

CERTIFIED FINANCIAL PLANNER BOARD OF STANDARDS, INC.

ANONYMOUS CASE HISTORIES  
NUMBER 27930

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This is a summary of a Settlement Agreement entered into at 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 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 CFP® professional (“Respondent”) violated CFP Board’s *Standards of Professional Conduct* when he: 1) did not perform due diligence on a 1031 exchange intermediary prior to recommending him to his clients as a Qualified Intermediary for 1031 exchanges; and 2) failed to immediately report to his employer that Intermediary had borrowed clients’ funds to repay his own Internal Revenue Service (“IRS”) tax liability, and instead loaned Intermediary the money to repay the borrowed funds.

II. Findings of Fact

***2008 Firm Termination***

In late 2007, Respondent had Client 1 and Client 2 participate in a 1031 exchange where a property was sold and the proceeds went to a Qualified Intermediary (“Intermediary”), whom Respondent recommended. The proceeds were to be invested in a Tenancy-In-Common 1031 investment that was offered through Firm. When the time came to transfer the money to the new investment, Respondent could not locate Intermediary. A few days later, Intermediary came to Respondent’s office and explained that he had spent some of the proceeds, approximately \$64,000, in order to satisfy an IRS tax liability. Intermediary thought he could replace the funds by borrowing against a rental property, but that did not work out. Intermediary then asked Respondent if Respondent could loan him the amount necessary to complete the 1031 exchange. Respondent and Intermediary were running out of time to complete the transaction, so Respondent used an equity line of credit on his house to loan Intermediary the necessary funds. The loan was secured by mortgages against three properties Intermediary owned. Respondent stated that he kept Client 1 apprised of the situation, informing him that he was loaning money to Intermediary so that the 1031 exchange could be completed. Intermediary thought he could repay Respondent with income earned during tax season since he was also a certified public accountant (“CPA”). Intermediary never repaid Respondent and Respondent foreclosed on one of the properties.

After selling the foreclosed property, Respondent lost \$19,000 on the loan. Respondent’s actions did not harm Client 1 and Client 2 because the 1031 exchange was completed. After the exchange, a Sheriff’s Department investigator interviewed Respondent about the 1031 exchange as part of their investigation into Intermediary’s possible thefts from clients. Respondent informed Firm regarding the investigation. Firm then reviewed all the documentation regarding the transaction. Two days later, Firm discharged Respondent, stating that he had violated Firm’s internal policies and procedures.

In December 2010, Intermediary was convicted of five felony counts of theft by conversion and six felony counts of theft by taking. Prosecutors argued that he was responsible for funneling into his personal and business accounts thousands of dollars that clients had placed in escrow to pay payroll taxes. Intermediary received a 20-year sentence and is currently serving a three-year prison term.

### ***Respondent's Relationship with Intermediary***

Respondent opened his CPA Office in State in late 2005. Intermediary came to Respondent's office to meet the new CPA in town, since he was also a CPA. Intermediary described his practice, which included work as a Qualified Intermediary for 1031 transactions. Respondent told Intermediary about Tenant-In-Common investments that were then available and Intermediary offered his services as a Qualified Intermediary. Respondent referred one of his clients to Intermediary for a 1031 transaction, and that transaction went smoothly. About one year later, another opportunity arose for a 1031 transaction, and Respondent once again referred Client 1 and Client 2 to Intermediary. Respondent referred no other clients to Intermediary.

Respondent stated that Qualified Intermediaries are not licensed and are not required to be bonded. He stated that he knew Intermediary was respected in the local community as a CPA and knew he was a leader in the local veteran's affairs group. Respondent stated that he trusted Intermediary's reputation, and was not sure what else he could have done. Respondent added that he lives in a small community and he was surprised that anyone local offered services as a Qualified Intermediary.

### ***2008 FINRA Investigation***

In August 2008, FINRA began an inquiry into Respondent's termination from Firm. A FINRA Investigator ("Investigator") requested information and documentation regarding the termination and any other matter with Firm that was unresolved or resolved within the last three years. In August 2008, Respondent's attorney ("Attorney") responded on behalf of Respondent to Investigator. In his response, Attorney included an explanation of Client 1 and Client 2's 1031 exchange and Respondent's relationship with Intermediary. Attorney attached several exhibits to his response, including documentation on Client 1 and Client 2's 1031 exchange and a copy of the promissory note Respondent and Intermediary executed. Attorney also stated that Respondent had no other complaints to report from Firm and that to the best of his knowledge, Client 1 and Client 2 had not filed a complaint with Firm. In April 2009, a FINRA Examination Manager ("Examination Manager") sent a letter to Respondent notifying him that FINRA had completed its inquiry into the Firm Termination and determined to take no action and closed its file.

### ***2008 State Securities and Business Regulation Department Investigation***

In September 2008, State's Department of Securities and Business Regulation ("State") began an inquiry into Respondent's termination from Firm. State's Manager of Securities Registration and Licensing requested information and documentation regarding the internal review, termination and regulatory action listed on Respondent's Central Registration Depository record. In October 2008, Attorney responded on behalf of Respondent to State's Manager of Securities Registration and Licensing.

In November 2008, State's Assistant Commissioner of Securities entered into a Conditional Registration Agreement with Respondent. Respondent consented to being placed on heightened supervision for a period of two years, effective November 2008. Respondent stated that he was currently in good standing with both FINRA and State.

### **III. Rule Violations**

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

Respondent failed to exercise reasonable and prudent professional judgment in providing professional services when he: 1) failed to perform proper due diligence on Intermediary prior to recommending him to his clients as

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a Qualified Intermediary for 1031 exchanges; and 2) failed to immediately report to his employer that Intermediary had borrowed clients' funds to repay his own IRS tax liability, and instead loaned Intermediary the money to repay the borrowed funds. Thus, Respondent violated *Code of Ethics* Rule 201.

*B. Rule 406 – 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*

Respondent failed to perform services with dedication to the lawful objectives of the employer and/or in accordance with the *Code of Ethics* when he failed to immediately report to his employer that Intermediary had borrowed clients' funds to repay his own IRS tax liability, and instead loaned Intermediary the money to repay the borrowed funds, violating his firm's internal policies and procedures. Respondent's firm terminated him due to these violations. Thus, Respondent violated *Code of Ethics* Rule 406.

*C. Rule 607 – 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*

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: 1) failed to perform proper due diligence on Intermediary prior to recommending him to his clients as a Qualified Intermediary for 1031 exchanges; and 2) failed to immediately report to his employer that Intermediary had borrowed clients' funds to repay his own IRS tax liability, and instead loaned Intermediary the money to repay the borrowed funds. Thus, Respondent violated *Code of Ethics* Rule 607.

*D. Rule 701 – A CFP Board designee shall provide services diligently*

Respondent failed to provide services diligently when he failed to perform proper due diligence on Intermediary prior to recommending him to his clients as a Qualified Intermediary for 1031 exchanges. Thus, Respondent did not violate *Code of Ethics* Rule 701.

#### IV. Discipline Imposed

The Commission found grounds for discipline under Article 3(a) 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, 406, 607 and 701 of the *Code of Ethics*. The Commission 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 to Respondent a Private Censure pursuant to Article 4.1 of the *Disciplinary Rules*.

In reaching its decision, the Commission considered *Sanction Guideline* 12 (Employer Policy Violation) and did not consult any Anonymous Case Histories.

The Commission did not consider any mitigating or aggravating factors.