

CERTIFIED FINANCIAL PLANNER BOARD OF STANDARDS, INC.

ANONYMOUS CASE HISTORIES
NUMBER 26476

This is a summary of a decision issued following the March 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 before and after January 1, 2009. The Rules in effect for conduct occurring before January 1, 2009 were Rules 101 through 705 of CFP Board’s *Code of Ethics and Professional Responsibility* (“*Code of Ethics*”). The Rules in effect for conduct occurring after January 1, 2009 were Rules 1.1 through 6.5 of CFP Board’s *Rules of Conduct*.

I. Issue Presented

Whether a CFP® professional (“Respondent”) violated CFP Board’s *Standards of Professional Conduct* when he concentrated clients’ assets in private placements.

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

2010 Client 1 and Client 2 Customer Complaints

In May 2010, Client 1’s attorney sent a complaint and demand letter to Respondent and the Chief Executive Officer of Firm 1. Client 1’s attorney alleged that Respondent and his firm, Firm 2, gave misleading presentations in an effort to sell Firm 1 private placements to clients. Client 1’s attorney alleged that the presentations led clients to believe they were investing in a company other than the issuer and that the Private Placement Memorandum was misleading.

In May 2010, Client 1’s attorney sent an identical letter on behalf of Client 2. Both clients purchased units of Firm 1 in early 2008 for approximately \$100,000. Respondent’s BrokerCheck report stated that these complaints were closed in March 2012. Respondent did not provide any statement other than denying the allegations made in the letters. CFP Board did not make any allegations regarding these complaints.

2011 FINRA Arbitration

In August 2005, Client 3 and Client 4 received a letter from Respondent soliciting them to attend a free-dinner seminar presented by Respondent. Client 3 and Client 4 attended the seminar and then met with Respondent in his office. Shortly thereafter, Client 3 and Client 4 completed a “Confidential Personal Financial Planning Guide.” The first page of this guide stated:

“This comprehensive, personal financial planning summary is designed to help you take inventory and assign realistic values to your personal assets and liabilities. It’s the essential first step in organizing a sensible financial plan for your future.”

In the Guide, Client 3 and Client 4 indicated that were 70 years old and derived their income from social security, pensions, and a rental property. In October 2005, Client 3 and Client 4 completed a new account form. Client 3 and Client 4 listed their net worth excluding their home as approximately \$690,000. When selecting their investment objectives, Client 3 and Client 4 checked every box but aggressive

growth. They listed their time horizon as less than five years and current liquid assets as approximately \$300,000. In October 2005, Respondent sold Client 3 and Client 4 partnership interests in an oil company for approximately \$25,000. Respondent did not develop or present Client 3 and Client 4 with a financial plan.

In November 2005, Respondent sold Client 3 and Client 4 partnership interests in a real estate company for approximately \$50,000. In May 2008, Respondent sold the Smiths partnership interests in an energy company for approximately \$20,000. According to Client 3 and Client 4's Statement of Claim, Respondent sold their approximately \$690,000 worth of partnership interests or other alternative investments from 2005 through 2010.

In May 2010, Client 3 signed a memorandum entitled "Over concentration of illiquid and non-traditional assets" and acknowledged approving his reinvestment of funds in Firm 1 investments and in the energy company. The memorandum also stated that Client 1 was comfortable with the diversified investments approved by the firm as well as the liquidity of his investments. This memorandum was dated nine days after Client 1's attorney's complaint letters were sent to Respondent regarding Firm 1 investments. The record did not reflect that Respondent sold Client 3 and Client 4 anything other than partnership interests or alternative investments.

In March 2011, Client 3 and Client 4 filed for arbitration against Respondent alleging that Respondent sold them unsuitable private placements. In June 2011, Respondent filed his Answer and alleged that he informed the clients of the risk associated with the products. In March 2012, the parties entered into a settlement agreement wherein Respondent and his firm agreed to pay Client 3 and Client 4 approximately \$235,000.

III. Commission's Analysis and Conclusions Regarding Rule Violations

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

The Complaint alleged that Respondent engaged in conduct involving dishonesty, fraud, deceit or misrepresentation, or knowingly making a false or misleading statement to a client when he held himself out as a financial planner providing comprehensive financial planning services but did not provide financial planning services to the clients. The Commission determined that Respondent provided financial planning services. Respondent provided written materials to CFP Board such as a client profile that was used to create a financial plan. Respondent did not provide a copy of the written plan that was generated, but did testify under oath that he created a written plan and delivered it to the clients. Respondent was unable to provide the written plan as part of the record since his firm no longer uses the software. Thus, Respondent did not violate *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 Respondent failed to exercise reasonable and prudent professional judgment in providing professional services when he sold the Client 3 and Client 4 unsuitable partnership interests and alternative investments from 2005 through 2008. The Commission recognized that alternative investments/partnership interests may have a place in an overall portfolio, but Respondent repeatedly recommended these types of investments. The underlying investments did not appear to meet

the client's stated investment objectives. The cumulative investments into these strategies led to an unsuitable allocation into these asset classes for Client 3 and Client 4. In addition, the investments were inconsistent with Client 3 and Client 4's time horizon of less than five years. Thus, Respondent violated *Code of Ethics* Rule 201.

C. Rule 202 – A financial planning practitioner shall act in the interest of the client

The Commission determined that Respondent failed to act in the interest of the clients when he sold Client 3 and Client 4 unsuitable partnership interests and alternative investments from 2005 through 2008. The Commission determined that the record reflected that Respondent provided financial planning services to Client 3 and Client 4. The Commission recognized that alternative investments/partnership interests may have a place in an overall portfolio, but Respondent repeatedly recommended these types of investments. The cumulative investments into these strategies led to an unsuitable allocation into these asset classes for Client 3 and Client 4. Respondent testified that his financial planning recommendations consisted of a diversified investment portfolio, but the client was not interested in traditional asset allocation. Respondent continued, however, to purchase illiquid risky investments for the clients. Thus, Respondent violated *Code of Ethics* Rule 202.

D. Rule 606(b) – A CFP Board designee shall perform services in accordance with applicable rules, regulations and other established policies of CFP Board

The Commission determined that Respondent failed to perform services in accordance with applicable rules, regulations and other established policies of CFP Board when he sold Client 3 and Client 4 unsuitable partnership interests and alternative investments from 2005 through 2008, in violation of Rules 201, 202, 607 and 703. Thus, Respondent violated *Code of Ethics* Rule 606(b).

E. 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 determined that Respondent engaged in conduct that reflects adversely on his integrity and fitness as a CFP Board designee, upon the marks, and upon the profession when he sold Client 3 and Client 4 unsuitable partnership interests and alternative investments from 2005 through 2008. The Commission recognized that alternative investments/partnership interests may have a place in an overall portfolio, but Respondent repeatedly recommended these types of investments. The cumulative investments into these strategies led to an unsuitable allocation into these asset classes for Client 3 and Client 4. Thus, Respondent violated *Code of Ethics* Rule 607.

F. Rule 703 – A financial planning practitioner shall make and/or implement only recommendations which are suitable for the client

The Commission determined that Respondent failed to make and implement only those recommendations that are suitable for the client when he sold Client 3 and Client 4 unsuitable partnership interests and alternative investments from 2005 through 2008. The Commission recognized that alternative investments/partnership interests may have a place in an overall portfolio, but Respondent repeatedly recommended these types of investments. The underlying investments did not appear to meet the clients' stated investment objectives. The cumulative investments into these strategies led to an unsuitable allocation into these asset classes for Client 3 and Client 4. In addition, the investments were inconsistent with Client 3 and Client 4's time horizon of less than five years. Thus, Respondent violated *Code of Ethics* Rule 703.

G. Rule 1.3 – The certificant or the certificant’s employer shall enter into a written agreement governing financial planning services

The Commission determined that Respondent held himself out as a financial planner providing comprehensive financial planning services but failed enter into a written agreement governing financial planning services. The Commission noted that Respondent did not have a written agreement specifying the parties, the date and duration of the agreement, the terms on which the parties may terminate the agreement or the services to be provided as part of the agreement. Thus, Respondent violated *Rules of Conduct* Rule 1.3.

H. 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

The Commission determined that Respondent failed to place a client’s interest ahead of his own and failed to act with the duty of care of a fiduciary when he sold Client 3 and Client 4 partnership interests and alternative investments from 2009 through 2010. The Commission recognized that alternative investments/partnership interests may have a place in an overall portfolio, but Respondent repeatedly recommended these types of investments. The underlying investments did not appear to meet the clients’ stated investment objectives. The cumulative investments into these strategies led to an unsuitable allocation into these asset classes for Client 3 and Client 4. In addition, the investments were inconsistent with Client 3 and Client 4’s time horizon of less than five years. Thus, Respondent violated *Rules of Conduct* Rule 1.4.

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

The Commission determined that Respondent failed to exercise reasonable and prudent professional judgment in providing professional services when he sold Client 3 and Client 4 unsuitable partnership interests and alternative investments from 2009 through 2010. The Commission recognized that alternative investments/partnership interests may have a place in an overall portfolio, but Respondent repeatedly recommended these types of investments. The underlying investments did not appear to meet the clients’ stated investment objectives. The cumulative investments into these strategies led to an unsuitable allocation into these asset classes for Client 3 and Client 4’s. In addition, the investments were inconsistent with Client 3 and Client 4’s time horizon of less than five years. Thus, Respondent violated *Rules of Conduct* Rule 4.4.

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

The Commission determined that Respondent failed to exercise reasonable and prudent professional judgment in providing professional services when he sold Client 3 and Client 4 unsuitable partnership interests and alternative investments from 2009 through 2010. The Commission recognized that alternative investments/partnership interests may have a place in an overall portfolio, but Respondent repeatedly recommended these types of investments. The underlying investments did not appear to meet the clients’ stated investment objectives. The cumulative investments into these strategies led to an unsuitable allocation into these asset classes for Client 3 and Client 4. In addition, the investments were inconsistent with Client 3 and Client 4’s time horizon of less than five years. Thus, Respondent violated *Rules of Conduct* Rule 4.5.

K. 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

The Commission determined that Respondent engaged in conduct that reflects adversely on his integrity and fitness as a CFP Board designee, upon the marks, and upon the profession when he sold Client 3 and Client 4 unsuitable partnership interests and alternative investments from 2009 through 2010. The Commission recognized that alternative investments/partnership interests may have a place in an overall portfolio, but Respondent repeatedly recommended these types of investments. The underlying investments did not appear to meet the clients' stated investment objectives. The cumulative investments into these strategies led to an unsuitable allocation into these asset classes for Client 3 and Client 4. In addition, the investments were inconsistent with Client 3 and Client 4's time horizon of less than five years. Thus, Respondent violated *Rules of Conduct* Rule 6.5.

L. Practice Standard 100-1 – Defining the scope of the engagement

The Commission determined that Respondent failed to mutually define the scope of engagement before providing financial planning services when he held himself out as a financial planner providing comprehensive financial planning services but did not provide financial planning services to the clients. The Commission determined that Respondent delivered a written plan but failed to clarify the scope of the engagement. Thus, Respondent violated *Practice Standard 100-1*.

M. Practice Standard 400-2 – Developing the financial planning recommendations

The Commission determined that Respondent failed to develop recommendations in an effort to reasonably meet the clients' goals, needs and priorities when he recommended and sold the clients partnership interests that were unsuitable, individually, because they had a high degree of risk and were illiquid and unsuitable, collectively, because of Client 3 and Client 4's concentrated portfolio of alternative investments and nonexistent diversification across investment classes. The Commission determined that Respondent's testimony that he made suitable investment recommendations in his written financial plan was contradicted by the fact that he repeatedly sold Client 3 and Client 4 unsuitable partnership interests and alternative investments. Thus, Respondent violated *Practice Standard 400-2*.

N. Practice Standard 500-2 – Selecting products and services for implementation

The Commission determined that Respondent failed to select appropriate products and services that were consistent with the clients' goals, needs and priorities when he recommended and sold the clients partnership interests that were unsuitable, individually, because they had a high degree of risk and were illiquid and unsuitable, collectively, because of Client 3 and Client 4's concentrated portfolio of alternative investments and nonexistent diversification across investment classes. The Commission determined that Respondent's testimony that he made suitable investment recommendations in his written financial plan was contradicted by the fact that he repeatedly sold Client 3 and Client 4 unsuitable partnership interests and alternative investments. Thus, Respondent violated *Practice Standard 500-2*.

IV. Discipline Imposed

The Commission found grounds for discipline under Articles 3(a) and 3(b) of the *Disciplinary Rules and Procedures* ("Disciplinary Rules"). Article 3(a) of CFP Board's *Disciplinary Rules* provides grounds for discipline for any act or omission that violates the *Code of Ethics* and *Rules of Conduct*. The Commission found grounds for discipline under Article 3(a) because Respondent violated Rules 201, 202, 606(b),

607 and 703 of the *Code of Ethics* and Rules 1.3, 1.4, 4.4, 4.5, and 6.5 of the *Rules of Conduct*. Article 3(b) of CFP Board's *Disciplinary Rules* provides grounds for discipline for any act or omission that violates the *Practice Standards*. The Commission found grounds for discipline under Article 3(b) because Respondent violated *Practice Standards* 100-1, 400-2 and 500-2. Pursuant to Article 4.3 of the *Disciplinary Rules*, the Commission issued a two-year suspension.

While considering the degree of sanction to impose, the Commission consulted Anonymous Case Histories 20996, 22866 and 23352. The Commission also considered *Sanction Guidelines* 5 (Breach of Fiduciary Duty), 11 (Diligence), 16 (Failure to Enter Into a Written Financial Planning Agreement) and 31 (Suitability). The panel relied mainly on the *Sanction Guidelines* for Breach of Fiduciary Duty and Suitability to arrive at a two-year suspension.

The Commission considered the following mitigating factors:

1. The client signed a letter claiming they understood and were comfortable with the over concentration in illiquid assets; and
2. Respondent testified that he delivered a financial plan that suggested a diversified investment portfolio.

The Commission considered as an aggravating factor that Respondent received a public letter of admonition in 2001 that was related to suitability issues and had a history of FINRA complaints relating to suitability.