CERTIFIED FINANCIAL PLANNER BOARD OF STANDARDS, INC.

ANONYMOUS CASE HISTORIES NUMBER 27037

This is a summary of a decision issued following the June 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 prior to 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. Issues Presented

Whether a CFP® professional ("Respondent") violated CFP Board's *Standards of Professional Conduct* when he: 1) sold 20,000 stock put options in SH and YH's account, resulting in a total unrealized loss of $430,000 and a realized loss of almost $2 million; 2) charged SH and YH full commissions on their trades when they should have been entitled to discounted rates based on the size of their investment accounts; 3) charged SH and YH an exorbitant fee of 8% a year; 4) altered the clients' new account forms with White-out, causing Firm to retain and preserve altered records and causing him to be suspended by Financial Industry Regulatory Authority ("FINRA") for violation of firm policy and National Association of Securities Dealers ("NASD") Conduct Rules 2110 and 3110; and 5) failed to report his FINRA suspension within 30 days.

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

2009 SH and YH Arbitration

In April 2009, SH and YH filed a Statement of Claim ("SOC") with FINRA alleging that Respondent and his former firm took advantage of the written discretion SH and YH granted Respondent over their accounts to eradicate approximately $3 million of the account value. SH and YH alleged breach of fiduciary duty, misrepresentation, fraud and negligence against Respondent and his firm. Specifically, SH and YH alleged that Respondent charged excessive commissions, engaged in outrageous use of margin debt and invested their accounts in multiple high-risk investments.

According to SH and YH, they met Respondent in 1998 while he was employed with Company A. After SH and YH's previous investment advisor retired, Respondent assumed responsibility for their account. SH and YH stated that the previous advisor invested SH and YH's assets almost entirely in municipal bonds. Beginning in 1999, SH, an attorney, went to work in the public sector for an annual salary of approximately $30,000 a year, an amount far below what he had earned as an attorney in private practice. SH informed Respondent that he would need an additional income of approximately $12,500 a month to maintain the standard of living he enjoyed while employed in the private sector. SH also informed Respondent that he was interested in low risk investments that would not place his principal at risk.

In Respondent's Answer to the FINRA SOC, he stated that his relationship with SH and YH began in 1999. According to Respondent, SH and YH's investments were mostly in municipal bonds at the beginning of their business relationship while Respondent was employed with Company A. However, SH and YH subsequently expressed dissatisfaction with this investment strategy. SH and YH complained that their portfolio did not grow at the desired rate of return because their investments were solely in municipal bonds and they wanted a better return on his investments. After a discussion regarding equities, Respondent recommended that SH and YH open a second joint account for equities and mutual fund investments. To accomplish this objective, Respondent recommended that as some of SH and YH's municipal bonds matured, they use the bond interest to purchase additional equities and mutual funds. Thus, SH and YH changed their investment objective to growth, which remained their investment objective for the remaining five years their account was with Company A.

In February 2006, after Company A was acquired, Respondent resigned from Company A to work for Firm. SH and YH transferred their assets from Company A and opened four accounts with Firm: 1) a joint account with approximately $1.2 million in municipal bonds ("Account 1"); 2) a joint margin account with approximately $2.8 million in assets ("Account 2"), including $140,000 in cash, $1.5 million in equities and $1.2 million in mutual funds; 3) one IRA account for SH with approximately $34,000 in mutual funds; and 4) one IRA account for YH with approximately $34,000 in mutual funds.

According to SH and YH, they granted written discretion to Respondent over all four accounts. SH and YH claimed that Respondent charged them full commissions on all trades when they should have been entitled to a discounted rate based on the size of their investment accounts. Respondent carried margin balances between $1 and $2 million in SH and YH's margin account, and the margin balance grew to approximately $4 million in 2008. Respondent and his firm collected over $580,000 in trading commissions over a three-year period. Respondent and his firm collected over $122,000 in margin interest alone during the period. SH and YH alleged that between the commissions and margin interest, Respondent and his firm were collecting 8% a year in fees from them.

In Respondent's Answer to the SOC, he stated that SH and YH never complained about the commission and margin interest charges at the time they were incurred and paid. All the charges were in accordance with the governing agreements and fully disclosed.

SH and YH further alleged that Respondent engaged in inappropriate and unsuitable options trading in their accounts. In June 2008, Respondent sold 100 put options of the stock at a strike price of $140. When the option expired, the stock share price had dropped to $121 per share and SH and YH were obligated to purchase 100 shares of the stock at $140 for a total cash outlay of $1.4 million, representing approximately 35% of SH and YH's net equity in their account. This resulted in an overconcentration of the stock in SH and YH's account and an unrealized loss of over $180,000.

According to SH and YH, the next day Respondent sold another 100 put options of the stock at a $125 strike price, betting that the stock would rebound. Instead, when the option expired, the stock price had dropped to $100 per share, and SH and YH were obligated to purchase another 10,000 shares of the same stock for $1.25 million. This resulted in an immediate unrealized loss of $250,000. To cover this purchase of stock, Respondent used all SH and YH's available margin, causing the margin debt to rise to over $4 million. In order to meet the minimum margin call, Respondent sold over $1 million worth of mutual funds in SH and YH's account. Thus, SH and YH were invested in $2.65 million worth of the stock, which continued to fall. In October 2008, Respondent sold all 20,000 shares of stock for $33.59 a share. The realized loss on this transaction was almost $2 million. SH and YH claim that Respondent's discretionary trading caused them more than $2.8 million in losses.

In Respondent's Answer to the FINRA SOC, he denied all allegations of wrongdoing and stated that SH and YH sought to erase the losses they suffered as a result of the 2008 market crisis, and have Respondent guarantee the performance of their investments. When SH and YH opened the accounts in 2006, SH was employed as an Assistant Attorney General with the Attorney General's office and YH worked as a teacher at a community college. Their stated annual income was between $50,000 and $100,000 and their combined net worth, excluding their home, was between $1 and $5 million.

SH and YH's accounts at Firm were not discretionary in nature. Respondent stated that he discussed each transaction with SH and received his authorization before initiating any trade. The primary investment objective for SH and YH's joint accounts was growth with high risk and the secondary investment objective was speculation with high risk. In connection with the opening of Account 2, SH and YH requested and received a margin loan feature. SH and YH also executed an Option Agreement and Suitability Form in order to trade options in the account. SH and YH reported extensive experience with equities, bonds, and other investments on the four January 5, 2006 account-opening forms they signed at Firm. In addition, when seeking approval to trade options in their accounts, SH and YH reported 30 years of experience with equities and 10 years of experience with options. SH and YH's investment objectives were noted on their new account forms, account verification letters and each monthly account statement.

In response to SH and YH's allegations concerning the stock, Respondent stated that Firm's Compliance Department mailed notices to SH and YH about the concentrated positions in Account 2. Over the course of 27 months, the Compliance Department sent out 15 notices stating a concentrated position in one stock that ranged from 19.82% to a high of 49.14% of the account balance. The notices informed SH and YH of the concentrated position and stated that any decline in the value of that security would adversely reduce the balance in the account. The Firm Compliance Department also mailed a letter to SH and YH on August 4, 2008, informing them that the stock comprised 32.17% of the account balance in Account 2. In addition, Firm mailed an August 4, 2008 letter to SH and YH regarding a 43.84% concentration in a second stock CF Industries. These two concentrated positions represented more than 76% of Account 2's investment balance.

According to Respondent, SH and YH transferred a total of 16 securities into Account 2. The size of the positions ranged from approximately $50,000 to $545,000, with an average size of $200,000. Respondent stated that these investments were consistent with SH and YH's investment objectives of growth with high risk and speculation with high risk, which was evidence that SH and YH had a history of taking large positions and that they continued that practice at Firm.

By August 2008, SH and YH had realized a profit in excess of $1 million in Account 2 and had an account balance of more than $4 million. The account had only five stock positions as of August 2008. Respondent discussed liquidation with SH and suggested an exit strategy that contained alternatives to reduce risk, but SH was unwilling to make any changes because of the large gains Account 2 experienced in 2008. In September 2008, Account 2 lost $2.7 million and in October 2008, it lost another $1 million in value.

The exhibits attached to Respondent's Answer to the SOC appeared to support Respondent's version of the facts regarding SH and YH's investment objectives and risk tolerance. There was controversy surrounding Respondent's exhibits, specifically the account opening documents signed by SH and YH. Upon closer examination, it is clear that white-out was used on all four account opening documents, indicating that SH and YH's investment objectives were changed after the documents were executed.

SH and YH switched advisors in November 2008. The SH Arbitration was settled for $1.1 million in May 2010. In Respondent's FINRA BrokerCheck report, the firm stated that Respondent was responsible for the full amount of the settlement. However, Respondent stated that he was not asked to contribute to the settlement.

According to Respondent's BrokerCheck record, Firm terminated Respondent on December 15, 2009, because of a pending legal claim involving large investment losses and Respondent's failure to follow firm policy regarding altered documents discovered during a FINRA Inquiry. Respondent stated that as of August 2012, there were no allegations that he falsified client information. Rather, Respondent altered the applications to correct certain incorrect information. In response to CFP Board's request for a copy of Firm's termination letter to Respondent, he stated that Firm did not terminate him in writing.

2009 FINRA Investigation and 2012 FINRA Letter of Acceptance, Waiver and Consent ("AWC")

FINRA opened an investigation into Respondent's conduct in 2009. In January 2010, FINRA sent Respondent an inquiry letter requesting information related to the 2009 SH and YH Arbitration and the use of options in SH and YH's account. Respondent responded to FINRA in January 2010. Respondent admitted to using Whiteout to change SH and YH's investment objective/risk tolerance.

According to the 2012 FINRA AWC, in January 2006, upon commencing his employment with Firm, and on two additional occasions in 2008, Respondent altered information on certain new account forms as an accommodation to his customers. Specifically, upon discovering apparent discrepancies on the new account forms related to the customers' account profile information, Respondent covered the incorrect information with Whiteout and inputted the correct information on their original new account forms, rather than have the customers complete and return revised new account forms to the firm. Respondent then entered the updated account information into the firm's electronic account system, which triggered the mailing of an account information-verification letter to each of the customers, highlighting Respondent's changes to the new account forms. By altering the original new account forms and causing the firm to retain and preserve altered records, Respondent violated NASD Conduct Rules 2110 and 3110.

Respondent stated that SH and YH's account was one example of the new client records he altered because they contained incorrect information. Respondent stated that his practice was to contact the client to confirm the correct information and then reflect the corrections on the client record. Respondent stated that SH and YH originally indicated that they had moderate experience with equities, bonds, options/futures and margin trading, and that they had a growth objective with medium risk tolerance and no secondary risk objective. Respondent amended the forms to reflect that SH and YH had: 1) extensive experience with equities, bonds, options/futures, and margin trading; and 2) a primary objective of growth with a high risk-tolerance and a secondary objective of speculation with a high risk-tolerance.

Respondent stated that, as was his practice, prior to making the changes to the account opening documents, he called SH who gave his verbal approval for the changes. Respondent explained to SH that per firm policy, a copy of all the corrected forms would be mailed to him for review and verification. After SH received the account-verification information, he did not indicate that the changes Respondent made were inaccurate. Later, Firm terminated Respondent after discovering that Respondent made changes to SH and YH's new account records, instead of sending the clients new forms to execute, in violation of the firm's policy.

Respondent signed the AWC in July 2012 and FINRA's Office of Disciplinary Affairs accepted the AWC in August 2012. FINRA suspended Respondent for 45 days, from September 2012 to October 2012, and issued Respondent a $10,000 fine. Respondent was also required to re-take and pass the Series 7 exam in order to re-qualify as a General Securities Representative, which he did on October 2012. Respondent failed to notify CFP Board within 30 days of his FINRA suspension, as he was required to do pursuant to Article 12.2 of the *Disciplinary Rules*.

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.

CFP Board's Complaint alleged that Respondent failed to exercise reasonable and prudent professional judgment in providing professional services when he: 1) sold 20,000 stock put options in SH and YH's account, resulting in a total unrealized loss of $430,000 and a realized loss of almost $2 million; 2) charged SH and YH full commissions on their trades when they should have been entitled to discounted rates based on the size of their investment accounts; 3) charged SH and YH an exorbitant fee of 8% a year; and 4) altered the clients' new account forms with White-out, causing Firm to retain and preserve altered records, in violation of firm policy and NASD Conduct Rules 2110 and 3110.

The Commission determined that Respondent did not have discretionary control over SH and YH's account. In addition, the Commission determined that the record did not contain any evidence indicating that the options purchases were unsuitable for SH and YH. With respect to the discount rates, the Commission determined that the record did not contain any substantiation for the allegation that SH and YH were eligible to receive a discounted commission rate. The Commission also determined that there was no evidence that the fees were exorbitant. Respondent disclosed the fees to SH and YH who had the opportunity to attempt to reduce the fee by moving their account to a fee-based account. It is notable that SH and YH chose not to make any changes to their accounts despite signing documents indicating that it would be to their advantage to make the change. Finally, with respect to the document alteration, Respondent admitted that he engaged in this conduct. Respondent presented compelling testimony that he has a disease that forces him to ensure that documents are accurate. Respondent should have made arrangements for heightened supervision of his activities due to this disease. Thus, Respondent violated *Code of Ethics* Rule 201.

B. Rule 202 Violation – A CFP Board designee shall act in the interest of the client.

CFP Board's Complaint alleged that Respondent failed to act in the interest of his clients when he: 1) sold 20,000 stock put options in SH and YH's account, resulting in a total unrealized loss of $430,000 and a realized loss of almost $2 million; 2) charged SH and YH full commissions on their trades when they should have been entitled to a discounted rate based on the size of their investment accounts; 3) charged SH and YH an exorbitant fee of 8% a year; and 4) altered the clients' new account forms with White-out to reflect changes in their risk-tolerance and experience, rather than have the clients complete and return revised new account forms to the firm.

The Commission determined that Respondent acted in the interest of his clients. Respondent met with his clients regularly to ensure they were aware of and agreed with the investment strategy in place. Thus, Respondent did not violate *Code of Ethics* Rule 202.

C. Rule 405 Violation – A CFP Board designee shall set fair and reasonable compensation.

CFP Board's Complaint alleged that Respondent failed to set fair and reasonable compensation when he charged the SH and YH an exorbitant fee of eight percent a year to manage their portfolio. The Commission determined that the compensation charged by Respondent was fair and reasonable. The record reflected that the SH and YH were aware of Respondent's compensation and had several opportunities to change the fee structure, including through notification by Firm that a fee-based account would be better for them, but they refused to make the change. Thus, Respondent did not violate *Code of Ethics* Rule 405.

D. Rule 406 Violation – A CFP Board designee shall perform professional services with dedication to the lawful objectives of the employer and/or in accordance with the Code of Ethics.

The Commission determined that Respondent failed to perform services with dedication to the lawful objectives of the employer when he altered his clients' new account forms with Whiteout, causing his firm to retain and preserve altered records, in violation of Firm's policy and NASD Conduct Rules 2110 and 3110. Respondent admitted that he engaged in this conduct. Respondent presented compelling testimony that he has a disease that forces him to ensure that documents are accurate. Respondent should have made arrangements for heightened supervision of his activities due to this disease. Thus, Respondent violated *Code of Ethics* Rule 406.

E. Rule 606(a) Violation – A CFP Board designee shall perform services in accordance with applicable laws, rules and regulations of governmental agencies and other applicable authorities.

The Commission determined that Respondent failed to perform services in accordance with applicable laws, rules and regulations of governmental agencies and other applicable authorities when he altered his clients' new account forms with Whiteout, causing his firm to retain and preserve altered records, in violation of Firm's policy, and NASD Conduct Rules 2110 and 3110. Respondent admitted that he engaged in this conduct. Respondent presented compelling testimony that he has a disease that forces him to ensure that documents are accurate. Respondent should have made arrangements for heightened supervision of his activities due to this disease. Thus, Respondent violated *Code of Ethics* Rule 606(a).

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

CFP Board's Complaint alleged that Respondent failed to perform services in accordance with applicable rules, regulations and other established policies of CFP Board when he: 1) sold 20,000 stock put options in SH and YH's account, resulting in a total unrealized loss of $430,000 and a realized loss of almost $2 million; 2) charged SH and YH full commissions on their trades when they should have been entitled to a discounted rate based on the size of their investment accounts; 3) charged SH and YH an exorbitant fee of 8% a year; 4) altered the clients' new account forms with White-out, causing Firm to retain and preserve altered records, in violation of firm policy, and NASD Conduct Rules 2110 and 3110; and 5) over-concentrated SH and YH's portfolio in stock.

The Commission determined that Respondent did not have discretionary control over SH and YH's account. In addition, the Commission determined that the record did not contain any evidence indicating that the options purchases were unsuitable for SH and YH. With respect to the discount rate, the Commission determined that the record did not contain any substantiation for the allegation that SH and YH were eligible to receive a discounted commission rate. The Commission also determined that there was no evidence that the fees were exorbitant. Respondent disclosed the fees to SH and YH who had the opportunity to attempt to reduce the fee by moving their account to a fee-based account. It is notable that SH and YH chose not to make any changes to their accounts despite signing documents indicating that it would be to their advantage to make the change. Finally, with respect to the document alteration, Respondent admitted that he engaged in this conduct. Respondent presented compelling testimony that he has a disease that forces him to ensure that documents are accurate. Respondent should have made arrangements for heightened supervision of his activities due to this disease. Thus, Respondent violated *Code of Ethics* Rule 606(b).

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

CFP Board's Complaint alleged that Respondent engaged in conduct that reflects adversely on his integrity and fitness as a CFP® professional, upon the CFP® marks and upon the profession when he: 1) sold 20,000 stock put options in SH and YH's account, resulting in a total unrealized loss of $430,000 and a realized loss of almost $2 million; 2) charged SH and YH full commissions on their trades when they should have been entitled to a discounted rate based on the size of their investment accounts; 3) charged SH and YH an exorbitant fee of 8% a year; and 4) altered his clients' new account forms with White-out, causing Firm to retain and preserve altered records, in violation of firm policy and NASD Conduct Rules 2110 and 3110.

The Commission determined that Respondent did not have discretionary control over SH and YH's account. In addition, the Commission determined that the record did not contain any evidence indicating that the options purchases were unsuitable for SH and YH. With respect to the discount rate, the Commission determined that the record did not contain any substantiation for the allegation that SH and YH were eligible to receive a discounted commission rate. The Commission also determined that there was no evidence that the fees were exorbitant. Respondent disclosed the fees to SH and YH who had the opportunity to attempt to reduce the fee by moving their account to a fee-based account. It is notable that SH and YH chose not to make any changes to their accounts despite signing documents indicating that it would be to their advantage to make the change. Finally, with respect to the document alteration, Respondent admitted that he engaged in this conduct. Respondent presented compelling testimony that he has a disease that forces him to ensure that documents are accurate. Respondent should have made arrangements for heightened supervision of his activities due to this disease. Thus, Respondent violated *Code of Ethics* Rule 607.

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

The Commission determined that Respondent failed to provide services diligently when he altered his clients' new account forms with White-out to reflect changes in their risk-tolerance and experience, rather than have the clients complete and return revised new account forms to the firm, thereby causing Firm to retain and preserve altered records. Respondent admitted that he engaged in this conduct. Respondent presented compelling testimony that he has a disease that forces him to ensure that documents are accurate. Respondent should have made arrangements for heightened supervision of his activities due to this disease. Thus, Respondent violated *Code of Ethics* Rule 701.

I. Rule 6.5 Violation – 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® professional, upon the CFP® marks and upon the profession when he was suspended by FINRA for altering his clients' new account forms with White-out and causing Firm to retain and preserve altered records, in violation of firm policy and NASD Conduct Rules 2110 and 3110. Respondent admitted that he engaged in this conduct. Respondent presented compelling testimony that he has a disease that forces him to ensure that documents are accurate. Respondent should have made arrangements

arrangements for heightened supervision of his activities due to this disease. Thus, Respondent violated *Rules of Conduct* Rule 6.5.

IV. Discipline Imposed

The Commission found grounds for discipline under Article 3(a), 3(d) and 3(e) of CFP Board's *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* or *Rules of Conduct*. The Commission found grounds for discipline under Article 3(a) because Respondent violated Rules 201, 406, 606(a), 606(b), 607 and 701 of the *Code of Ethics* and Rule 6.5 of the *Rules of Conduct.* Article 3(c) provides grounds for discipline for any act that is the proper basis for professional discipline. The Commission found grounds for discipline under Article 3(d) because FINRA suspended Respondent for 45 days. Article 3(e) provides grounds for discipline for any act or omission that violates the *Disciplinary Rules*. The Commission found grounds for discipline under Article 3(e) because Respondent failed to notify CFP Board within 30 days of his FINRA suspension, as he was required to do pursuant to Article 12.2 of the *Disciplinary Rules*. Pursuant to Article 4.1 of the Disciplinary Rules, the Commission issued a Private Censure to Respondent.

The Commission considered as mitigating factors that:

1. Respondent no longer trades options for clients;
2. SH and YH were provided with the chance to reduce the volatility and the costs of their account but chose not to;
3. The document alterations were done as client accommodations; and
4. Respondent advises most of his clients to move their money to managed fee-based accounts.

The Commission considered as an aggravating factor that Respondent should have made arrangements for heightened supervision of his activities due to his disease.

The Commission consulted Anonymous Case Histories ("ACH") 22798 and 27087. Both ACHs involved the alteration of a document that was done as a client accommodation and resulted in either a private censure or a dismissal with caution. The Commission determined that Respondent's actions did not warrant a public disciplinary action based on the ACHs cited and the mitigating factors listed above. Respondent has clearly demonstrated that he is taking steps to change his practice and avoid practices such as options trading. The Commission encouraged Respondent to request heightened supervision to ensure he is not continuing to alter documents and engage in options trading.