CERTIFIED FINANCIAL PLANNER BOARD OF STANDARDS, INC.

ANONYMOUS CASE HISTORIES
NUMBER 28783

This is a summary of a Settlement Agreement entered into at the June 2015 hearings of the Disciplinary and Ethics Commission ("the 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* were Rules 101 through 705.

I. Issues Presented

Whether a CFP® professional ("Respondent") violated CFP Board's *Standards of Professional Conduct* when he: 1) recommend a private placement to clients with low risk tolerances; 2) concentrated a significant percentage of the clients' assets in a private placement; and 3) represented a private placement as having low risk.

II. Findings of Fact

MG Customer Complaint

In August 2011, Respondent disclosed a customer complaint filed by his client, MG, on his Renewal Application for CFP® Certification. MG claimed that Respondent misrepresented the CF Fund as a safe investment and it became worthless.

In an Investment Policy Statement dated August 2006, MG indicated that she wanted retirement, investment, tax, and estate planning services. She also indicated that she had a low risk tolerance and that she planned to retire in 18 months. A Client Account Information Form dated August 2006 indicated that MG was 64-years old and had a net worth of $400,000, which consisted of her $175,000 home, $150,000 liquid assets, and $75,000 non-liquid assets. The form indicated that MG's investment objective was income.

Based on the scope of their engagement, services provided, and comprehensiveness of the data gathering; Respondent was in a financial planning engagement with MG. Respondent addressed the complaint in a letter to GC dated July 2011. Respondent said that, in 2006, MG had a net worth of $400,000, $290,000 of which was investable assets. Respondent also acknowledged that MG wanted a "no-risk investment" and that he told her that the CF Fund was "low risk" and secured by buildings and property. Respondent stated that MG purchased $50,000 of the CF Fund using money rolled over into an IRA account in 2006. MG. purchased an additional $50,000 of the CF Fund using another rollover into the IRA account in November 2007.

In 2011, the CF Fund stopped making payments to investors and began the process of liquidation. MG requested to sell the CF Funds but Respondent told her that he could not because they were in default. Respondent also told MG that "if she tried to sell the certificates now, she'd be lucky to get ten cents on the dollar." In meeting in August 2011with MG and her son in law, Respondent told them that investing $100,000 in the CF Fund was suitable for MG. Respondent also told them that the CF Fund was not rated with a bond credit rating.

In September 2011, GC denied MG's written complaint stating that the CF Funds were not unsuitable and offered her no compensation.

In May 2012, CFP Board closed its investigation into MG's denied customer complaint but CFP Board Counsel reserved the right to reopen the investigation. CFP Board Counsel has reopened the investigation.

DL and JL FINRA Mediation

In September 2013, Respondent disclosed a Financial Industry Regulatory Authority, Inc. ("FINRA") mediation from 2012 on his Renewal Application for CFP® Certification. In an Investment Policy Statement dated April 2007, DL & JL indicated that they wanted estate, investment, retirement, and tax planning services. They also indicated that they had a low tolerance for risk. DL & JL selected a conservation portfolio with benchmarks of 20% equity and 80% fixed/cash. Based on the scope of their engagement, services provided, and comprehensiveness of the data gathering; Respondent was in a financial planning engagement with DL & JL. However, Respondent told CFP Board that he did not prepare or present a formal financial plan to DL & JL.

In May 2007, Respondent recommended and sold DL & JL $250,000 of CF Fund certificates. In April 2008, Respondent recommended that DL & JL invest an additional $86,000 in the CF Fund certificates and they did. Respondent said he presented corporate bonds to DL & JL as an option to the CF Fund, but the interest rates of the corporate bonds were too low. Despite the CF Fund's promises of high returns, Respondent represented the CF Fund to DL & JL as a "low risk investment option" secured by real estate. A Client Account Information Form dated May 2008 indicated that DL & JL were 68 and 63 years old, had a net worth of $2 million, and had an investment objective of preservation of capital. $580,000 of DL & JL's $2 million net worth was real estate consisting of their home and vacation home.

In December 2011, DL called GC to complain about their investment in the CF Fund. A partner at GC, GR, told DL that there was nothing he could do and GR did not offer compensation to DL. In May 2012, DL & JL filed a request for mediation with FINRA Dispute Resolution. In August 2012, GC agreed to pay DL & JL $48,500. GC also paid the mediator's fees.

The CF Fund certificates were unregistered securities sold under an exemption in the Securities Act of 1933 and they promised to pay investors 7% interest. The certificates were not tax exempt, had no formal credit rating, and did not have an established trading market. In addition, loan policies of the Issuer, BF, may be less stringent than loan policies of commercial lenders and, therefore, remedies typically available to a commercial lender or bank may not be available to the Issuer.

The CF Fund certificates were securities equivalent to alternative investments but Respondent represented them to clients as if they were corporate bonds. Respondent represented the unregistered, unrated, illiquid CF Fund certificates to both MG and DL & JL as low risk investments.

In order to determine what amount of alternative investments are suitable for clients, some financial firms develop specific guidelines. LF, an investment advisor and broker-dealer, developed a form titled Alternative Investment Purchase Approved Public Direct Participation Program that contains Alternative Investment Approval Guidelines. The Alternative Investment Approval Guidelines state the maximum percentage of a client's liquid net worth after the purchase that can be invested in alternative investments according a client's investment objective and age. The LF Alternative Investment Approval Guidelines state that the maximum recommended concentration of alternative investments for a 64-year-old client with a $225,000 liquid net worth and an investment objective of income and growth was 20% of liquid net worth. The LF Alternative Investment Approval Guidelines state that the maximum recommended concentration of alternative investments for 63- and 68-year-old clients with a $1,420,000 liquid net worth and an investment objective of capital preservation was 0% of liquid net worth.

Respondent stated the he presented CF Fund prospectuses to the clients. Respondent also stated that he received $2,916 in commissions from his sale of the CF Funds to DL & JL.

III. <u>Grounds for Discipline</u>

First Ground for Discipline

Pursuant to Article 3(a) of the *Disciplinary Rules,* there are grounds to discipline Respondent for acts or omissions that violate Rule 102 of the *Code of Ethics*, which provides that, 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.

Respondent, a CFP Board designee, engaged in conduct involving dishonesty, fraud, deceit or misrepresentation or knowingly made a false or misleading statement to MG, DL & JL when he represented the CF Fund as low risk.

Thus, Respondent violated Rule 102 of the *Code of Ethics*.

Second Ground for Discipline

Pursuant to Article 3(a) of the *Disciplinary Rules*, there are grounds to discipline Respondent for acts or omissions that violate Rule 201 of the *Code of Ethics*, which requires a CFP Board designee to exercise reasonable and prudent professional judgment in providing professional services.

Respondent, a CFP Board designee, failed to exercise reasonable and prudent professional judgment in providing professional services when he recommended and sold $100,000 of CF Fund certificates to MG because: 1) she had a low risk tolerance; and 2) the $100,000 of CF Fund certificates constituted 25% of her total net worth and 44% of her net worth excluding her home.

Respondent, a CFP Board designee, failed to exercise reasonable and prudent professional judgment in providing professional services when he recommended and sold $336,000 of CF Fund certificates to DL & JL because: 1) they had a low risk tolerance and an investment objective of preservation of capital; and 2) the $336,000 of CF Fund certificates constituted 17% of their total net worth and 24% of their net worth excluding homes.

Thus, Respondent violated Rule 201 of the *Code of Ethics*.

Third Ground for Discipline

Pursuant to Article 3(a) of the *Disciplinary Rules,* there are grounds to discipline Respondent for acts or omissions that violate Rule 202 of the *Code of Ethics*, which provides that a financial planning practitioner shall act in the interest of the client.

Respondent, a financial planning practitioner, failed to act in MG's interest when he recommended and sold $100,000 of CF Fund certificates to her because: 1) she had a low risk tolerance; and 2) the $100,000 of CF Fund certificates constituted 25% of her total net worth and 44% of her net worth excluding her home.

Respondent, a financial planning practitioner, failed to act in DL & JL's interest when he recommended and sold $336,000 of CF Fund certificates to them because: 1) they had a low risk tolerance and an investment objective of preservation of capital; and 2) the $336,000 of CF Fund certificates constituted 17% of their total net worth and 24% of their net worth excluding homes.

Thus, Respondent violated Rule 202 of the *Code of Ethics*.

Fourth Ground for Discipline

Pursuant to Article 3(a) of the *Disciplinary Rules*, there are grounds to discipline Respondent for acts or omissions that violate Rule 703 of the *Code of Ethics*, which provides that a financial planning practitioner shall make and/or implement only recommendations that are suitable for the client.

Respondent, a financial planning practitioner, made and implemented unsuitable recommendations to MG when he recommended and sold $100,000 of CF Fund certificates to her because: 1) she had a low risk tolerance; and 2) the $100,000 of CF Fund certificates constituted 25% of her total net worth and 44% of her net worth excluding her home.

Respondent, a financial planning practitioner, made and implemented unsuitable recommendations to DL & JL when he recommended and sold $336,000 of CF Fund certificates to them because: 1) they had a low risk tolerance and an investment objective of preservation of capital; and 2) the $336,000 of CF Fund certificates constituted 17% of their total net worth and 24% of their net worth excluding homes.

Thus, Respondent violated Rule 703 of the *Code of Ethics*.

Fifth Ground for Discipline

Pursuant to Article 3(b) of the *Disciplinary Rules*, there are grounds to discipline Respondent for acts or omissions that violate *Practice Standard* 400-3, which requires a financial planning practitioner to communicate the recommendations in a manner and to an extent reasonably necessary to assist the client in making an informed decision.

Respondent, a financial planning practitioner, failed to communicate his recommendation of the CF Fund in a manner and to an extent reasonably necessary to assist MG in making an informed decision when he represented the CF Fund as low risk.

Respondent, a financial planning practitioner, failed to communicate his recommendation of the CF Fund in a manner and to an extent reasonably necessary to assist DL & JL in making an informed decision when he represented the CF Fund as a low risk investment.

Thus, Respondent violated *Practice Standard* 400-3.

Sixth Ground for Discipline

Pursuant to Article 3(b) of the *Disciplinary Rules*, there are grounds to discipline Respondent for acts or omissions that violate *Practice Standard* 500-2, which requires a financial planning practitioner to select appropriate products and services that are consistent with the client's goals, needs and priorities.

Respondent, a financial planning practitioner, failed to select appropriate products and services that are consistent with the client's goals, needs and priorities when he recommended and sold $100,000 of CF Fund certificates to MG because: 1) she had a low risk tolerance; 2) the $100,000 of CF Fund certificates constituted 25% of her total net worth and 44% of her net worth excluding her home.

Respondent, a financial planning practitioner, failed to select appropriate products and services that are consistent with the client's goals, needs and priorities when he recommended and sold $336,000 of CF Fund certificates to DL & JL because: 1) they had a low risk tolerance and an investment objective of preservation of capital; 2) the $336,000 of CF Fund certificates constituted 17% of their total net worth and 24% of their net worth excluding homes.

Thus, Respondent violated *Practice Standard* 500-2.

IV. Discipline Imposed

The Commission found that Respondent violated Rules 102, 201, 202 and 703 of CFP Board's *Code of Ethics* and *Financial Planning Practice Standards* 400-3 and 500-2, providing grounds for discipline under Articles 3(a) and 3(b). Based on the terms of the Settlement Agreement, the Commission issued to one-year suspension of his CFP® certification pursuant to Article 4.3 of the *Disciplinary Rules*.

The Commission identified as an aggravating factor that Respondent's conduct caused harm to two clients.

The Commission identified as mitigating factor that Respondent had no prior disciplinary history and his conduct was not indicative of a pattern of misconduct.

The Commission consulted *Sanctions Guidelines* 20(d) (Misrepresentation to Clients and Prospective Clients) and 31 (Suitability Violation). The Commission also consulted Anonymous Case Histories ("ACH") 27735, which resulted in a Public Letter of Admonition, and 28393, which resulted in a one-year and one-day suspension.