

CERTIFIED FINANCIAL PLANNER BOARD OF STANDARDS, INC.

ANONYMOUS CASE HISTORIES  
NUMBER 21937

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This is a summary of a decision issued following the February 2010 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. Issues Presented

Whether a CFP<sup>®</sup> professional (“Respondent”) violated CFP Board’s *Standards of Professional Conduct* when he: 1) failed to conduct adequate due diligence of investments that he recommended to clients; and 2) entered into a settlement agreement with the Securities and Exchange Commission (“SEC”) in which he agreed to a one-year bar from associating with any investment adviser.

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

In October 2008, the SEC issued an order (“2008 SEC Order”) instituting cease-and-desist proceedings against Respondent and an investment adviser (“Company”), which Respondent co-founded. According to the 2008 SEC Order, Respondent was President and Chief Compliance Officer of the Company. Respondent’s partner (“Partner”) was Vice-President, Co-Founder and Co-Owner of the Company.

According to the 2008 SEC Order, the Company’s predecessor was formed in 1999 by Respondent, the Partner and three accountants. In 2002, the Company began recommending that its clients participate in the Partner’s investment pools. Through Respondent and the Partner, the Company sold \$6.5 million of these investments to 25 of its clients. The Company’s Web site also provided a direct link to the Web site of the Partner’s LLC. In 2003, the three accountants resigned from the Company’s predecessor. Respondent and the Partner then formed the Company. Respondent owned two-thirds of the Company, and the Partner owned one-third. From 2003 through 2005, the Company’s business grew rapidly and by 2005 the Company’s assets under management exceeded \$30 million.

In March 2007, the SEC conducted an examination of the Company’s offices. The SEC found that contrary to his representations to investors and Respondent, the Partner had misappropriated or lost approximately \$90 million of investor funds. In May 2007, the Partner, the Partner’s LLC and a related entity were enjoined from violating Section 17(a) of the Securities Act of 1933, Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder, and from violating or aiding and abetting in violations of Sections 206(1) and 206(2) of the Investment Advisers Act of 1940 (“Advisers Act”). The Company received approximately \$97,000 in fees based upon the client assets invested in

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the pools. Respondent received approximately \$6,000 of that amount.

The 2008 SEC Order required that Respondent:

1. cease and desist from committing or causing any violations of Sections 206(1), 206(2) and 206(4) of the Advisers Act and Rule 206(4)-7 thereunder;
2. be barred from association with any investment adviser; and
3. disgorge \$5,864 plus prejudgment interest and pay a civil penalty of \$40,000.

Respondent did not actively assist the Partner in his deceptions because the Partner misled Respondent. Respondent ceased recommending the investment pools to his clients after Respondent discovered Partner's deception. Finally, Respondent's clients' funds were reinvested in other fixed income securities.

### III. Commission's Analysis and Conclusions Regarding Rule Violations

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

The Commission found that by not taking steps to investigate whether the Partner's investment pools were legitimate investments, Respondent failed to exercise reasonable and prudent professional judgment in providing professional services. Thus, Respondent violated Rule 201.

*B. 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's settlement with the SEC and his one-year bar from association with any registered investment adviser, \$40,000 civil penalty and \$5,864 disgorgement was evidence that Respondent failed to perform professional services in accordance with the rules and regulations of governmental agencies. By violating Sections 206(1), 206(2) and 206(4) of the Advisers Act and Rule 206(4)-7 promulgated thereunder, Respondent failed to perform professional services in accordance with rules and regulations of governmental agencies. Thus, Respondent violated Rule 606(a).

*C. 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 by violating Rules 201, 606(a), 607 and 701, Respondent failed to perform services in accordance with applicable rules, regulations and other established policies of CFP Board. Thus, Respondent violated Rule 606(b).

*D. 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 found that by: 1) not inquiring whether the Partner's investment pool funds were, in fact, being invested consistent with the representations made to investors; and 2) violating Sections 206(1), 206(2) and 206(4) of the Advisers Act and Rule 206(4)-7 promulgated thereunder, Respondent engaged in conduct that reflects adversely on his integrity and fitness as a CFP Board designee, upon the marks and upon the profession. Thus, Respondent violated Rule 607.

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

The Commission found that, as Respondent acknowledged during testimony before the Commission, Respondent failed to conduct adequate due diligence by not inquiring whether the pooled funds were legitimate investments. By failing to conduct adequate due diligence regarding his clients' investments in the pools, Respondent failed to provide services diligently. Thus, Respondent violated Rule 701.

#### IV. Discipline Imposed

The Commission found grounds for discipline under Articles 3(a) and 3(e) of the *Disciplinary Rules and Procedures* ("*Disciplinary Rules*"). Article 3(a) of the *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 201, 606(a), 606(b), 607, and 701 of the *Code of Ethics*. Article 3(e) of the *Disciplinary Rules* provides grounds for discipline for any violation of the *Disciplinary Rules*. The Commission found Article 3(e) grounds for discipline because, although Respondent did eventually disclose the 2008 SEC bar to CFP Board, he failed to disclose the bar within 10 calendar days as required under Article 12.2 of the *Disciplinary Rules*. Pursuant to Article 4.3 of the *Disciplinary Rules*, the Commission issued Respondent a one-year suspension.

The Commission considered the following mitigating factors:

1. Respondent's contrite admission of his failure to exercise reasonable and prudent professional judgment and diligence;
2. Respondent disclosed to CFP Board that he was the subject of an SEC investigation;
3. Respondent accepted responsibility for his actions and failure to act;
4. Respondent's had no prior disciplinary history; and
5. Respondent did not profit from the Partner's fraud.

The Commission considered no aggravating factors.