CERTIFIED FINANCIAL PLANNER BOARD OF STANDARDS, INC.

ANONYMOUS CASE HISTORIES
NUMBER 25999

This is a summary of a Settlement Agreement entered into at the October 2013 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 after January 1, 2009. The Rules in effect at that time under the *Rules of Conduct* were Rules 1.1 through 6.5.

I. Issue Presented

Whether a CFP® professional ("Respondent") violated CFP Board's *Standards of Professional Conduct* when he recommended that clients purchase a high-risk illiquid security without researching the financial condition of the firm proving financial support of the investment.

II. Findings of Fact

From October 2008 to May 2010, Respondent served as a General Securities Representative and Financial Consultant with an investment management firm ("Investment Firm"). A wealth management firm ("Wealth Firm") owned over 99% of Investment Firm from which it derived all of its income. At the time Respondent joined the firm, Investment Firm had experienced annual operating losses for several years. Wealth Firm created a private offering, 9% 3-year convertible note ("Note"), in order to generate profit in an attempt to offset flagging revenue. A Confidential Private Placement Memorandum ("PPM") disclosed that Wealth Firm's only asset constituted its 99.8% ownership interest in Investment Firm. The PPM also stated that the Notes involved a high degree of risk and that the Notes were suitable only for persons of substantial net worth who had the ability to purchase a high-risk, illiquid investment and could "bear the risk of a complete loss of their investment." Respondent claimed to have no knowledge of the firm's financial instability. Respondent relied on information provided by his superiors and never asked for documentary or other confirmation corroborating the firm's positive financial condition. The effort to save the firm failed and on May 2010; the firm ceased conducting business and filed a Broker Dealer Withdrawal form with the Financial Industry Regulatory Authority, Inc. ("FINRA", formerly known as the National Association of Securities Dealers, Inc. or "NASD").

2010 Client Arbitration

In early 2010 Client 1, acting via power of attorney on behalf of her 81-year old cousin Client 2, met with an Investment Firm broker ("Broker") to develop a financial plan designed to generate income to cover Client 2's nursing home expenses. As part of the comprehensive financial plan, Broker recommended that Client 2 use $50,000 of her net worth to invest in the Note issued by Wealth Firm. Respondent met with Client 1 and assisted in explaining the specifics regarding the financial plan and the Note. Client 2 was not an accredited investor and did not have substantial net worth.

In May 2010, when Client 1 became aware of fraud allegations against Wealth Firm, he/she filed a complaint with FINRA that alleged unsuitability, misrepresentation and omissions. The matter settled in April 2011 for approximately $9,000 with 100% contribution from Respondent.

In 2007, Client 3, a widow and retired bookkeeper, opened an account with Investment Firm. At that time, Client 3's account information form calculated her annual income at approximately $51,000 and her total net worth at approximately $600,000 with no need for income from her portfolio, and no expectation of making withdrawals. Client 3 was an unaccredited and unsophisticated investor.

Respondent became Client 3's broker in 2009. Prior to meeting with Respondent, Client 3 sold her home and added the approximately $166,000 in proceeds of the sale to her portfolio. According to Client 3, her account information regarding need for income and risk tolerance remained unchanged from 2007. By Respondent's own assessment, Client 3 possessed a "conservative risk profile." In February 2010, based on the recommendation of Respondent, Client 3 invested approximately $50,000 into the Note. Respondent advised Client 3 of the risks associated with the Note but assured her that, should Wealth Firm go out of business, she would likely recoup her investment plus 11% interest.

In November 2011, FINRA issued a Complaint against Respondent alleging unsuitable recommendations and failure to adequately inform himself of the risks regarding Client 3 and the Note.

In January 2013, FINRA concluded that Respondent made an unsuitable recommendation in violation of NASD Conduct Rule 2310, NASD IM-23 I0-2, and FINRA Conduct Rule 2010, and suspended him from associating in any capacity with any FINRA member firm for two business days, and ordered him to pay restitution in full to Client 3 in the amount of approximately $50,000, with interest. Respondent's suspension was effective for one week in March 2013.

III. Rule Violations

A. Rule 1.4 – A certificant shall at all times place the interest of the client ahead of his or her own. When the certificant provides financial planning or material elements of financial planning, the certificant owes to the client the duty of care of a fiduciary as defined by CFP Board.

Respondent failed to place the interest of the client ahead of his own when he recommended that his clients purchase a high-risk, illiquid security without sufficiently researching the financial condition of the firm and proving financial support of the investment. Thus, Respondent violated *Rules of Conduct* Rule 1.4.

B. Rule 3.3 – A certificant shall obtain the information necessary to fulfill his or her obligations or inform the prospective client or client of any and all material deficiencies in necessary information.

Respondent failed to obtain the information necessary to fulfill his or her obligations or inform the prospective client or client of any and all material deficiencies in necessary information when he recommended that his clients purchase a high-risk, illiquid security without sufficiently researching the financial condition of the firm and proving financial support of the investment. Thus, Respondent violated *Rules of Conduct* Rule 3.3.

C. Rule 4.3 – A certificant shall comply with applicable regulatory requirements governing professional services provided to the client.

Respondent failed to comply with applicable regulatory requirements governing professional services provided to the client when he made an unsuitable recommendation, in violation of NASD Conduct Rule 2310, NASD IM-23 I0-2, and FINRA Conduct Rule 2010. Thus, Respondent violated *Rules of Conduct* Rule 4.3.

D. *Rule 4.4 – A certificant shall exercise reasonable and prudent professional judgment in providing professional services to clients.*

Respondent failed to exercise reasonable and prudent professional judgment in providing professional services to clients when he made unsuitable recommendations that clients purchase a high-risk, illiquid security without sufficiently researching the financial condition of the firm and proving financial support of the investment. Thus, Respondent violated *Rules of Conduct* Rule 4.4.

E. *Rule 4.5 – A certificant shall make and/or implement only recommendations that are suitable for the client.*

Respondent failed to make and/or implement only recommendations that were suitable for clients when he recommended the clients purchase a high-risk, illiquid security that was inconsistent with their investment objectives and financial condition and without sufficiently researching the financial condition of the firm and proving financial support of the investment. Thus, Respondent violated *Rules of Conduct* Rule 4.5.

F. *Rule 6.5 – 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.*

Respondent engaged in conduct that reflects adversely on his integrity and fitness as a certificant, upon the CFP® marks, and upon the profession when he made unsuitable recommendations that clients purchase a high-risk illiquid security without sufficiently researching the financial condition of the firm and proving financial support of the investment. As a result of his conduct, Respondent was: 1) found to be in violation of NASD Conduct Rule 2310, NASD IM-23 I0-2, and FINRA Conduct Rule 2010; 2) suspended from association in any capacity with any FINRA member firm for two business days; and 3) ordered to pay restitution in full to the client in the amount of $50,000. Thus, Respondent violated *Rules of Conduct* Rule 6.5.

IV. Discipline Imposed

The Commission found grounds for discipline under Articles 3(a) and 3(d) of CFP Board's *Disciplinary Rules and Procedures* ("*Disciplinary Rules*"). Articles 3(a) of CFP Board's *Disciplinary Rules* provides grounds for discipline for any act or omission that violates the *Rules of Conduct.* The Commission found grounds for discipline under Article 3(a) because Respondent violated Rules 1.4, 3.3, 4.4, 4.5, and 6.5 of the *Rules of Conduct.* Article 3(d) of CFP Board's *Disciplinary Rules* provides grounds for discipline for any act that is the proper basis for professional discipline. The Commission found grounds for professional discipline under Article 3(d) because FINRA suspended Respondent for two business days. CFP Board and Respondent entered into a Settlement Agreement in which Respondent consented to the Findings of Fact and Rule Violations. Based on the terms of the Settlement Agreement, the Commission issued a one year and one day suspension, pursuant to Article 4.3 of the *Disciplinary Rules*.

In proposing this Counter Offer, the Commission considered as a mitigating factor that this was Respondent's first client complaint in 24 years of practice.

The Commission cited the following aggravating factors:

1. Respondent put two clients into the same investment, which required investors be accredited investors, when both clients were unaccredited and unsophisticated investors;
2. FINRA suspended Respondent for two-days due to his actions regarding the private placement;
3. Respondent failed to conduct independent research to verify his firm's claims regarding the private placement. The PPM from Respondent's own investment firm stated that the investment was taking losses and the firm went out of business shortly (three months) after Respondent sold the private

placement bond. Due to Respondent's high level of experience, Respondent should have known of the need to do more research;

4. Though Respondent was not a principal, he should have been aware of financial condition of firm;
5. It appeared Respondent was under firm pressure to sell and conducted meetings to go over client lists to find non-accredited clients with cash;
6. Respondent knew from the PPM that the investment was high risk, yet he told a client that if the firm went out of business he/she would earn at least an 11% return of principal;
7. The client reported that he/she was told that the risk notice was "no big deal" and just a formality;
8. Respondent's FINRA response, which indicated that the only factors he considered when determining suitability were that he were familiar with the investment product, that it was "only" 10% of client's portfolio, and that client had signed the papers, signaled that Respondent made an inadequate assessment of suitability before making the recommendation;
9. The record indicated that Respondent was engaged in material elements of financial planning based on the comprehensiveness of his information gathering, the presentation of the recommendation and his implementation of the plan. Therefore, Respondent had a fiduciary duty; and
10. Respondent placed his and the firm's interest to sell bonds because of financial difficulty ahead of client's safety and suitability of the recommendations.

In arriving at its decision, the Commission reviewed Anonymous Case Histories 26284, 15094, 27406, 25389, 22866, 16836 and 13449. The Commission also consulted *Sanction Guidelines* 20(d) (Misrepresentation to Clients and Prospective Clients), 30 (Securities Law Violation), 31 (Suitability Violation) and 33 (Professional discipline as defined in Article 13.6 involving a suspension for more than one calendar month and less than three calendar months).