

CERTIFIED FINANCIAL PLANNER BOARD OF STANDARDS, INC.

ANONYMOUS CASE HISTORIES
NUMBER 22986

This is a summary of a decision issued following the June 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 candidate for CFP® certification (“Respondent”) violated CFP Board’s *Standards of Professional Conduct* when she: 1) engaged in outside business activities without obtaining written approval from her employer; 2) did not notify CFP Board of her suspension; 3) recommended that her clients invest in promissory notes issued by her son’s company; and 4) did not disclose risks and other material and relevant information regarding the promissory notes to her clients.

II. Findings of Fact

In June 2006, a State Securities Division began an investigation (“2006 State Investigation”) of Respondent concerning her recommendation that her clients purchase promissory notes from her son’s real estate development company (“Real Estate Company”). Respondent made the recommendation while employed with an investment advisory company (“Company”).

Respondent represented Real Estate Company to investors as a safe investment project that would purchase and develop about 520 acres of land in the State. Respondent told the clients that: 1) the notes were secured by real property; and 2) the notes carried her son’s unconditional and irrevocable personal guarantee. The notes were not recorded on the land records or secured by real property.

Respondent did not disclose to her clients that: 1) her son had little experience managing complex real estate development projects; 2) her son had recently filed for personal bankruptcy; 3) her son’s debts were discharged just months before the first promissory note was sold; 4) her son’s guarantee had limited value; 5) the Company did not authorize the sale of the promissory notes; and 6) the Company did not conduct a due diligence investigation of the soundness of the investment program.

Between October 2004 and November 2005, Real Estate Company issued 11 promissory notes for a total of \$1,000,000, including \$800,000 for nine notes sold to four of Respondent’s clients. Real Estate Company filed for Chapter 11 bankruptcy in May 2006, and the bankruptcy was

dismissed when Real Estate Company was unable to reorganize. Real Estate Company was foreclosed upon and lost any rights it had to the land it had purchased for development.

In November 2007, Respondent entered into a Financial Industry Regulatory Authority (“FINRA”) Letter of Acceptance Waiver and Consent (“AWC”). Respondent agreed in the AWC: 1) that she violated National Association of Securities Dealers (“NASD”, now known as FINRA) Rules 2110 and 3040 when she participated in several private securities transactions without the prior written approval of her employer; and 2) to a \$5,000 fine and a three-month suspension.

In December 2008, Respondent entered into a Consent Agreement with the State Securities Commissioner. The Commissioner determined that: 1) promissory notes are securities as defined by the State Securities Act (“Act”); 2) the promissory notes were required to be registered or exempted from registration in the State; 3) Respondent violated the Act by offering and selling unregistered and non-exempt securities; 4) Respondent violated the Act by failing to disclose the risks of the investments; and 5) Respondent violated the Act by failing to provide complete information in connection with her applications for registration.

Respondent did not notify CFP Board of her FINRA suspension as required under Article 12.2 of the *Disciplinary Rules and Procedures* (“*Disciplinary Rules*”). Respondent’s certification with CFP Board expired in February 2008, and Respondent had a grace period of 90 days to renew her certification. Respondent did not renew her certification within the 90-day grace period.

While considering the degree of sanction to impose, the Commission found that Respondent: 1) encouraged clients to discuss substantial investments in her son’s real estate venture; 2) asked her son to contact her clients or arranged initial meetings with the clients; 3) implied to her clients that she was familiar with and supportive of investing in the speculative real estate venture involving her son; 4) misrepresented the value of the real estate market and referred clients to her son’s real estate venture without providing any other investment options; 5) testified that she was familiar with the disclosure required for similar investments, yet failed to make even a cursory attempt to inquire into her son’s real estate venture on behalf of her clients; and 6) admitted that she failed to renew her certification in a timely manner.

III. 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 found that Respondent engaged in conduct involving dishonesty, fraud, deceit, or misrepresentation when she: 1) told the clients that the promissory notes were secured by real property; 2) told the clients that the promissory notes had her son’s unconditional and irrevocable guarantee and did not disclose that the guarantee was limited; 3) did not disclose to the clients that

her son had little experience managing complex real estate development projects; 4) did not disclose to the clients her son's bankruptcy filing; 5) did not disclose to the clients that the Company had not authorized the sale of the promissory notes; and 7) did not disclose to the clients that the Company had not conducted a due diligence investigation of the soundness of the investment program. Thus, Respondent violated *Code of Ethics* Rule 102.

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

The Commission determined that by making the above-mentioned misrepresentations to her clients regarding the promissory notes, Respondent failed to exercise reasonable and prudent professional judgment in providing professional services. Thus, Respondent violated *Code of Ethics* Rule 201.

C. Rule 401(a) – In rendering professional services, a CFP Board designee shall disclose to the client material information relevant to the professional relationship, including conflict(s) of interest, the CFP Board designee's business affiliation, address, telephone number, credentials, qualifications, licenses, compensation structure and any agency relationships, and the scope of the CFP Board designee's authority in that capacity.

The Commission found that Respondent failed to disclose to the clients material information relevant to the professional relationship when she did not inform the clients that: 1) the promissory notes were not secured by real property; 2) her son's personal guarantee was limited; 3) her son had little experience managing real estate development projects; 4) her son had filed for bankruptcy; 5) the Company had not authorized the sale of the promissory notes; and 6) the Company had not conducted a due diligence investigation of the soundness of the investment program. Thus, Respondent violated *Code of Ethics* Rule 401(a).

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 professional services in accordance with applicable laws, rules and regulations of governmental agencies and other applicable authorities when she: 1) violated provisions of the Act; and 2) violated FINRA Rules 2110 and 3040. Thus, Respondent violated *Code of Ethics* Rule 606(a).

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

The Commission determined that Respondent failed to perform professional services in accordance with applicable rules, regulations and other established policies of CFP Board when she violated Rules 102, 201, 401(a), 606(a), 607 and 612 of CFP Board's *Code of Ethics*. Thus, Respondent violated *Code of Ethics* Rule 606(b).

F. Rule 607 – A CFP Board designee shall not engage in 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 Respondent engaged in conduct which reflects adversely on her integrity and fitness as a CFP Board designee, upon the marks, and upon the profession when she: 1) did not inform the clients that the Company had not authorized the sale of the promissory notes; 2) offered and sold unregistered and non-exempt securities; 3) failed to disclose the risks of the investments and her son's bankruptcy filing; 4) promised that the investments would be secured by real property; and 5) failed to renew her certification in a timely manner. Thus, Respondent violated *Code of Ethics* Rule 607.

G. Rule 612 – A CFP Board designee shall comply with all renewal requirements established by CFP Board.

The Commission found that Respondent failed to comply with all applicable renewal requirements established by CFP Board when she did not renew her certification in a timely manner. Thus, Respondent violated *Code of Ethics* Rule 612.

IV. 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 Articles 3(a), 3(d) and 3(e) because Respondent violated Rules 102, 201, 401(a), 606(a), 606(b), 607 and 612 of the *Code of Ethics*. Pursuant to Article 4.3 of the *Disciplinary Rules*, the Commission issued a four-year suspension to Respondent.

The Commission considered the following mitigating factor:

1. Respondent had no prior disciplinary history.

The Commission considered the following aggravating factors:

1. Respondent continued to insist at hearing that the only problem with the promissory notes was a failure to record the encumbrances on the real property;
2. Respondent recommended the promissory notes to multiple clients;
3. Respondent caused individual clients to suffer losses in excess of \$10,000;
4. Respondent recommended the promissory notes to clients who were elderly and disabled;
5. Respondent was unable to see conflicts of interest in her multiple roles;
6. Respondent disclosed the clients' confidences to her son; and
7. Respondent conducted outside business activities without permission from her broker-dealer.