in the fund*. Therefore, in the event the broker absconds with the fund's assets or uses the fund to carry out a pyramid scheme, the customer has no protection under SIPA. Nothing is missing, after all.[238]

This suggests that the structure of an investor's discretionary arrangement with her brokerage firm is critically important. If the investor bought an interest in a fund sponsored by the firm, in the event of a Stanford-like fraud she likely would end up with nothing. However, if the investor instead placed her assets in a separately managed brokerage account, she would likely be compensated with SIPA insurance. Arguably, this is one difference between Stanford's victims and Madoff's—the latter, but not the former, were deemed entitled to at least some com-

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234. See Accounts—Opening a Brokerage Account, U.S. Sec. & Exch. Comm'n, http://www.sec.gov/answers/openaccount.htm (on file with the *Columbia Law Review*) (last modified Mar. 26, 2008) (explaining investor opening brokerage account may choose to give broker discretionary authority, permitting broker to invest investor's account assets "without consulting [the investor] about the price, the type of security, the amount, and when to buy or sell").

235. See SIPC Brief, supra note 215, at 11 ("SIPA protects only the cash or securities that a brokerage is holding for a person when it fails . . . ." (emphasis omitted)).

236. See id. at 10–13 (summarizing what SIPA covers and what it does not cover). That result is perhaps surprising, given that SIPA is expressly not a statute designed for antifraud purposes. See id. at 12 ("SIPA does not protect against . . . fraud . . . ."); see also S. Rep. No. 91-1218, at 2–3 (1970) (observing although Securities Act of 1933 and Exchange Act require disclosure and protect investors against "fraudulent, manipulative, or deceptive selling schemes[,] . . . neither statute prevents the investor from losing his entire investment if his broker fails because of operational and, ultimately, financial difficulties").

237. In both the Stanford context and the typical hedge fund context, for example, investors receive securities in exchange for their contributions of capital. Cf. Office of Investor Educ., SEC, Investor Bulletin: Hedge Funds (2013), available at http://www.sec.gov/investor/alerts/ib_hedgefunds.pdf (on file with the *Columbia Law Review*) (describing common limitations imposed by hedge funds on investors' ability to redeem shares).

238. However, the customer has fraud-based claims under federal, and probably state, securities laws. See SIPC Brief, supra note 215, at 12 ("SIPA does not guarantee the value of investments even if they fail . . . .").

pensation from SIPC.[239] It is also a difference between entity-centrism and a more complete understanding of how financial services firms are structured and function. As soon as a broker-dealer establishes a "pool"—an entity—for investing customer assets, regulation refuses to look beyond the boundaries of that entity and the fact of the continuing existence of the securities that the pool issued, however worthless they may have become.[240]

III. BASES OF REGULATION'S DISSONANCE

If the entity-centrism of financial services regulation appears inconsistent, in many respects, with the operations of financial services firms, it is worth considering why it is so prevalent. Why are entities, rather than subentity or multi-entity units, the subject of financial services regulation?[241] What is the basis of the doctrine that investment advisers owe their regulatory duties to an entity that they created and control?[242] Why do financial services regulations that apply to insolvencies cause a multi-entity enterprise that in life functioned as a unitary firm to break into warring units in death?[243] And why does the brokerage customer insurance regime not encompass customers of all entities formed, owned, and controlled by the same person?[244] What, in other words, has led to the entity-centrism of financial services regulation?

Only by better understanding the origins of this problematic aspect of financial services regulation can we appreciate that it is by no means indispensable and, more importantly, equip ourselves to move beyond it and to think of alternative and more effective regulatory approaches.

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239. See John Wasik, Is SIPC Doing Enough for Scam Victims?, Forbes (Sept. 20, 2012, 12:38 PM), http://www.forbes.com/sites/johnwasik/2012/09/20/is-sipc-doing-enough-for-scam-victims/ (on file with the *Columbia Law Review*) (reporting SIPC's announcement that "nearly $2.5 billion in checks were mailed to victims in the liquidation of Bernard Madoff Investment Securities LLC").

240. One might wonder whether only more sophisticated investors might choose to obtain investment services through a pooled, or fund, structure rather than through a separately held discretionary brokerage account and whether, if so, there might be less need for regulatory protections in the context of the pooled structure. If there is a greater tendency for sophisticated investors to choose one mode of investing over the other, arguably that tendency would be in the direction of discretionary account arrangements. Discretionary account arrangements permit the broker or adviser to tailor investment decisions to the investor's particular needs, whereas pooled structures work well for investors whose investment assets might not reach the threshold necessary for a discretionary account arrangement.

241. See supra notes 43–56 and accompanying text (observing entity, rather than some other unit, is typically regulatory subject).

242. See supra Part I.B.2 (noting investment adviser owes regulatory obligations to funds it has created, rather than to funds' investors).

243. See supra Part II.A.3 (discussing MF Global bankruptcy).

244. See supra Part II.B.3 (evaluating whether customers of non-SIPC entity under common ownership with SIPC member were owed SIPC compensation).

Accordingly, this Part suggests that two processes, largely unwitting ones, have played a role—and will continue to play a role—in bringing about the pervasive entity-centrism of financial services regulation. First, as Part III.A describes, early entity-based approaches to formulating securities regulation may have dictated the formulation of regulation in other financial services contexts, a tendency this Article calls "regulatory inertia." Second, as Part III.B discusses, regardless of what processes influenced the formulation of entity-centric regulation, its most harmful manifestations have occurred when essentially unused or untested laws and rules have been dusted off and put into action to address new sets of facts but have been incapable of doing so, a tendency this Article calls "regulatory atrophy."

A. *Regulatory Inertia*

One lens through which to evaluate the bases of entity-centrism is the notion, first developed in Part I, that the entity focus of financial services regulation has some affinities with the norms and principles of corporate governance.[245] The body of laws, rules, norms, and practices by which corporations are governed concern themselves, by definition, with the entity.[246] That observation, of course, does not address the reasons why financial services regulation would have followed suit. The connection, however, can be discerned by returning to the first principles of financial services regulation, beginning with its commonsensical definition: Financial services regulation is the regulation of firms in their capacities as providers of specific types of financial services. As discussed in Part I, the term "financial services," for its part, encompasses such activities as providing securities and futures brokerage services, financial and investment advisory services, and mutual fund or other pooled investment services.[247] Financial services regulation, then, is a similarly broad label.[248]

It did not start out that way, however, which becomes evident when one considers where some of the earliest U.S. financial services regulation might be found—namely, within the suite of securities statutes

245. See supra notes 33–35 and accompanying text (observing corporate governance norms are entity-focused).

246. See supra notes 33–34 and accompanying text (discussing how corporate governance doctrine is both entity-focused and centered on entity's internal relationships).

247. See supra notes 43–55 and accompanying text (describing various services encompassed by "financial services" label).

248. See supra Part I.B (describing various types of financial services regulation and their entity-centric deficiencies); see also Lawrence J. White, Technological Change, Financial Innovation, and Financial Regulation: The Challenges for Public Policy 14–20 (Wharton Fin. Insts. Ctr., Working Paper No. 97-33, 1997), available at http://fic.wharton.upenn.edu/fic/papers/97/white.pdf (on file with the *Columbia Law Review*) (discussing structure and content of various types of financial services regulation).

enacted in the aftermath of the 1920s stock market crash. One of those statutes is the Advisers Act,[249] which, along with the SEC's rules under that statute,[250] governs advisers that provide investment advice as to securities; another is the Investment Company Act,[251] which, with the associated SEC rules,[252] sets forth the regulatory framework covering public "investment companies," such as mutual funds. Finally, broker-dealers, including investment banks, underwriters, and those creatures the media refers to as "trading firms," are regulated through various provisions of the Exchange Act[253] and associated SEC rules.[254] Insofar as financial services regulation pertains to investment advisers, publicly offered investment entities, and securities brokerage firms, it is a form of *securities* regulation.[255] Accordingly, we might say that financial services regulation originated as a form of securities regulation.

Not all components of the early securities statutes can be considered financial services regulation, however. In particular, perhaps the most fundamental of the Depression-era securities statutes is the Securities Act of 1933 ("Securities Act"),[256] which, along with the SEC's rules under it,[257] regulates firms' issuance of securities to investors, whether through public or private offerings. In addition, although the Exchange Act contains the regulatory framework governing broker-dealers, it encompasses considerably more than that.[258] Specifically, it primarily governs securities exchanges and the trading of public companies' securities in the secondary markets.[259]

There are, then, critical distinctions among the types of activities the securities laws regulate. The financial services regulatory provisions contained in and under the securities laws—encompassing, again, regulation of broker-dealers, investment advisers, and investment companies—are forms of professional services regulation. That is, they govern and

249. 15 U.S.C. §§ 80b-1 to 80b-21 (2012).

250. 17 C.F.R. §§ 275.0-2 to 275.222-2 (2013).

251. 15 U.S.C. §§ 80a-1 to 80a-64.

252. 17 C.F.R. §§ 270.0-1 to 270.60a-1.

253. 15 U.S.C. §§ 78o-1 to 78o-3.

254. 17 C.F.R. pt. 240.

255. That is, securities regulation pertains to the issuance of or investment in securities and is set forth in the securities laws and the rules adopted by the SEC pursuant to the authority that the securities laws grant to that agency. The securities statutes, which include the Securities Act of 1933, the Exchange Act, the Advisers Act, the Investment Company Act, and the Trust Indenture Act of 1939, combined with the SEC's rules under those statutes, contain the laws and rules governing broker-dealers, investment advisers, and mutual funds.

256. 15 U.S.C. §§ 77a–77aa.

257. 17 C.F.R. pt. 230.

258. See Larry D. Soderquist & Theresa A. Gabaldon, Securities Law 185–92 (4th ed. 2011) (summarizing Exchange Act's regulatory purview).

259. See id. (summarizing Exchange Act's regulation of secondary securities markets).

supplement the relationships between, on the one hand, those who provide financial services and, on the other hand, those persons' "clients" and/or "customers" (with the applicable term depending on the particular financial services context).[260] By contrast, laws and rules governing securities offerings and trading exist only to structure the relationships among constituencies of a business association—namely, the parties that manage the business and those that own it. In other words, this latter form of securities regulation exists to further and support corporate governance norms by supplying mandatory requirements and procedures for aspects of the firm's (a stand-alone entity's) constitution and the relationship among its key components.[261] It does so, moreover, in the name of promoting market integrity and protecting those who could and do supply capital to business enterprises—or, more accurately, to particular entities that conduct business activities—or who otherwise put their capital at risk in the securities markets.[262]

Put another way, securities regulation of the second sort is all about the entity. Conversely, it is also plausible to say that, without the entity, there is no securities regulation. To be sure, the entity's central position is especially evident in the Securities Act, focusing as it does—and as it must to achieve its goals—on issuers' (entities') obligations vis-à-vis shareholders, even though its regulation nominally pertains to "distributions of securities."[263] The Exchange Act, however, also necessarily has an entity focus, notwithstanding its core concern with the secondary markets. That suggestion arises from the circumstance that secondary market regulation is concerned with who, at any given time, owns shares of a particular entity and how those persons came to acquire that status.[264] That is, part of what secondary market regulation requires is transparency regarding large stakeholder and insider holdings, as well

260. See generally Carolyn Cox & Susan Foster, Bureau of Econ., FTC, The Costs and Benefits of Occupational Regulation 2–20 (1990), available at http://www.ftc.gov/be/consumerbehavior/docs/reports/CoxFoster90.pdf (on file with the *Columbia Law Review*) (describing regulation of professionals in United States and, in particular, its rationale, costs, and benefits).

261. See Smith & Williams, supra note 14, at 175 (noting securities regulation is "important overlay" for state corporation statutes and provides "mechanism of accountability within the corporation").

262. See The Investor's Advocate: How the SEC Protects Investors, Maintains Market Integrity, and Facilitates Capital Formation, U.S. Sec. & Exch. Comm'n, http://www.sec.gov/about/whatwedo.shtml (on file with the *Columbia Law Review*) (last modified June 10, 2013) (describing U.S. securities regulatory framework and noting SEC's "mission" is "to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation").

263. Thomas Lee Hazen, Federal Securities Law 27 (Kris Markarian ed., 3d ed. 2011).

264. See id. at 100–05, 110–23 (summarizing Exchange Act's regulatory coverage).

as strictures against fraudulent and misleading statements or conduct by those who are privy to confidential information about the issuer.[265]

The distinctions between the types of work the securities laws perform lead to the following state of affairs: Ensconced within a set of statutes that is "all about the entity" are provisions pertaining to those financial services providers who facilitate securities trades and those who provide advice on securities investments. Perhaps it should come as little surprise, then, that the financial services regulation contained in the Securities Act and the Exchange Act and their compatriots (the Advisers Act and the Investment Company Act) gives a central role to the entity. In other words, it was natural, if not inevitable, for those regulatory provisions similarly to use the self-contained entity as the core around which specific obligations and sanctions revolve. This tendency may be discerned, for example, in the doctrine that deems a hedge fund or other private fund (and not its investors) the client of the fund's investment adviser[266] and in the mutual fund regulatory regime, which aims regulation at the fund rather than its investment adviser, even though the former is but an instrument for the latter's providing its services.[267]

It is the ostensible "inevitability"—or inertia—in the production of regulation that paves the way to regulation's continued elevation and reification of entity boundaries in not only the entity's operations but also its winding up, even though, from a functional perspective, entity boundaries may be next to meaningless. Yet there is an important distinction between the traditional function of securities regulation (the regulation of the issuance and resale of securities) and services that merely involve, facilitate, or relate to that function. Financial services regulation effectively supplements private ordering, specifying aspects of the relationship between financial services providers and their customers and clients.[268] It does so on the basis of lawmakers' and regulators' determinations that private ordering—the functioning of the market—will systematically fail to protect market participants or create unduly and

265. See id. (describing provisions of Exchange Act governing tender offers and takeover bids and prohibiting fraudulent and manipulative conduct).

266. See supra notes 72–82 and accompanying text (describing doctrine and its potentially adverse implications for investor protection). If the traditional client was the thing at which the adviser directed its advice, the argument goes, then that approach should continue to apply when the clients of yore have pooled their assets in an entity. The entity now receives the advice, so the entity should now be the "client," never mind that the adviser created and controls the entity and that its purpose is simply to facilitate the adviser's management of numerous (would-be) clients' assets. Supra notes 71–82 and accompanying text.

267. See supra Part I.B.2 (summarizing regulatory focus of mutual fund regulation and advisers' use of mutual funds to provide investment services).

268. See supra notes 17–20 and accompanying text (noting purpose of financial services regulation is to protect those who use financial services).

unproductively large transaction costs.[269] Much like securities regulation as traditionally understood, then, its purpose is to protect investors (that is, clients and customers) and to promote market integrity.[270] However, there is no need to base its content on the entity or on entity-focused corporate governance norms. Unlike corporate codes, corporate governance norms, or even bread-and-butter securities regulation,[271] financial services regulation does not perform a constitutive role within entities, and its efficacy does not depend on the existence of entities, whether of the corporate kind or otherwise.

B. *Regulatory Atrophy*

That the U.S. securities laws lump securities regulation centering on corporate governance concerns with that centering on financial services that involve securities likely has been only one factor affecting the development and evolution of financial services regulation. After all, financial services regulation encompasses more, and less, than securities regulation, in that not all financial services regulation falls under the securities regulation umbrella.[272] Moreover, whatever might explain the origins of regulatory entity-centrism, policymakers long ago recognized the growth and emerging dominance of multi-entity financial services enterprises.[273] Accordingly, there has to be more to the story of entity-centrism.

One possibly glaring consideration in that regard is the rather mundane circumstance that laws and rules are prone to become obsolete

269. See Joel P. Trachtman, The International Economic Law Revolution, 17 U. Pa. J. Int'l Econ. L. 33, 53 (1996) (asserting regulation is appropriate only to extent it minimizes combined cost of "(i) deadweight loss due to [the market's] failure to provide the optimal mix of [particular goods at issue], and (ii) transaction costs in arriving at the final allocation").

270. See, e.g., Lloyd's Market Supervision (Formerly Lloyd's Regulatory Requirements) Change in Syllabus and Study Book for October 2003 Examination Session, Lloyd's Market Bull. (July 25, 2003), available at http://www.lloyds.com/~/media/Files/The%20Market/Communications/Market%20Bulletins/Market%20bulletins%20pre%2005%202010/2003/Y3102.pdf (on file with the *Columbia Law Review*) ("The origins and purpose of financial services regulation [are] consumer protection . . . and maintaining confidence in the financial system.").

271. This term refers to foundational securities regulation: the regulation of the issuance of securities under the Securities Act and the regulation of the resale of securities under the Exchange Act. See supra notes 256–259 and accompanying text (describing core functions of Securities Act and Exchange Act).

272. See supra notes 40–42 and accompanying text (listing types of financial services regulation that are not components of securities regulation).

273. Indeed, in the banking context, the Bank Holding Company Act of 1956 is, as its name implies, predicated on the longstanding circumstance that banks are typically subsidiaries in multi-entity enterprises. See 12 U.S.C. § 1841(a) (2012) (defining "bank holding company" as "any company which has control over any bank or over any company that is or becomes a bank holding company by virtue of [the Bank Holding Company Act]").

over time.[274] Although grounding financial services laws and rules in corporate governance norms may have been appropriate at the time the statutes and codes were enacted or adopted, financial services firms' structures have changed over time to the point that what once worked has become ineffective, if not counterproductive. For example, the expansion and maturation of the mutual fund industry in the past eighty years has rendered nigh archaic the securities statute that governs it[275]—and, in particular, its entity-focused framework relying on governance and oversight by fund boards of directors.[276]

Nevertheless, recent events suggest that the tale of entity-centrism is more complex than the tale of regulation falling behind in the march of time and human creativity. The now-defunct global brokerage firm, Lehman Brothers, exemplifies this point. When that firm went bankrupt in the throes of the financial crisis, some clients of its U.S. brokerage subsidiary, to their unwelcome surprise, were disadvantaged by certain provisions of U.K. securities regulation governing the protection of customer funds.[277] Lehman Brothers's U.K. subsidiary (LBIE), it turns out, had been using the so-called "alternative approach" under U.K. rules for segregating clients' funds from the firm's own funds.[278] Pursuant to that approach, rather than keeping client funds segregated at all times, the firm could accept client funds into, and pay client funds out of, its "house" accounts, so long as, at the end of each day, it segregated client money into a client bank account based on the total amount to which all clients would be entitled if they withdrew all of their assets.[279] The result of Lehman Brothers's using that method was the creation of an inherent

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274. Wendy L. Gramm & Gerald D. Gay, Leading a Regulatory Agency: Lessons from the CFTC, Regulation, Fall 1994, at 64, 65 ("As markets change, existing regulations become obsolete and require elimination or updating.").

275. That statute is, again, the Investment Company Act, 15 U.S.C. §§ 80a-1 to 80a-64 (2012).

276. See supra Part I.B.2 (describing Investment Company Act's regulatory approach and investor protection concerns it produces); see also Krug, Investment Company as Instrument, supra note 57, at 272–74 (describing how regulation of mutual funds under Investment Company Act is based on corporate governance norms inconsistent with how mutual funds actually operate).

277. See Lukas Becker, Protection Racket, Risk, June 2012, at 62, 62 (reporting "[c]lients and affiliates of Lehman Brothers' UK-based entity found themselves in [a] trap when the securities firm went bust . . . [d]ue largely to an unexplained last-minute money transfer").

278. See id. at 62–63 (observing "LBIE used what is known as the alternative approach to segregation, in which client assets are initially paid into a house account before being transferred into client money accounts at the end of the day").

279. See Fin. Servs. Auth., Client Assets Sourcebook § 7.4.16 (2013), available at http://media.fshandbook.info/content/full/CASS/7/4.pdf (on file with the *Columbia Law Review*) (describing protocol for using "alternative approach" for segregating clients' funds); cf. Becker, supra note 277, at 64 ("The alternative approach was developed as an acknowledgement that large, international institutions are too big and complex to immediately track and process every client money payment, so regulators allowed them to reconcile the accounts at the end of the day instead.").

risk that the firm would somehow use or dissipate client funds before the required end-of-the-day reconciliation.

One can surely imagine the rest of the story: Such "dissipation" is exactly what occurred as the firm became insolvent, leaving the pool of client funds on deposit with LBIE depleted relative to the amounts owed to clients.[280] By all accounts, the effect of the alternative method in the Lehman Brothers bankruptcy came as a surprise not only to clients and customers but also to the regulators themselves.[281] Accordingly, although Lehman Brothers, consisting of entities scattered over the globe, operated as a single firm, whether a client's funds were adequately protected turned on the particular entity that happened to hold them—and that determinant was, as it happened, rather random.[282] U.S. regulation would have provided greater client protections had it applied,[283] but entity-based regulation meant that those protections were moot once the assets were transferred to an entity in another country. These unprecedented events not only revealed certain questionable aspects of U.K. regulation but also demonstrated, for the first time, the ease with which enterprises may shuffle client and customer assets among entities and, more importantly, the limitations of U.S. regulation in preventing and remedying the worst consequences of such occurrences.

We might glean from the Lehman Brothers saga, one of a number of calamitous events during the financial crisis, that some of the most troublesome entity-centric laws and rules have simply gone unused, neither applied to actual facts or extreme circumstances nor, therefore,

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280. See Becker, supra note 277, at 63 ("Upon insolvency there was a significant amount of cash left in the house account—including client money that had not yet been segregated.").

281. The questions raised by the U.K. subsidiary's undersegregation of client funds—in particular, regarding the whereabouts, designation, and return of client funds—ultimately required answering by the U.K. Supreme Court. See In re Lehman Bros., [2012] UKSC 6, [18] (appeal taken from Eng.), available at http://www.supremecourt.gov.uk/docs/UKSC_2010_0194_Judgment.pdf (on file with the *Columbia Law Review*) (ruling on number of questions relating to LBIE's segregation of client assets).

282. Specifically, some U.S.-based clients who had deposited their funds with Lehman's U.S. subsidiary found themselves subject to the troublesome U.K. regulatory regime, rather than the more protective rules that applied to the U.S. subsidiary, simply because, in the final days, the U.S. subsidiary transferred client funds to LBIE, apparently acting without client authorization. See Becker, supra note 277, at 62 (observing shortfall in client assets was "[d]ue largely to an unexplained last-minute money transfer and a failure to correctly segregate" those assets); see also Lehman Client Money Issue Resolved by UK Supreme Court, Practical Law Co. (Mar. 1, 2012), http://us.practicallaw.com/8-518-2963?q=&qp=&qo=&qe= (on file with the *Columbia Law Review*) ("Many of the LBIE 'clients' were US prime brokerage customers, such as hedge funds, and swap counterparties that entered into transactions with Lehman's US affiliates, but which had their posted collateral transferred to LBIE.").

283. U.S. regulation requires that the assets of brokerage customers and clients be segregated at all times from the firm's assets or any other assets. See 17 C.F.R. § 240.15c3-3 (2013) (setting forth customer protection requirements relating to brokers' custody of customer assets).

evaluated for their efficacy. Their shortcomings have become apparent only when, at last, they have been put to the test, in connection with events that had not previously occurred (and that no one had expected to occur) or that had features not present in previous episodes of financial tumult.[284] And we might, in turn, glean from these observations that the phenomenon of deploying aging and little-used regulation to new circumstances is not confined to "tail" events or to the "perfect storm" circumstances of the crisis years.

Once again, the case studies set forth in Part II are instructive. When MF Global declared bankruptcy in 2008 and when Allen Stanford's financial fraud came to light in 2009, U.S. financial services laws and rules that had lain mostly dormant or had been insufficiently examined were put into action. Starting with MF Global, due to the unprecedented circumstance that customer funds were missing from the firm's custodial accounts at the time of the bankruptcy, sleepy CFTC customer-protection rules became relevant for the first time.[285] These rules, premised as they were on the notion that each regulated entity is separate and independent from all other entities, effectively rendered regulators helpless and MF Global Inc.'s customers without recourse.[286] The problems originated with the typical approach to regulation: Although MF Global comprised tens of entities based in far-flung jurisdictions, only a small handful of those entities were subject to regulation as futures or securities brokers.[287] Therefore, only a small handful of entities were obligated to adhere to the customer-protection rules—feeble rules, as it turned out, given the coordinated operations of the MF Global entities.

The Ponzi scheme that Allen Stanford operated through the Stanford Financial Group companies is also illustrative. As described in Part II, in connection with the liquidation of Stanford Investment Bank, Ltd. and Stanford Group Company, the SEC, for the first time ever, sought to compel SIPC to use its authority under SIPA to provide compensation to Stanford's victims, who collectively had lost billions to the

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284. A primary example in this regard is the effect of institutional interconnectedness among "systemically important" institutions. The financial difficulties or insolvencies of Bear Stearns and Lehman Brothers arose, in large part, from the circumstance that large institutions attempted to shed risk in a manner that would allow an institution's failure or near failure to dramatically and adversely affect many other institutions. See Kevin Buehler, Andrew Freeman & Ron Hulme, The Risk Revolution 10–11 (McKinsey & Co., McKinsey Working Paper on Risk No. 1, 2008), available at http://www.mckinsey.com/~/media/McKinsey/dotcom/client_service/Risk/Working%20papers/1_The_Risk_Revolution.ashx (on file with the *Columbia Law Review*) (recounting how "risk transfer markets" led to failure of various large financial institutions).

285. See supra notes 180–187 and accompanying text (describing rules).

286. See supra notes 180–187 and accompanying text (describing how rules worked to disadvantage MF Global's customers).

287. See supra notes 133–138 and accompanying text (summarizing MF Global's organizational structure and regulatory status).

Stanford companies.[288] Due in part to SIPA's having failed to address the possible (and, indeed, likely) relationship among entities employed in a common brokerage enterprise, the federal district court evaluating the SEC's claim found no statutory basis for the SEC's request.[289] As with the CFTC's customer protection rules, lawmakers could have addressed SIPA's inadequacy vis-à-vis multi-entity enterprises long ago, but presumably did not because no circumstances had yet arisen that might have flagged the concerns.

In each of these examples, relevant U.S. statutes and regulations had to be applied in circumstances that had not theretofore arisen and, perhaps, had not theretofore been contemplated, and proved themselves to be too limited in their coverage or, worse, wholly inadequate to further the purposes for which they were created. Notwithstanding that the relevant provisions may have served their respective purposes at the time of their inception, as applied to today's brokerage firms, they revealed themselves to be unsuited to do the job. More precisely, they revealed themselves to be too entity-centric to do the job. That they stood as the only tools that U.S. regulators and courts had at their disposal to address investor injury evinces an atrophy of sorts—a subtle, yet significant, loss of strength and ability that has occurred through disuse and over time, as contexts have changed and as stand-alone entities have become multi-entity enterprises.

This conception helps explain why entity-centrism in financial services regulation has not, until now, received significant scholarly attention. The problems that entity-centrism causes arise in a piecemeal fashion, as crisis events occur and resolution is pursued. In the efforts to formulate regulatory changes to prevent an episode's reoccurrence and aid the injured, the connections among episodes are not sought, let alone evaluated. Each catastrophe, much like the fictional entities at the base of much financial services legislation and rulemaking, is perceived as isolated and stand-alone. To be sure, the catastrophe is deemed connected to events that might possibly occur in the future and that, therefore, necessitate preventive tools, in a type of vertical connectedness among similar events occurring at different times. It is not, however, seen as related to contemporaneous events. This failure to perceive such horizontal relationships—to discern similarities among ostensibly dissimilar contemporaneous incidents—is a failure of policymaking and regulation. Again, the issue, as likely as not, is that no one has paid attention. Let us begin paying attention.

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288. See supra notes 211–212 and accompanying text (describing SEC's role in seeking SIPC compensation for Stanford's victims).

289. See supra notes 213–219 and accompanying text (summarizing SIPC's arguments—with which court agreed—that SIPA coverage was not appropriate in Stanford context).

IV. ESCAPING ENTITY-CENTRISM

Beyond exposing the entity-centrism of financial services regulation, the previous Parts reveal the ways in which entity-centrism prevents regulation from achieving its objective, which primarily is to protect those who seek and receive investment, brokerage, and other finance-related services. Financial services regulation must overcome its current entity-centric premises—that is, its implicit assumptions that financial services providers are stand-alone entities and that entity boundaries are necessarily meaningful for regulatory purposes. An obvious further task, then, is to think critically about how best to move beyond entity-centrism and toward more logical and more effective modes of financial services regulation.

The task is formidable. It requires addressing a number of questions, including what, exactly, is problematic about entity-centrism. As preliminary answers to that question, Parts I and II suggest that, when regulation centers on entities, viewing them as distinct units, it ignores the ways in which entities are related to one another and the ways in which their activities are intertwined.[290] It also fails to acknowledge that the discrete entity, though possessing its own management and ownership structure, may in fact be controlled by something or someone who controls affiliated entities and deploys them all for a common, overarching purpose.[291] Both of these descriptions signal the same phenomenon, namely that financial services firms are enterprises that, whether for good or bad, comprise multiple entities working in coordination with one another. Moreover, sporadic exceptions to regulatory entity-centrism, such as the doctrines of "control person" liability in securities regulation[292] and substantive consolidation in bankruptcy law,[293] serve to confirm this conclusion rather than belie it. The problem with entity-centrism is that it is blind to the regulatory complications that the financial services firm creates.

That observation, however, is not meant to suggest that all manifestations of entity-centrism are problematic. As Part III indicates, to the extent securities regulation, in all its forms, can be viewed as a type of financial services regulation, the need for an entity focus becomes apparent.[294] Securities regulation originates with the entity and, in

290. See, e.g., supra Parts I.B.2–3, II.A.3–4 (describing, in mutual fund and futures brokerage contexts, how regulation inappropriately regards entities as isolated units).

291. See, e.g., supra Part II.B.3 (describing how Allen Stanford used multiple entities to carry out fraudulent activities).

292. See supra note 20 and accompanying text (describing control person liability).

293. See supra notes 165–172 and accompanying text (summarizing substantive consolidation doctrine).

294. See supra notes 261–266 and accompanying text (describing relevance of entities for securities regulation).

particular, the entity's activities in raising capital from third parties.[295] Regulating what an issuer—an entity—may, must, and cannot do in that process has entailed specifying the entity's and its management's disclosure obligations, permissible personal trading practices, and so forth.[296] With the enactment of the Sarbanes-Oxley Act, it now also entails dictating the composition of board committees and the standards by which firm audits must be conducted.[297] To be sure, Sarbanes-Oxley's requirements are entwined with the defining facet of entities—their governance norms and procedures—and, hence, are entity-centric. However, the goal of those requirements, like the primary objectives of the Securities Act and much of the Exchange Act, is to rationalize the (intrafirm) relationship between ownership, on the one hand, and "control," on the other.[298]

Nevertheless, because mutual funds and other registered investment companies are subject to at least some aspects of Sarbanes-Oxley by virtue of their status as publicly held companies, the statute has financial services regulatory implications—and, it would appear, may be hindered by entity-centrism to that extent. For example, the statute provides certain protections for "whistleblower" employees of public companies who report fraudulent conduct or securities laws violations.[299] If an employee of an investment adviser reports fraudulent adviser conduct that caused losses to the shareholders of mutual funds (which, again, are public companies) that the adviser manages, the question arises as to whether the employee would (or should) fall within Sarbanes-Oxley's protections. Although the close relationship between mutual funds and their advisers might suggest an affirmative answer,[300] the adviser is nonetheless a separate entity from the one whose shareholders suffered losses (and is usually a privately owned firm, at that). It is unclear

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295. See supra notes 261–263 and accompanying text (noting securities regulation's focus on protecting shareholders).

296. See Hazen, supra note 263, at 2–4 (describing, in broad strokes, regulatory approaches embodied in Securities Act and Exchange Act).

297. Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (codified as amended in scattered sections of 15, 18, and 28 U.S.C.) (subjecting public companies to various requirements designed to increase corporate accountability and financial disclosures and to prevent accounting fraud).

298. See Elaine A. Welle, Freedom of Contract and the Securities Laws: Opting Out of Securities Regulation by Private Agreement, 56 Wash. & Lee L. Rev. 519, 534 (1999) ("The goal [of the federal securities regulatory structure] has been to protect investors by prohibiting fraudulent and manipulative practices and by requiring disclosure of information material to investment decisions so as to provide investors and the marketplace with sufficient information to make informed investment decisions.").

299. 18 U.S.C. § 1514A (2012) (providing no publicly traded company "or any . . . contractor [or] subcontractor . . . of such company . . . may . . . discriminate against an employee in the terms and conditions of employment because of" employee's engagement in certain protected activities).

300. See supra notes 93–100 and accompanying text (describing relationship between investment adviser and mutual funds it manages).

whether Sarbanes-Oxley's whistleblower provision contemplates that arrangement, although the Supreme Court is poised to decide the matter.[301]

These considerations pose another question, however: How are the circumstances in which entity-centrism "works" to be distinguished from those in which it does not? This is another way of asking how, from a purely practical perspective, we should rethink the contours of financial services regulation. It is a question of which rules, in particular, are in need of reform and a predicate to the further question of how that reform should be carried out. Although that query is sufficiently difficult that further analysis is necessary to address it thoroughly, a few considerations come to mind.

As an initial matter, lawmakers and regulators should be especially vigilant in discerning an unwarranted elevation of the entity in the regulation of financial services activities that typically are pursued by multi-entity enterprises, in which affiliations among entities tend to be manifold and overlapping. The key is to focus on the "movers and shakers," as it were—that is, circumstances in which, as to the enterprise as a whole, there exists a core group of decisionmakers, operating within the parent company or perhaps as owners of the various entities within the group. Regulation should center on these decisionmakers, so that regulatory "form" is dictated by substance—namely, the "who," "how," and "why" behind both financial services activities and the complex multi-entity business structures in which they are situated. If many entities are involved in providing a larger corpus of financial services under the same general name or under common control, then there emerges the likely prospect that they or units within them are being operated as a larger, comprehensive business.

A recent episode of CFTC rulemaking highlights the problems this vigilance could avoid. In particular, in the aftermath of MF Global's bankruptcy,[302] and with the intent of moderating futures brokers' counterparty risk (such as the risk that a counterparty will become insolvent), the agency adopted a new rule imposing counterparty concentration limitations.[303] Under the rule, a futures broker is prohibited from entering into reverse repurchase agreements with any single counterparty (yes, an entity) beyond the point at which the securities the broker

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301. The Supreme Court has granted certiorari and will proceed with the case in late 2013. Lawson v. FMR LLC, 670 F.3d 61 (1st Cir. 2012), cert. granted, 81 U.S.L.W. 3648 (U.S. May 20, 2013) (No. 12-3); see Lawrence Hurley, Supreme Court Agrees to Hear Fidelity Whistleblower Case, Reuters (May 20, 2013, 10:24 AM), http://www.reuters.com/article/2013/05/20/us-usa-court-fidelity-idUSBRE94J0F020130520 (on file with the *Columbia Law Review*) (reporting Supreme Court's grant of certiorari in *Lawson* and summarizing facts of case and issue to be decided).

302. See supra Part II.A.3–4 (describing regulatory failings that became apparent after bankruptcy).

303. 17 C.F.R. § 1.25(b)(3)(v) (2013).

purchases from the counterparty under the agreements exceed twenty-five percent of the value of the assets that the broker holds in segregation for customers.[304] Incredibly, in adopting the rule the CFTC evinced no recognition that any particular counterparty inevitably will be part of a multi-entity enterprise and that, once the magnitude of a broker's reverse repurchase arrangements with one counterparty threatens to breach the twenty-five percent threshold, the broker and that enterprise could readily circumvent the rule's strictures by simply substituting another entity within the enterprise as the nominal counterparty. Although the CFTC later took steps to close this loophole,[305] it did so without acknowledging the broader challenges posed by its entity-centric approach to rulemaking. Without that recognition, however, we should expect that its—and other agencies'—rulemaking will continue to produce loopholes to be patched or other deficiencies to be remedied later on, ensuring a regulatory process that is both blinkered and inefficient.

Other signals for policymaking vigilance include circumstances in which the goals of a particular brand of financial services regulation cannot be said to be corporate governance goals. In other words, if regulation is not directed at protecting shareholders from management or otherwise pursued in the name of managerial accountability, then the rationale for focusing regulation on the entity is necessarily muted. This characterization of at least some financial services regulation squarely encompasses the many types of service providers who facilitate transactions in securities, futures contracts, and other investment instruments—service providers who, in other words, play an intermediating role in the financial markets. Regardless of whether a firm is a broker-dealer, an investment adviser, a futures commission merchant, a commodity trading advisor, a swap dealer,[306] or one of any number of other types of intermediaries operating in the securities and futures markets and

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304. See Investment of Customer Funds and Funds Held in an Account for Foreign Futures and Foreign Options Transactions, 76 Fed. Reg. 78,776, 78,788–89 (Dec. 19, 2011) (codified at 17 C.F.R. pts. 1, 30) (describing rationale for setting concentration limit at twenty-five percent of value of segregated customer assets).

305. In 2012, the CFTC proposed to close the loophole by amending the rule to require that an FCM "must aggregate the value of the securities purchased from two or more different counterparties . . . if the counterparties are under common control or ownership." Enhancing Protections Afforded Customers and Customer Funds Held by Futures Commission Merchants and Derivatives Clearing Organizations, 77 Fed. Reg. 67,866, 67,888 (Nov. 14, 2012) (to be codified at 17 C.F.R. pt. 1).

306. A swap dealer is a person who is in the business of serving as a counterparty to swap agreements. See Swap Dealer, Investopedia, http://www.investopedia.com/terms/s/swap-dealer.asp (on file with the *Columbia Law Review*) (last visited Oct. 7, 2013) (defining "swap dealer"). Swap dealers, like futures commission merchants, commodity trading advisors, and commodity pool operators, are regulated by the CFTC under the Commodity Exchange Act. See Registration Information for Swap Dealers and Major Swap Participants, Nat'l Futures Ass'n, http://www.nfa.futures.org/NFA-registration/sd-and-msp/index.HTML (on file with the *Columbia Law Review*) (last visited Oct. 7, 2013) (summarizing regulatory requirements applicable to swap dealers).

beyond, the entity is not a relevant guidepost in formulating regulatory obligations because that regulation is not directed at adjusting the balance of power among the core corporate constituencies.[307] Its aims, rather, are to protect consumers of financial services and to ensure the integrity of the markets.

Finally, lawmakers should have heightened skepticism of entity-centrism in regulation that elevates the importance of an entity that is used as a mechanism of convenience to group and order those who would be separately entitled to regulatory protections. This indicator is present anywhere a group of clients or their assets are regarded as a single "thing" by virtue of pooling arrangements, and it describes most investment entities, whether public (such as mutual funds) or private (such as hedge funds and private equity funds). If an entity is used as a tool, after all, then its relevance lies not in its role in bringing together entrepreneurs and investors (whose relationship is the focus of corporate governance doctrine) but, rather, in its altering the form of processes or procedures that, in substance, could proceed in the entity's absence.

Taken together, these indicia suggest that various parties need to be particularly alert to entity-centrism—and, further, take steps to address it—in regulatory contexts in which the entity itself has no function or meaning apart from its role as a facilitator. This is particularly true for lawmakers and regulators, who are accustomed to thinking of regulatory subjects in terms of entities, and for providers of financial services, who are able to realize efficiencies both by pooling (in entities) consumers of their financial services and by separating (into entities) the assets and liabilities associated with particular tasks or functions. After all, an entity can be regarded as a "mechanism" or facilitator only when it can be viewed from a perspective outside of itself and can be controlled and manipulated by something beyond itself.

Of course, regulatory approaches that partly mute entity boundaries have long been staples of particular financial services regulatory domains, particularly banking regulation, which might suggest that financial services regulation has already identified and addressed the concerns that multi-entity firms generate. For example, under the Bank Holding Company Act of 1956 (BHCA),[308] the parent companies ("bank holding companies" or BHCs) of entities that are U.S. banks are subject to regulation by the Federal Reserve, which provides "consolidated supervision" of both the parent company and its subsidiaries.[309] In addi-

307. See supra notes 249–265 and accompanying text (discussing distinction between "core" securities regulation and financial services regulation).

308. Pub. L. No. 84-511, 70 Stat. 133 (codified as amended at 12 U.S.C. §§ 1841–1852 (2012) and in scattered sections of 26 U.S.C.).

309. See Saule T. Omarova & Margaret E. Tahyar, That Which We Call a Bank: Revisiting the History of Bank Holding Company Regulation in the United States, 31 Rev. Banking & Fin. L. 113, 118 (2011) (observing under BHCA any company owning or

tion, if an entity within a multi-entity organizational structure becomes insolvent or undercapitalized, banking regulation requires that other entities within that structure provide certain types of financial support to the troubled entity.[310]

To be sure, banking regulation might seem to preclude a BHC from pursuing many types of financial services activities. Among other things, BHCs generally are not permitted to hold large ownership stakes in businesses that pursue nonfinancial or certain non-banking-related financial activities,[311] thereby distinguishing them from the financial services activities that are the focus of this Article. However, BHCs that meet certain capitalization and management requirements and that, therefore, qualify as "financial holding companies" or "FHCs" may engage in nonbanking financial activities, such as underwriting and dealing in securities.[312] Furthermore, the Dodd-Frank Act applies a version of the BHCA's model of regulation to "systemically important financial institutions" or "SIFIs"—that is, enterprises that are sufficiently large or connected to other financial enterprises that their insolvency would threaten the stability of the financial system.[313] Perhaps, then, the financial services world has already overcome entity-centrism.

That conclusion would be unwarranted. First, the BHCA's regulatory approach is limited because it governs banks and their affiliates and, therefore, does not address the entity-centrism that pervades the nonbanking regulatory domains this Article discusses. Second, when one looks more carefully at the requirements to which banks and their affiliates are subject under the BHCA, it becomes apparent that entity-centric difficulties persist even in the banking context because subsidiaries in that context, as in other financial services contexts, generally remain subject to regulation based on the specific functions of discrete

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controlling U.S. bank must "register with, and become subject to consolidated regulation and supervision by, the Federal Reserve").

310. See Lissa Lamkin Broome, Redistributing Bank Insolvency Risks: Challenges to Limited Liability in the Bank Holding Company Structure, 26 U.C. Davis L. Rev. 935, 960–67 (1993) (summarizing cross-guarantee provision of Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) and controlling company guarantee provision of FDIC Improvement Act of 1991); Jackson, supra note 65, at 536–37 (describing FIRREA's cross-guarantee provision).

311. See 12 U.S.C. § 1843(a) (setting forth restrictions on banks' nonbanking activities).

312. See id. § 1841(o)(9) (setting forth requirements BHC must meet to be "well managed"); 12 C.F.R. § 225.2(r)(1) (2013) (setting forth requirements BHC must meet to be "well capitalized"); Omarova & Tahyar, supra note 309, at 119 (describing thresholds BHC must meet to be deemed so-called financial holding company).

313. See Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 113, 124 Stat. 1376, 1398–402 (2010) (codified at 12 U.S.C. § 5323) (setting forth regulations for certain nonbank financial companies); see also Omarova & Tahyar, supra note 309, at 127 (observing Dodd-Frank Act "effectively expands the BHCA model of regulation and supervision . . . to all financial institutions designated as 'systemically important' and thus subject to consolidated supervision by the Federal Reserve").

entities.[314] That is, regulation of the subsidiaries remains based on entity boundaries. Third, to the extent that nonbanking financial enterprises, such as FHCs and SIFIs, are similarly subject to consolidated regulation, that circumstance does not affect the regulation governing enterprises that cannot be FHCs (because they are not subject to the BHCA) or that are not sufficiently large to be deemed SIFIs. Put another way, it does not affect, let alone remedy, the entity-centrism that characterizes the regulation of the overwhelming majority of financial services enterprises. Accordingly, despite policymakers' attempts to overcome entity-centrism in regulating banking and systemically important enterprises, much work remains to be done.

All of this does not, however, address what a new mode of regulation might look like, a challenge that must be reserved for future projects. There are many avenues, indeed. One conclusion possibly arising from the case studies presented in Part II, for example, is that regulation should entail subjecting not only the relevant subsidiaries *but also* the parent entity to regulatory requirements. Alternatively, but similarly, perhaps "regulation" should mean regulation of the enterprise in its *entirety*, encompassing not just the parent entity but also other affiliated entities. The important component of both of these alternative approaches is that the entities and individuals that stand in a controlling position vis-à-vis the regulated subsidiaries would fall squarely within regulation's ambit, notwithstanding that those parties may not themselves provide financial services.

In the contexts of both MF Global[315] and the Stanford Financial Group,[316] such an "enterprise-based" regulatory approach likely would have forestalled the difficulties that ultimately arose. For example, by directly subjecting a parent entity, such as MF Global Holdings Ltd., to the regulatory regime to which the service-providing subsidiaries are subject, the assets of the subsidiary would, almost by definition (and certainly by express mandate), encompass the parent entity's assets.[317]

314. See Omarova & Tahyar, supra note 309, at 119–20 ("[A]ll functionally regulated non-bank BHC subsidiaries—including securities broker-dealers, investment advisers, insurance companies or commodity futures professionals—are regulated and examined by the applicable primary regulatory agency, such as the [SEC], [CFTC] or state insurance regulators.").

315. See supra Part II.A (describing entity-centrism in MF Global context).

316. See supra Part II.B (describing entity-centrism in Stanford Financial Group context).

317. Such an approach would accord with, but arguably go beyond, certain rules in the banking regulatory context. Under these rules, in the event of a banking subsidiary's insolvency, entities affiliated with the subsidiary must provide certain types of financial support to the subsidiary. This requirement "modif[ies] the concept of limited liability and corporate separateness." Broome, supra note 310, at 938; see Jackson, supra note 65, at 511 (discussing, in financial holding company context, "legal requirements that holding companies guarantee . . . the solvency of their regulated subsidiaries," such as through

Moreover, if the parent entity were regulated in the same manner as the service-providing subsidiaries, then "substantive consolidation," whereby multiple entities within an enterprise effectively are liquidated as though they were a single entity,[318] would be considerably more workable than at present because both the parent entity and the subsidiary presumably would be subject to the same bankruptcy liquidation procedures.

An enterprise-based regulatory approach could also more effectively further SIPA's objectives, including in circumstances involving Stanford-like fraud. Applicable rules might, for example, specify that if any two or more entities within the group perform functions together that if performed by a single entity would subject the entity to SIPA's requirements, then the group as a whole will be subject to SIPA. Accordingly, the assets of the entire group would be available to compensate victims of whatever fraud the entities might jointly perpetrate or other losses the entities might jointly cause. Similarly, if regulation were to apply to the entire group, then regardless of whether a brokerage subsidiary creates a fund or other pool through which to provide services, that new entity, too, will automatically be captured by SIPA.

A move toward an enterprise-based regulatory approach in the private fund (e.g., hedge fund) and public fund (e.g., mutual fund) contexts[319] would similarly be a move toward viewing the investment adviser and the funds it manages as an enterprise. In both contexts, after all, the fund is part of an enterprise, one whose constitutive entities are connected to one another not through ownership but, instead, through control in fact: But for the adviser, the entity would not exist, and, without the adviser, the entity would not continue to exist. Accordingly, as suggested in Part I,[320] a new mode of regulation would acknowledge that the fund is controlled by something beyond itself—the investment adviser—and that the fund is really nothing that is not reducible to its investment adviser (and the adviser's investment strategy), on the one hand, and its disparate investors, on the other. In this alternative approach to regulation, the adviser would have the primary regulatory duties, and the investors would be the primary beneficiaries of those duties.

It is also worth considering whether the goals furthered by enterprise-based regulation could be achieved more efficiently through more limited measures. For example, rather than subject a parent entity to regulation, perhaps CFTC rules could simply require that, for discrete

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"recapitaliz[ing] insolvent subsidiaries or . . . compensat[ing] government authorities for losses that failed subsidiaries impose on public claimants . . . or public insurance funds").

318. See supra notes 165–172 and accompanying text (describing substantive consolidation doctrine).

319. See supra Part I.B.1–2 (describing difficulties arising from entity-centrism in these contexts).

320. See supra Part I.B.1–2 (suggesting alternative approaches for regulating investment advisers and mutual funds).

purposes, a subsidiary's proprietary assets are deemed to include those of the parent entity. Or, perhaps the rules could specify that a parent entity and its regulated subsidiary may be substantively consolidated upon bankruptcy, notwithstanding that the entities involved are otherwise subject to different bankruptcy liquidation rules. Another approach might be to direct regulation at the various categories of risks the different entities in an enterprise create. For example, if one entity has the authority to use an affiliated entity's assets for business or trading purposes and, therefore, might be said to act jointly with the affiliated entity in placing the affiliate's proprietary capital or customer assets at risk, then both the entity and the affiliated entity could be subject to targeted regulation aimed at protecting those assets.[321]

Beyond the regulatory arenas that this Article highlights, future projects might also involve analyzing the Commodity Exchange Act or the financial services components of the Exchange Act, such as the laws and rules governing broker-dealers, to catalogue provisions that assume a stand-alone entity and to formulate an efficient means of dislodging that assumption or muting its effects, such as through definitional amendments. Yet another project might extend the analysis of entity-centrism more directly into the realms of banking or insurance regulation, where, as in other financial services arenas, multi-entity enterprises dominate. Still another might evaluate whether entity-centrism is more pronounced or more harmful in particular regulatory contexts, with the objective of informing policymaking priorities. Finally, it will be important to study the relative costs and benefits of less entity-centric regulation, with a view toward analyzing whether the relative efficiencies of current regulatory approaches might, in at least some contexts, ultimately justify their shortcomings.

CONCLUSION

Focusing on discrete examples and case studies, this Article brings to light the problems arising from entity-centric laws and rules. It also shows that entity-centrism can be observed in other financial services regulatory contexts and, as a relatively consistent affront to common sense, ties together circumstances that might otherwise seem unrelated. This is not to say, however, that entity-centrism appears in all regulatory contexts or that an overhaul of all laws and rules necessarily is in order. Yet in many regulatory arenas, entity-centrism is prevalent enough, and its

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321. This proposal is reminiscent of the suggestion in the banking context that regulation should be oriented around risk. See Schooner, supra note 5, at 478–87 (proposing "regulatory model built around risk"). For example, "if the activities of a bank affiliate could cause a loss to the bank insurance fund, the laws enacted to protect the fund must reach that activity, or impose the necessary firewalls or other protections to ensure that those activities do not create that risk." Id. at 480.

deficiencies pervasive enough, to warrant a thoughtful, concerted focus on it.

To "focus" on it suggests at least two things. First there needs to emerge a recognition of what financial services regulation is—that is, what its relationship is to the "securities laws" or the "commodities laws." The laws and rules governing financial services are subsumed within broader bodies of laws and rules—broker-dealer regulation is set forth in the Exchange Act, for example—and they also extend beyond those other bodies of laws and rules; not all of financial services regulation is found in the securities statutes, for example. That circumstance means that it is necessary to reconsider longstanding assumptions about the homogeneity of laws and rules united by a single subject heading (but perhaps not much else). The securities laws do two very different jobs. On the one hand, they specify aspects of the relationship among the constituents in a single entity—namely, owners (investors) and management—and, in particular, specify what protections need to be given to owners in acquiring that status. In that sense, aspects of the securities laws are entity-centric, and rightly so. On the other hand, the securities laws regulate the behavior of those who facilitate investors' activities in the securities markets. That is, they regulate securities-related financial services, and, in that process, the entity is not relevant.

Second, scholars and regulators will need to dedicate their efforts to formulating new approaches to financial services regulation, keeping in mind that laws and rules are entity-centric in various ways. Some fail to recognize that financial services providers use entities as mere mechanisms or instruments in providing their financial services, changing the way in which the service is delivered but not the service itself. Others fail to reflect that a "firm" need not be a single entity but instead may consist of two, three, or hundreds of entities that provide financial services together, operating as a single unit ultimately controlled by a core group of decisionmakers. The effort also needs to keep in mind the different ways in which entity-centrism pervades a range of contexts, such as investors' and others' understanding of the boundaries of the regulatory subject,[322] and courts' adjudication of claims against an investment adviser based on the conduct of a mutual fund the adviser manages[323] or claims by an adviser's employees for whistleblower protection based on harm the adviser caused the mutual fund's (rather than the adviser's) shareholders.[324]

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322. See supra notes 86–87 and accompanying text (noting investors' apparent confusion about organizational structure of firms from which they seek financial services).

323. See supra notes 103–104 and accompanying text (noting courts have adopted entity-centric approaches to decide cases involving mutual funds).

324. See supra notes 299–300 and accompanying text (noting entity-centrism impedes efficacy of Sarbanes-Oxley Act, as statute applies to mutual funds).

Given the complexities of financial services regulation, of course, constructive new regulatory approaches cannot be advanced in the abstract. However, it should be clear that overcoming regulation's entity-centrism does not entail defeating important goals of corporate governance. For example, the project does not, nor should it, have any implications for limited liability principles protecting shareholders. Nor does it or should it expand or reshape the generally established conditions for piercing the corporate veil, as that doctrine traditionally has been understood.[325] The important part of rethinking regulation is the recognition of the forces that cause it to fail. For it is that recognition that permits moving beyond piecemeal, one-off fixes for crisis events and newly discovered problems, to more encompassing, and more coherent, financial services regulatory approaches. In this day and age, with ever more complex corporate structures, only such approaches will sustain the work that financial services regulation is supposed to do.

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325. See Smith & Williams, supra note 14, at 220–25 (summarizing veil piercing doctrine).

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