CERTIFIED FINANCIAL PLANNER BOARD OF STANDARDS, INC.

ANONYMOUS CASE HISTORIES
NUMBER 30664

This is a summary of a Settlement Agreement entered into at the February 2018 hearings of the Disciplinary and Ethics Commission ("the Commission") of Certified Financial Planner Board of Standards, Inc. ("CFP Board"). The conduct at issue in this case occurred after January 1, 2009. The Rules in effect at that time under the *Rules of Conduct* were Rules 1.1 through 6.5.

I. Issues Presented

Whether a CFP® professional ("Respondent") violated CFP Board's *Standards of Professional Conduct* when he: (1) engaged in private securities transactions without informing his employer, in writing, in violation of NASD and FINRA rules; (2) invested his money, and the money of a work colleague, into a mortgage-lending fraud; (3) was the subject of a FINRA investigation and regulatory suspension; and (4) was the subject of a state DFS regulatory fine.

II. Findings of Fact

Respondent became a CFP® professional in January 2003 and has maintained his certification since that date. Respondent holds Series 7 (General Securities Representation) and Series 66 (Uniform Combined State Law) licenses.

Respondent was registered with Firm ABC ("ABC") in City X for the first three years of his career, from August 2000 to November 2003. Between January 2004 and April 2009, he worked for Firm DEF ("DEF") in City Y. Respondent then worked in suburban Y as a registered representative of Firm GHI ("GHI") from April 2009 until his termination in January 2017. GHI announced in a Form U5 Notice of Termination that Respondent had been discharged for cause: "registration was terminated due to the disciplinary action taken by FINRA as a result of his involvement with private securities transactions."

After leaving ABC in November 2003, Respondent went to work as a benefits consultant for an Insurance Agency ("IA") in city Y. IA's President was a longtime friend of Respondent. The President's sister ("PS") also worked at IA.

Private Securities Transactions Involving a "Business Venture" (2006-2008)

In 2005, Respondent met with a client of IA named Customer A to help him purchase life insurance, disability insurance, and health insurance. During the course of their dealings, Customer A described a business venture ("BV") he'd formed. BV supposedly matched homeowners who had defaulted on their home mortgages with individual investors who were willing to provide loans that could help the homeowners pay down their delinquent debt and remain in their homes. BV claimed that it would find mortgage companies that would refinance the homes, and then money from the refinancing was ostensibly going to be used to repay the individual investors' loans at high interest rates.

In 2006, Respondent began investing his own funds in BV. He initially invested approximately $50,000, and received a return of his principal, plus interest. In late 2006, PS expressed interest in investing in BV. Respondent suggested that she and he pool their funds to make additional investments in BV that would be held in Respondent's name. Respondent agreed to forward PS her portion of any payment she received from the joint investment. During 2006, they jointly

invested $160,000, $100,000 of which came from Respondent. In 2006 and 2007, PS's contributions totaled approximately $60,000, and Respondent's total contributions were about $150,000.

In exchange for each investment, Respondent received a note issued by BV which had maturity dates of nine months or longer. BV made three payments to Respondent during 2008 in January, March, and April. Respondent forwarded a total of $5,640 of those payments to PS representing her share. Soon thereafter, BV was "exposed as a fraud" and the balance of their joint investment was lost.

Respondent suggested to CFP Board that he invested in BV for altruistic reasons:

> I was impressed by [BV], particularly with the opportunity to help others while investing my money and, unfortunately, became an investor in 2006. I later learned that BV was not a legitimate company, and I lost tens of thousands of dollars in Customer A's fraudulent scheme.

Respondent provided CFP Board with a copy of a December 2007 Loan Agreement and Promissory Note between Customer A and BV ("Borrowers") and IA ("Lender"). According to the terms of the Loan Agreement, the Lender loaned $52,00 to Customer A that did not yet exist. The "Collateral" section of the three-page Loan Agreement stated:

> Within 30 days after the execution of this Agreement, the Borrowers shall provide a copy of said life and disability insurance policy to the Lender with the inclusion of the Lender as beneficiary. All loans are secured by mortgages on properties as well as deeds in lieu of foreclosure in the name of [BV] and the lender. Property locations and mortgagors cannot be revealed in order to protect the privacy of mortgagors under federal and state privacy laws.

It is not clear from the record that Respondent's loans to Customer A and BV were provided on terms that were equally usurious. PS said Customer A had promised her and Respondent "interest on the investments in an amount in excess of 50% per annum." The terms contained in BV's Loan Agreement with IA and the assertions of PS suggest that Respondent's investment in BV might have been less altruistic than Respondent has suggested.

As a CFP® professional and a registered broker, Respondent should have noticed the red flags and conducted additional due diligence before he invested his own funds and the funds of a colleague in BV.

Respondent told CFP Board and staff that Customer A subsequently became the subject of a criminal investigation by the State's Attorney General. Respondent said he personally testified before a state grand jury in April 2009 as one of numerous victims of Customer A's "fraudulent loan scheme." Respondent noted that Customer A had also been "charged separately with fraudulently using a child care center to cheat the state out of more than $400,000."

FINRA eventually ruled that the BV notes constituted securities, and that Respondent's investments between 2006 and 2008 constituted private securities transactions. While Respondent was working for IA, he was also working as a registered representative of DEF. Pursuant to FINRA Rule 3040 and DEF's internal policies and procedures, Respondent was obliged to inform DEF about all of the outside investments in which he was participating. As discussed below, Respondent failed to provide his firm with the prior written notice or obtain the advanced written approval that was required.

Private Securities Transactions Involving Company X

In 2007, Respondent learned of an investment opportunity in a "friends and family" round of financing for a start-up company called Company T. When PS learned about this investment opportunity, she asked to participate in

Respondent's investment. In January 2007, Respondent invested $100,000 in Company X, including $56,000 provided by PS. As before, they agreed to distribute any returns on their joint investment on pro rata basis. In exchange for this investment, Respondent received a stock certificate issued in his name documenting the number of shared purchased. According to a "Form D—Notice of Sale of Securities" filed by Company X with the SEC, Respondent's shares accounted for at least 10% of the outstanding shares of the company. The share certificates issued by Company X were eventually found by FINRA to constitute securities.

This 2007 joint investment of $100,000 represented Respondent's only investment in Company X. The investment never yielded any dividend payments or other profits to the joint investors. By 2008, it had become increasingly clear that the Company X investment was almost worthless.

PS's Lawsuit against Respondent

PS and IA grew increasingly disgruntled about the financial losses that PS suffered from her joint investments with Respondent. In mid-2008, eight FBI agents visited the offices of IA, causing Respondent to become concerned. Later, when he caught PS's father rifling through Respondent's personal files, his concerns increased. Respondent claims that he resigned from IA shortly thereafter.

In April 2009, Respondent left DEF and became registered with GHI. GHI was affiliated with GHI Finance Group, which also included "GHI National Life Insurance." Respondent's affiliation with GHI occurred at approximately the same time he left IA.

Respondent has asserted to CFP Board that PS and IA undertook a series of unfair and defamatory actions to pressure Respondent to reimburse PS for her substantial investment losses. In July 2010, an attorney for PS contacted Respondent's attorney, saying that he'd been retained to recover $168,000 that she had provided to Respondent for investment.

In November 2010, PS and IA filed a lawsuit against Respondent in State Court alleging fraud, conversion, and breach of fiduciary duty relating to PS's and IA's investments with BV and Company X.

In January 2011, Respondent signed a Settlement Agreement and Release which resolved the case that had been pending in court for only two months. Respondent agreed to pay $56,000 to PS, which equaled the precise amount that she had provided Respondent in January 2007 for investment in Company X. The Settlement Agreement and Release provided Respondent with sole ownership of the Company X investment. PS and IA agreed to withdraw the allegations, close the case, and release Respondent from any and all claims related to the losses IA and PS had suffered in the joint investments in BV and Company X.

GHI initially decided it did not need to file a Form U4 to disclose Respondent's January 2011 settlement with IA and PS within 30 days of the settlement date, apparently because GHI did not view the lawsuit to be a "consumer-initiated, investment-related civil litigation." However, in April 2014 GHI filed a Form 27530 Disclosure and Complaint Filing to disclose what it considered to be a non-firm-related civil litigation matter. By making this filing, GHI finally added to Respondent's CRD record a disclosure which publicly revealed that Respondent had paid $56,000 to settle the PS/IA litigation in January 2011. Respondent added the following note to his CRD record: "I do not consider this report to be required. However, I'm reporting it in an abundance of caution."

CFP Board's Investigation of the PS Grievance (2010-2012)

On September 16, 2010, approximately one month before PS and IA filed their November 2010 lawsuit, PS filed a formal grievance against Respondent with CFP Board. The lengthy complaint included a three page narrative containing extensive allegations of wrongdoing, including the following:

1. that Respondent had held himself out as having expertise in financial investments;
2. that PS had trusted Respondent because of a long-term family relationship;
3. that Respondent had pressed hard to convince PS to invest her personal funds and IA funds in BV and Company X;
4. that Respondent had failed to provide PS with any shares, promissory notes, or other materials that documented her investments;
5. that Respondent may have been an active participant in Customer A's fraud; and
6. that Respondent may have "improperly converted her funds for his own purposes."

Respondent and his attorney provided an extensive defense to these allegations and produced evidence suggesting that PS and IA may have exaggerated their allegations to gain leverage against Respondent in extracting a favorable settlement.

In July 2011, PS sent a letter to CFP Board staff which stated:

> [Respondent] and I have settled the dispute that gave rise to both my lawsuit and the complaint made to [CFP Board]. I am no longer interested in pursuing my complaint against [Respondent] with the Board. Accordingly, I would like to retract it and hereby request that it be dismissed.

CFP Board continued its investigation of Respondent for several more months in order to protect the public interest. In October 2011, the staff requested additional information, but did not seek any specific documents. In November 2011, Respondent provided a three-page response letter. In July 2012, CFP Board staff sent Respondent a dismissal letter stating that CFP Board had completed its investigation of the 2012 PS Grievance and decided to close the matter without further action. The letter noted, however that CFP Board reserved the right to reopen its investigation of the matter "if deemed appropriate."

Respondent's Criminal Conviction

In April 2013 Respondent was arrested for assaulting his ex-girlfriend. According to the Affidavit of Probable Cause to the Criminal Complaint, Respondent got into an argument with the mother of his child over the manner in which he was securing their one-year-old son in a car seat. She claimed that when she entered the car to adjust her son in the car seat, Respondent placed her in a "choke-hold." She said that she managed to break away, retrieve her son, and run inside to call the police. The police detective's affidavit stated:

> As a result of the altercation, [the ex-girlfriend] had visible injuries around her neck consistent with her statement to police. These injuries were photographed on scene. Due to [Respondent's] actions, he was placed under arrest and transported to police headquarters.

In December 2013, Respondent attended his criminal hearing and plead guilty to two misdemeanor crimes:

> **Count 1:** The original charge in Count 1 was reduced from Simple Assault to **Disorderly Conduct**;
> **Count 2:** This Charge remained unchanged, and he pled guilty to "**Harassment/Strike, shove/kick etc.**"—"Actor commits the crime of harassment when, with intent to harass annoy or alarm another, the person strikes, shoves, kicks or otherwise subjects the other person to physical contact, or attempts or threatens to do the same."

Respondent was sentenced to two 90 day probations and two fines for $75. The probation was ordered to run consecutively, as opposed to concurrently, so Respondent was essentially ordered to serve a total 180 days of probation. He was also required to pay a total of $150 in fines, plus a total of $175.25 in Court Costs and Hearing Fees.

Respondent did not disclose these misdemeanor convictions to CFP Board in writing within 30 calendar days of his December 2013 conviction, as required under Article 13.2 of the *Disciplinary Rules*. In December 2014, more than one year after his conviction, Respondent completed CFP Board's Ethics Questionnaire as part of his effort to renew his CFP® certification. He answered "Yes" to the question which asked whether he had been "charged with or…convicted of a misdemeanor (other than a minor traffic violation) within the last five years." Respondent provided a narrative description of the offense, which including the following statement: "I plead guilty to disorderly conduct & 6 months' probation. Even though I did nothing wrong, I accepted the reduced charge to try to get this unfortunate incident behind me."

In February 2015, CFP Board sent Respondent a Notice of Investigation ("NOI") asking him to produce documents and information relating to his misdemeanor convictions. In March 2015, Respondent provided a one page response describing his version of events that led to the conviction. He mentioned his original charge of Simple Assault in Count 1 was pleaded down to Disorderly Conduct. Respondent was also convicted of a criminal misdemeanor in Count 2—involving the charge of "Harassment/Strike, shove, kick, etc."

The conduct that resulted in Respondent's misdemeanor conviction for Disorderly Conduct and Harassment was not financial-related, and it did not involve Respondent's professional activities.

In June 2015, CFP Board sent Respondent a "Dismiss with Caution" letter which stated:

> CFP Board has completed its review of the 2013 Simple Assault Charge, Harassment Conviction, and Disorderly Conduct Conviction. Accordingly CFP Board is closing its review of the matters without further action. CFP Board does, however, caution you as to the importance of adhering to Rule 6.5, which states: "A certificant shall not engage in conduct which reflects adversely on his or her integrity or fitness as a certificant, upon the CFP® marks, or upon the profession." CFP Board also reminds you of your duty to report criminal conviction or professional discipline, in accordance with Article 13.2. This letter is not considered a form of discipline. This letter may be taken into consideration by the Disciplinary and Ethics commission in determining if any appropriate action should be taken if disciplinary violations occur in the future.

Respondent's Regulatory Action for "Failure to Disclose" (2015)

In January 2015, State W's Department of Financial Services ("DFS") initiated an investigation of Respondent's activities in connection with his application for a non-resident insurance license. DFS found that Respondent had failed to disclose his December 2013 misdemeanor convictions, even though applicants were specifically required to disclose criminal convictions. In May 2015, DFS imposed a Civil and Administrative Penalty/Fine of $750 on Respondent for violating the DFS disclosure rules.

Respondent's FINRA Settlement and Three-Month Suspension (January 2017)

In January 2017, Respondent entered in a Letter of Acceptance Waiver and Consent ("AWC") with FINRA in which he agreed to a three-month suspension from associating with any member firm in any capacity, and a fine of $5,000. FINRA found that Respondent violated NASD Rules 3040 and 2110 when he a) failed to provide his firm (DEF) with advanced notice in writing of his participation in the BV loans and Company X Form D Private Offering; and b) participated in these two private securities transactions without first obtaining written approval from his firm granting him authorization to participate in the investments.

NASD Rule 3040 prohibited associated persons from participating in any manner in a private securities transaction without providing prior written notice to their firm and, in some circumstances, without first receiving the firm's written approval. NASD Rule 2110 required persons registered with a FINRA member firm, in the conduct of their business, to observe high standards of commercial honor and just and equitable principles of trade.

In the AWC, FINRA found (and Respondent consented to the findings) that the notes and agreements that Respondent received from BV in 2006 and 2007, and the shares received from Company X in 2007, were "securities." The AWC also confirmed that Respondent's investments in these entities constituted "private securities transactions" that he needed to disclose to his firm, in writing, prior to his participation.

The FINRA AWC contained findings which suggest that PS was the initiator of her involvement in the BV investment; that Respondent had not been acting as her financial advisor; that he had not recommended the investment to her; and that he had not received a commission for bringing her in to the investment. FINRA also found that PS, not Respondent, had initiated her involvement in the Company X investment. FINRA did not identify any rules that were violated by Respondent's willingness to pool his own resources with PS's, or his willingness to hold the joint investments exclusively in his own name. However, it found that Respondent's failure to provide advanced written notice to DEF, and his failure to obtain advanced written approval from DEF, constituted separate violations of NASD Rules 3040 and 2110.

Respondent learned that FINRA had accepted and finalized his AWC in January 2017. However, he did not disclose his FINRA suspension to CFP Board in writing within 30 calendar days of learning of this professional discipline, as required under Article 13.2 of the *Disciplinary Rules*.

Respondent's Termination (January 2017)

Respondent had left DEF in April 2009, soon after PS began pressuring him to reimburse her for the losses she'd suffered from the joint investments in the private securities transactions. Respondent became registered with GHI in April 2009, and remained there until 2017.

In January 2017, Respondent was "discharged" by GHI based upon the following specified reasons: "Disciplinary action taken by FINRA resulting from involvement with private securities transactions." In a Form U5 Notice of Termination, GHI noted that FINRA had scheduled Respondent's suspension to last from February 2017 to May 2017.

In February 2017, GHI sent Respondent a letter informing him that it had cancelled his FINRA registration and state securities licenses. It also confirmed that GHI Insurance was cancelling his state variable appointments. Respondent has not been registered with a brokerage firm since his termination in January 2017.

CFP Board Investigation

In March 2017, Respondent filed an application to renew his CFP® certification. He answered "Yes" to the questions asking whether he had ever been:

a. terminated for cause;
b. subjected to an investigation by a self-regulatory organization;
c. suspended from having a professional license; or
d. convicted of a criminal misdemeanor

CFP Board's Ethics Questionnaire instructed CFP® Professionals to provide a detailed narrative describing the principal facts and outcome of each investigation or proceeding, including the date the investigation or proceeding was initiated. Respondent provided the following narrative: "FINRA imposed a $5,000 penalty & 3 mos suspension starting Feb [] 2017."

In April 2017, CFP Board sent a NOI informing Respondent it had opened a new investigation relating to his employment termination and the subsequent FINRA suspension he'd disclosed on the Ethics Questionnaire. In May 2017, Respondent provided a response to the NOI which consisted of a two-page letter and four documents.

Conclusion

Article 13.1 of the *Disciplinary Rules* provides that a letter or other writing from a governmental or industry self-regulatory authority to the effect that a Respondent has been the subject of an order of professional discipline by such authority shall conclusively establish the existence of such professional discipline for purposes of disciplinary proceedings and shall be conclusive proof of the basis for such discipline by the Respondent. As defined in Article 13.4 of the *Disciplinary Rules*, professional discipline "shall include the suspension, bar or revocation as disciplinary measure by…[an] industry self-regulatory organization or professional association."

FINRA is an industry self-regulatory authority. The January 2017 AWC is an order of professional discipline by FINRA, and the Respondent is subject of that order. Therefore, the AWC conclusively establishes the existence of such discipline for purposes of this disciplinary proceeding, and is conclusive proof of the basis for such discipline by Respondent.

As set forth in Article 13.3 of the *Disciplinary Rules*, since Respondent's professional discipline has been proven, Respondent shall have the right to be heard by the Hearing Panel only on matters of rebuttal of any evidence presented by CFP Board Counsel other than proof of professional discipline.

III. Grounds for Discipline

First Ground for Discipline

Pursuant to Article 3(a) of the *Disciplinary Rules*, there are grounds to discipline Respondent for acts or omissions that violate Rule 4.3 of the *Rules of Conduct*, which provides that a certificant shall comply with applicable regulatory requirements governing professional services provided to the client.

Respondent is a certificant and FINRA is an industry self-regulatory organization. The FINRA AWC imposing a three-month suspension is an order of professional discipline. The FINRA AWC provides conclusive proof that Respondent violated NASD Rules 300 and 2110 when he failed to provide prior written notice to his firm and failed to obtain prior written approval from his firm before participating in a private securities transaction that was outside the regular course and scope of Respondent's employment with his firm.

Respondent is a certificant, and DFS is a state financial regulator which establishes regulatory requirements governing when financial advisors can legally provide the services of a licensed insurance agent to clients in the state. The order fining Respondent $750 for failing to disclose his misdemeanor conviction on his application for a non-resident insurance license provides conclusive proof that Respondent violated the rules of DFS.

Based upon the allegations and conduct set forth herein, the findings of FINRA in the AWC, and the findings in the order imposed by DFS, Respondent violated Rule 4.3 of the *Rules of Conduct*.

Second Ground for Discipline

Pursuant to Article 3(A) of the *Disciplinary Rules*, there are grounds to discipline Respondent for acts or omissions that violate Rule 5.1 of the *Rules of Conduct*, which provides that certificant who is an employee/agent shall perform professional services with dedication to the lawful objectives of the employer/principal and in accordance with CFP Board's *Code of Ethics*.

Respondent, a certificant, failed to perform professional services with dedication to lawful objectives of his employer and in accordance with CFP Board's Code of Ethics when he violated his firm's policies and procedures which required him to provide prior written notice to his firm and to obtain written approval from his firm before participating in private securities transactions that were outside the regular course and scope of Respondent's employment with his firm. By engaging in these actions that violated his employer's policies and procedures, Respondent violated Rule 5.1 of the *Rules of Conduct*.

Third Ground for Discipline

Pursuant to Article 3(d) of the *Disciplinary Rules*, there are grounds to discipline Respondent for acts that are the basis for professional discipline and the AWC constitutes professional discipline. The suspension issued by FINRA constitutes professional discipline. Therefore, the AWC is conclusive proof that there are grounds to discipline Respondent for acts that are a proper basis for professional discipline.

Fourth Ground for Discipline

Pursuant to Article 3(a) of the *Disciplinary Rules*, there are grounds to discipline Respondent for acts or omissions that violate Rule 6.5 of the *Rules of Conduct*, which provides that a certificant shall not engage in conduct which

reflects adversely upon the certificant's integrity or fitness as a certificant, upon the CFP® marks, or upon the profession.

Respondent, a certificant, engaged in conduct that reflected adversely on his fitness as a certificant and upon the CFP® marks when he invested substantial sums of his own money and the money of a work colleague in the dubious BV scheme that was supposedly going to pay him 60% interest on loans that claimed to be secured by a) nonexistent life insurance policies, and b) mortgages held by mortgage holders who were already in default and whose names and addresses could purportedly not be revealed because of "federal and state privacy laws."

The BV investment scheme presented enough red flags to have alerted Respondent to conduct extensive due diligence before investing his own funds or anyone else's. The fact that Respondent invested more than $150,000 in this dubious scheme reflects poorly on his fitness to serve as a CFP® professional. If members of the public heard that a CFP® professional was investing large sums in a questionable scheme without conducting further due diligence, those members of the public could think less of the CFP® marks and the financial planning profession. Similarly public respect for the marks could diminish if members of the public learned that a CFP® professional was participating in a scheme to earn interest rates of approximately 50% by making loans to struggling mortgage-holders who were already in default.

Based on the allegations and conduct set forth herein, Respondent violated 6.5 of the *Rules of Conduct*.

IV. Discipline Imposed

The Commission and Respondent entered into a Settlement Agreement in which Respondent consented to the Findings of Fact and Grounds for Discipline. Pursuant to the terms of the Settlement Agreement, the Commission issued to Respondent a suspension of his right to use the CFP® certification for six months pursuant to Article 4.3 of the *Disciplinary Rules*.

In considering its decision to enter into a Settlement Agreement with Respondent, the Commission considered the following aggravating factors:

- That the private securities transactions occurred between 2006 and 2008 with multiple purchases in each security;
- That the transactions involved Respondent's money as well as the funds of a colleague; and
- That Respondent failed to disclose his misdemeanor criminal conviction (2013) and his FINRA suspension to CFP Board within 30 calendar days.

In mitigation, the Commission considered that the private securities transactions occurred more than five years ago, and that the Respondent acknowledged his misconduct and expressed remorse.

The Commission also considered Anonymous Case History ("ACH") 30456, which involved a respondent recommending two private securities transactions without disclosing or getting approval from his firm. In that case, the Commission suspended the Respondent for 10 months. However, the Commission saw a distinction between the ACH and the instant case, because the respondent in the ACH matter made private securities transactions on behalf of his clients, whereas the instant Respondent did not.