

CERTIFIED FINANCIAL PLANNER BOARD OF STANDARDS, INC.

ANONYMOUS CASE HISTORIES  
NUMBER 27735

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This is a summary of a decision issued following the February 2014 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. Issue Presented

Whether a CFP® professional (“Respondent”) violated CFP Board’s *Standards of Professional Conduct* when she: 1) recommended that a client, a risk-adverse retiree, invest \$100,000 into The Fund, an investment that Respondent described as a partnership, but which was in actuality a hedge fund; 2) failed to disclose the conflict of interest that existed as a result of Respondent’s role as Advisor for The Fund; 3) recommended The Fund to Grievant although Respondent when the client may not have met the requirements to be an accredited investor; and 4) denied any remunerative connection to The Fund, despite her advisory role.

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

*Initiation of Relationship with Grievant*

Respondent and Grievant began a relationship in February 2008. Respondent informed Grievant that she was a CFP® professional and that she welcomed the opportunity to meet with Grievant regarding her financial planning needs. Respondent asked Grievant to complete and fill out the following forms and provide the following documents for their first meeting:

- Risk Tolerance Analysis Form
- Budget and Personal Information Forms
- Front page of all insurance documents (listing policy amounts)
- Most recent investment statements
- Tax Sheltered Annuities, if you are a participant
- Annuities, if you are invested in them
- Statements for any CD’s, Money Market Accounts, Savings Accounts, Demand Deposit (checking) Accounts
- Required Minimum Distributions (RMDs) information
- Last completed tax return

Respondent performed a Risk Tolerance Analysis for Grievant that was signed by both Grievant and Respondent. Respondent’s firm classified risk into five categories, based on the investor’s score in response to certain questions:

- |                    |       |
|--------------------|-------|
| 1. Current Income  | 9-16  |
| 2. Balanced        | 16-22 |
| 3. Growth & Income | 22-37 |
| 4. Growth          | 28-37 |
| 5. Maximum Growth  | 37-45 |

Grievant's score of 21 indicated that she had a balanced risk profile in Respondent's risk classification system. Grievant was a 73-year old retiree. Grievant stated that she sought Respondent's assistance with consolidating her retirement assets in order to ensure her disabled son's financial security in the future.

According to the 2008 and 2009 risk tolerance questionnaires, Grievant was prepared to take only a small degree of risk with her finances. The 2009 analysis showed that the best investment portfolio for Grievant would be: 1) 50% low risk/return investments; 2) 40% medium risk/return investments; and 3) 10% high risk/return investments.

Grievant and Respondent executed an agreement for investment management services ("Advisory Agreement") in July 2008, which gave Respondent discretionary control over the client's account.

Respondent stated that in addition to helping Grievant with investment advisory services, she and the Grievant also discussed financial planning and estate planning for Grievant and her son. Respondent agreed to provide an attorney referral to Grievant for Estate Planning services. According to Grievant, Respondent introduced her to the Estate Planning attorney in November 2008. Although Grievant did not initially have a formal financial plan, Respondent worked with Grievant's attorney to devise an estate plan for the client

#### *Recommendation of The Fund*

In addition to other recommendations, Respondent recommended that Grievant place \$100,000 into The Fund, an investment that Respondent described as a partnership. Respondent described The Fund as being in the "safety" investment category. The Fund was created for Respondent by The Fund's General Partner, who controlled The Fund.

The Confidential Private Offering Memorandum ("Offering Memorandum") for The Fund stated that an investor must be accredited and that an investment in The Fund was designed for sophisticated investors who were able to bear the loss of a substantial part of their investment. The Offering Memorandum also stated that the investment may be speculative. According to The Fund's Regulation D filing with the SEC, The Fund was a hedge fund that invested primarily in life insurance premium financing with the remaining funds invested with six money managers.

According to the Respondent's Firm's ADV, in order to be considered accredited for investment in The Fund, a client must invest a minimum of \$750,000 with the Firm or possess a net worth of at least \$1.5 million. Excluding Grievant's home, per SEC regulations, Grievant's net worth was less than \$1.5 million, and according to her portfolio holding statements, Grievant never had more than \$750,000 invested with the Firm.

According to The Fund Subscription Agreement, an accredited investor must have income in excess of \$200,000 in each of the previous two years and an expectation of making the same income in the coming year, or have a net worth in excess of \$1 million. Grievant was a retiree and her income was \$60,000 per annum, primarily earned from a pension and other investments. Grievant's net worth was less than \$1 million.

According to Grievant, Respondent failed to disclose the conflict of interest that existed as a result of Respondent's recommendation of The Fund to Grievant because Respondent served as Advisor for The Fund. Grievant also stated that Respondent denied any remunerative connection to The Fund, despite her advisory role. Grievant further stated that Respondent used her investment seminars offered to recruit new investors, without informing them of the risks associated with the investments she recommended.

According to Respondent, The Fund failed for two reasons: 1) the 2008-2009 market decline; and 2) alleged improprieties by the General Partner. As a result, the Firm resigned from serving as The Fund's Investment Advisor in November 2009 and notified law enforcement agencies, including the FBI, of the improprieties. Grievant was informed of the improprieties as they arose and blamed Respondent for the decline in her investments. By April 29, 2011, Grievant's \$100,000 investment had dwindled to \$1,619.53.

### *Other Investments*

Grievant stated that although The Fund was the focus of her grievance against Respondent, she had other issues and concerns regarding Respondent's recommendations to her. In April 2008, Respondent recommended the following investments to Grievant: 1) \$100,000 in The Fund, which Respondent classified as being in the safety investment category; 2) transfer an IRA to the Monday Fund managed by Interactive Brokers; 3) \$100,000 in American Funds; 4) transfer a TIAA-CREF Annuity to Allianz to receive a 7% guarantee; 5) transfer \$47,000 in an SII Brokerage TOD accounts to Schwab to invest in municipal bonds; and 6) \$58,000 in the bank for emergencies. These investment recommendations totaled \$528,000

### III. Commission's Analysis and Conclusions Regarding 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.*

CFP Board's Complaint alleged that Respondent engaged in conduct involving dishonesty, fraud, deceit or misrepresentation or knowingly made a false or misleading statement to a client when she: 1) recommended that Grievant invest \$100,000 into The Fund that Respondent described as being in a "safety" investment category, but which was actually a hedge fund; 2) failed to disclose the conflict of interest that existed as a result of Respondent's role as Advisor for The Fund; and 3) denied any remunerative connection to The Fund, despite her advisory role.

The Commission determined that CFP Board did not provide sufficient evidence to prove the allegations in its Complaint. The Commission determined that Respondent did not knowingly make a false statement regarding The Fund, but rather, was simply unknowledgeable regarding The Fund. Respondent failed to perform sufficient due diligence or research to fully educate herself on the exact details of The Fund, and as a result, Respondent failed to fully understand the risks associated with an investment in The Fund. 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.*

CFP Board's Complaint alleged that Respondent failed to exercise reasonable and prudent professional judgment in providing professional services when she: 1) recommended that Grievant, a risk-adverse retiree, invest \$100,000 into The Fund, an investment that Respondent described as a partnership, but which was in actuality a hedge fund; 2) failed to disclose the conflict of interest that existed as a result of Respondent's role as Advisor for The Fund; 3) recommended The Fund to Grievant although Respondent knew that the client was not an accredited investor; and 4) denied any remunerative connection to The Fund, despite her advisory role.

The Commission determined that CFP Board did not provide sufficient evidence to prove the allegations in its Complaint relating to a misrepresentation of fact. The Commission determined that Respondent did not knowingly make false statements regarding The Fund, but rather, was simply unknowledgeable regarding The Fund. Respondent failed to perform sufficient due diligence or research to fully educate herself on the exact details of The Fund, and as a result, Respondent failed to fully understand the risks associated with an investment in The Fund. The Commission determined, however, that Respondent's recommendation that Grievant invest in The Fund was unreasonable and imprudent given Grievant's assets and stated investment objectives. Thus, Respondent violated *Code of Ethics* Rule 201.

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

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CFP Board's Complaint alleged that Respondent failed to act in the interest of the client when she: 1) recommended that Grievant invest \$100,000 into The Fund that Respondent described as being in a "safety" investment category, but which was actually a hedge fund; 2) failed to disclose the conflict of interest that existed as a result of Respondent's role as Advisor for The Fund; and 3) recommended The Fund to Grievant although Respondent knew that the client was not an accredited investor.

The Commission determined that CFP Board did not provide sufficient evidence to prove the allegations in its Complaint relating to a misrepresentation of fact. The Commission determined that Respondent did not knowingly make false statements regarding The Fund, but rather, was simply unknowledgeable regarding The Fund. Respondent failed to perform sufficient due diligence or research to fully educate herself on the exact details of The Fund, and as a result, Respondent failed to fully understand the risks associated with an investment in The Fund.

The Commission determined that the circumstances as detailed in the factual findings demonstrated that Respondent and Grievant were in a financial planning relationship. The Commission further determined that Respondent's recommendation that Grievant invest in The Fund was not in the interest of Grievant given Grievant's assets and stated investment objectives. Thus, Respondent violated *Code of Ethics* Rule 202.

*D. 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.*

CFP Board's Complaint alleged that Respondent failed to disclose to the client material information relevant to the professional relationship when she: 1) informed Grievant that The Fund was a safe investment, although it was actually a hedge fund; and 2) failed to disclose the conflict of interest that existed as a result of Respondent's role as Advisor for The Fund.

The Commission determined that CFP Board did not provide sufficient evidence to prove the allegations in its Complaint relating to a misrepresentation of fact. The Commission determined that Respondent did not knowingly make false statements regarding The Fund, but rather, was simply unknowledgeable regarding The Fund. Respondent failed to perform sufficient due diligence or research to fully educate herself on the exact details of The Fund, and as a result, Respondent failed to fully understand the risks associated with an investment in The Fund. Thus, Respondent did not violate *Code of Ethics* Rule 401(a).

*E. Rule 606(b) – 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 she: 1) recommended that Grievant invest \$100,000 into The Fund that Respondent described as being in a "safety" investment category, but which was actually a hedge fund; 2) failed to disclose the conflict of interest that existed as a result of Respondent's role as Advisor for The Fund; 3) recommended The Fund to Grievant although Respondent knew that the client was not an accredited investor; and 4) denied any remunerative connection to The Fund, despite her advisory role, thereby violating Rules 102, 201, 202, 401(a), 607 and 703.

The Commission determined that CFP Board did not provide sufficient evidence to prove the allegations in its Complaint relating to a misrepresentation of fact. The Commission determined that Respondent did not knowingly make false statements regarding The Fund, but rather, was simply unknowledgeable regarding The Fund. Respondent failed to perform sufficient due diligence or research to fully educate herself on the exact details of The Fund, and as a result, Respondent failed to fully understand the risks associated with an investment in The Fund.

The Commission determined that Respondent's recommendation that Grievant invest in The Fund was not in the interest of Grievant given Grievant's assets and stated investment objectives. Thus, Respondent violated *Code of Ethics* Rule 606(b).

*F. 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.*

CFP Board's Complaint alleged that Respondent engaged in conduct that reflects adversely on his or her integrity and fitness as a CFP Board designee, upon the CFP® marks and upon the profession when she: 1) recommended that Grievant invest \$100,000 into The Fund that Respondent described as being in a "safety" investment category, but which was actually a hedge fund; 2) failed to disclose the conflict of interest that existed as a result of Respondent's role as Advisor for The Fund; 3) recommended The Fund to Grievant although Respondent knew that the client was not an accredited investor; and 4) denied, to Grievant, any remunerative connection to The Fund, despite her advisory role.

The Commission determined that CFP Board did not provide sufficient evidence to prove the allegations in its Complaint relating to a misrepresentation of fact and whether Grievant was an accredited investor. The Commission determined that Respondent did not knowingly make false statements regarding The Fund, but rather, was simply unknowledgeable regarding The Fund. Respondent failed to perform sufficient due diligence or research to fully educate herself on the exact details of The Fund, and as a result, Respondent failed to fully understand the risks associated with an investment in The Fund. The Commission determined, however, that Respondent's recommendation that Grievant invest in The Fund was not in the client's interest and reflected adversely on her integrity and fitness as a CFP® professional, on the marks and on the profession given Grievant's assets and stated investment objectives. Thus, Respondent violated *Code of Ethics* Rule 607.

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

CFP Board's Complaint alleged that Respondent failed to make and/or implement only recommendations that are suitable for the client when she: 1) recommended that Grievant, a risk-adverse retiree, invest \$100,000 into The Fund, an investment that Respondent described as a partnership, but which was in actuality a hedge fund; and 2) recommended The Fund to Grievant although Respondent knew that the client was not an accredited investor.

The Commission determined that CFP Board did not provide sufficient evidence to prove the allegations in its Complaint relating to a misrepresentation of fact. The Commission determined that Respondent did not knowingly make false statements regarding The Fund, but rather, was simply unknowledgeable regarding The Fund. Respondent failed to perform sufficient due diligence or research to fully educate herself on the exact details of The Fund, and as a result, Respondent failed to fully understand the risks associated with an investment in The Fund. The Commission determined, however, that Respondent's recommendation that Grievant invest in The Fund was not suitable for Grievant given her assets and stated investment objectives. Thus, Respondent violated *Code of Ethics* Rule 703.

*H. Practice Standard 500-2 – The financial planning practitioner shall select appropriate products and services that are consistent with the client's goals, needs and priorities.*

The financial planner's responsibilities include investigating products and services that reasonably address the client's needs and selecting products and services that are suitable and consistent with the client's goals, needs and priorities. The Commission determined that Grievant's primary objectives were to consolidate her retirement assets

in order to ensure her disabled son's financial security in the future. Respondent failed to appropriately address Grievant's stated investment objectives needs when she recommended that the client invest \$100,000 into The Fund and which she described as being in a "safety" investment category, but which was in actuality a hedge fund. Thus, Respondent violated *Practice Standard* 500-2.

#### IV. Discipline Imposed

The Commission found grounds for discipline under Articles 3(a) and 3(b) of CFP Board's *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*. 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*. Article 3(b) of CFP Board's *Disciplinary Rules* provides grounds for discipline for any act or omission that violates the *Financial Planning Practice Standards*. The Commission found grounds for discipline under Article 3(b) because Respondent violated *Practice Standard* 500-2. Pursuant to Article 4.2 of the *Disciplinary Rules*, the Commission issued the Respondent a Public Letter of Admonition.

In mitigation, the Commission considered the following factors:

1. Respondent had 30 years of experience with no prior disciplinary history;
2. Respondent's attorney represented during the hearing that 45 of the 46 investors in The Fund were still Respondent's clients;
3. Respondent expended much effort to try to minimize the impact of The Fund's decline on clients;
4. Respondent's conduct was not part of a pattern of conduct; and
5. Respondent demonstrated exemplary conduct since the incident, which occurred over five years ago.

In aggravation, the Commission considered the following factors:

1. Respondent failed to adequately understand the risks associated with The Fund; and
2. Respondent failed to properly oversee the original general partner of The Fund despite knowing he had previously been suspended by the Securities and Exchange Commission.

In arriving at its decision, the Commission consulted *Sanction Guideline* 31 (Suitability). The Commission also consulted Anonymous Case Histories 25999, 25389 and 26746. The Commission determined to deviate from the *Sanction Guidelines* and the ACHs given the mitigating factors listed above and due to the fact that the Commission determined Respondent did not knowingly make a misstatement of fact. The Commission also considered that while the investment turned out to be unsuitable for Grievant, Respondent's error was that she failed to perform sufficient due diligence on The Fund to ensure a complete understanding of the investment.