

CERTIFIED FINANCIAL PLANNER BOARD OF STANDARDS, INC.

ANONYMOUS CASE HISTORIES
NUMBER 16502

This is a summary of a decision issued following the June 2011 hearings of the Disciplinary and Ethics Commission (“Commission”) of Certified Financial Planner Board of Standards, Inc. (“CFP Board”). The conduct at issue in this case occurred prior to January 1, 2009. The Rules in effect at that time under the *Code of Ethics and Professional Responsibility* (“Code of Ethics”) were Rules 101 through 705.

I. Issue Presented

Whether a CFP® professional (“Respondent”) violated CFP Board’s *Standards of Professional Conduct* when he sold promissory notes without receiving prior approval from his firm, resulting in: 1) a National Association of Securities Dealers (“NASD”) bar; 2) two terminations; and 3) two civil suits being filed against him.

II. Findings of Fact Relevant to the Commission’s Decision

While employed at a firm (“Firm 1”) in 1995, Respondent began selling promissory notes that were allegedly backed by real estate deeds of trust. Respondent’s colleague had introduced Respondent to the promissory notes, and shared commissions with Respondent for the sale of the promissory notes.

Respondent continued to sell the promissory notes when he joined another firm (“Firm 2”) in 1996. Respondent telephoned the compliance office of Firm 2 and mailed written materials to the compliance office related to the promissory notes. However, Respondent did not receive prior approval from Firm 2 before continuing to sell the promissory notes.

Between 1996 and 2000, Respondent sold over \$2 million in promissory notes to Firm 2 clients and received commissions on the sales. Respondent also purchased several promissory notes. Without conducting an investigation of the promissory notes, Respondent informed clients that the promissory notes were: 1) proven investments offering substantial returns; and 2) secured by recorded deeds of trust on real estate. Respondent’s statements were based on representations made to him by his former colleague. Respondent did not inform the clients that the promissory note recommendations were not based on a thorough investigation.

The deeds of trust securing the promissory notes were not in fact recorded. The promissory notes collapsed in 2000. Respondent initiated an involuntary bankruptcy against the promissory note issuer, recovering funds for clients and himself.

Following a NASD hearing and subsequent proceedings, Respondent was found to have:

- 1) Offered and sold unregistered securities in violation of NASD Conduct Rule 2110 and Section 5 of the Securities Act of 1933;
- 2) Engaged in private securities transactions for compensation without providing written notice to, or receiving written approval from, Firm 2, in violation of NASD Conduct Rules 3040 and 2110; and
- 3) Made material misrepresentations and misleading omissions amounting to fraud, in violation of Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 promulgated thereunder and NASD Conduct Rules 2120 and 2110.

Respondent was also the subject of two class action complaints filed against him related to the promissory notes. The civil cases were combined and settled. Respondent was also terminated by Firm 2 and by two subsequent firms.

III. Interim Suspension Proceedings

In August 2006, based on Respondent's conduct, CFP Board issued an Order to Show Cause to Respondent to show cause why his right to use the marks should not be temporarily suspended. Following a hearing before a quorum of the Commission in November 2006, the Commission determined not to order an Interim Suspension to Respondent.

IV. Commission's Analysis and Conclusions Regarding Rule Violations

- A. *Rule 102 – In the course of professional activities, a CFP Board designee shall not engage in conduct involving dishonesty, fraud, deceit or misrepresentation, or knowingly make a false or misleading statement to a client, employer, employee, professional colleague, governmental or other regulatory body or official, or any other person or entity.*

The Commission determined that Respondent engaged in conduct involving dishonesty, fraud, deceit or misrepresentation, or knowingly made false or misleading statements to clients when he: 1) falsely informed clients that the promissory notes would be secured; 2) made representations regarding the safety of the promissory notes without having performed any meaningful investigation into them; and 3) failed to inform clients that the promissory note recommendations were not based on a thorough investigation. Thus, Respondent violated Rule 102.

- B. *Rule 201 – A CFP Board designee shall exercise reasonable and prudent professional judgment in providing professional services.*

The Commission determined that Respondent failed to exercise reasonable and prudent professional judgment in providing professional services when he: 1) sold the promissory notes to clients without obtaining approval from Firm 2; 2) failed to investigate the promissory notes; 3) made statements to clients regarding the promissory notes without knowledge of the truth or

falsity of the statements; and 4) failed to disclose to clients that his recommendations were not based on a thorough investigation. Thus, Respondent violated Rule 201.

C. Rule 406 – A CFP Board designee who is an employee shall perform professional services with dedication to the lawful objectives of the employer and in accordance with the Code of Ethics.

The Commission found that Respondent failed to perform professional services with dedication to the lawful objectives of his employer when he: 1) sold unregistered securities in violation of NASD Conduct Rule 2110 and Section 5 of the Securities Act of 1933; and 2) engaged in private securities transactions for compensation without obtaining prior written approval from Firm 2, in violation of NASD Conduct Rules 3040 and 2110. Thus, Respondent violated Rule 406.

D. Rule 606(a) – In all professional activities a CFP Board designee shall perform services in accordance with applicable laws, rules and regulations of governmental agencies and other applicable authorities.

The Commission found that Respondent failed to perform services in accordance with applicable laws, rules and regulations of governmental agencies and other applicable authorities when he engaged in conduct that violated NASD Conduct Rules 2110, 2120 and 3040 and Section 5 of the Securities Act of 1933. Thus, Respondent violated Rule 606(a).

E. Rule 606(b) – In all professional activities a CFP Board designee shall perform services in accordance with applicable rules, regulations and other established policies of CFP Board.

The Commission found that Respondent failed to perform services in accordance with applicable rules, regulations and other established policies of CFP Board when he engaged in conduct that violated Rules 102, 201, 406, 606(a), 607, 701 and 704 of the *Code of Ethics*, as described herein. Thus, Respondent violated Rule 606(b).

F. Rule 607 – A CFP Board designee shall not engage in any conduct which reflects adversely on his or her integrity or fitness as a CFP Board designee, upon the marks, or upon the profession.

The Commission determined that Respondent engaged in conduct that reflected adversely on his integrity and fitness as a CFP Board designee, upon the marks and upon the profession when he: 1) failed to investigate the promissory notes he recommended to clients; 2) falsely informed clients that the promissory notes would be secured by recorded second deeds of trust; 3) failed to verify the truth of statements to clients regarding the promissory notes; 4) failed to disclose to clients that the promissory note recommendations were not based on a thorough investigation; 5) offered and sold the promissory notes to clients from 1996-2000 without obtaining approval from Firm 2 in violation of NASD Conduct Rule 2110 and Section 5 of the Securities Act of 1933; and 6) engaged in private securities transactions for compensation without obtaining prior

written approval from Firm 2 in violation of NASD Conduct Rules 3040 and 2110. Thus, Respondent violated Rule 607.

G. Rule 701 – A CFP Board designee shall provide services diligently.

The Commission found that Respondent failed to provide services diligently when he recommended the promissory notes to clients without conducting an investigation, sold them without obtaining approval from his firm, and made statements to clients regarding the promissory notes without confirming their veracity. Thus, Respondent violated Rule 701.

H. Rule 704 – A CFP Board designee shall make a reasonable investigation regarding the financial products recommended to clients.

The Commission determined, as found during Respondent's NASD proceedings, that Respondent did not conduct an independent analysis into the promissory notes, ignored risks related to the promissory notes, failed to perform any meaningful investigation into the promissory notes, and failed to make inquiries related to the promissory notes. In doing so, Respondent failed to make a reasonable investigation regarding the promissory notes, which were financial products that he recommended to his clients, and violated Rule 704.

V. Discipline Imposed

Article 3(a) of CFP Board's *Disciplinary Rules and Procedures* ("*Disciplinary Rules*") provides grounds for discipline for any act or omission that violates the *Code of Ethics*. The Commission found grounds for discipline under Article 3(a) because Respondent violated Rules 102, 201, 406, 606(a), 606(b), 607, 701 and 704 of the *Code of Ethics*. Pursuant to Article 4.2 of the *Disciplinary Rules*, the Commission issued Respondent a Public Letter of Admonition.

The Commission considered the following mitigating factors:

1. Respondent contacted Firm 2 regarding the promissory notes, but received no response;
2. Respondent invested his own funds into the promissory notes;
3. Respondent initiated an involuntary bankruptcy against the issuers of the promissory notes and obtained much of his clients' investment funds back for the clients.

The Commission considered the following aggravating factors:

1. Respondent sold complex securities that he did not understand;
2. Respondent represented to Firm 2 on yearly questionnaires that he did not receive compensation from a source other than Firm 2; and
3. Respondent shared compensation with his former colleague through personal checks written by the former colleague to Respondent.