

## IFA Disciplinary Committee Findings

The following are reports of Disciplinary Committee decisions. They are in reverse date order, with the most recent at the top.

### Case 8. April 2009

The Member is referred to as C.

#### Facts of the case

The important facts may be summarised as follows:

The charges against the Member were that he had breached Bylaw 1.2 and/or Rule 11 of the Code of Ethics and Professional Conduct in force during the relevant time.

Summarised, the particulars were:

- (a) In the course of providing advice to his complainant client in the period from September 2001 to June 2007, C variously recommended Bridgecorp Limited secured debentures, capital notes and units in mortgage trust entities and Capital + Merchant Finance Limited secured debentures for the investment by the complainant of;
  - (i) Up to \$150,000 in Bridgecorp secured debentures;
  - (ii) Up to \$95,000 in Bridgecorp capital notes;
  - (iii) Up to \$50,000 in Bridgecorp mortgage trust entities' units; and
  - (iv) Up to \$150,000 in Capital +Merchant Finance Limited secured debentures.
- (b) In providing these recommendations the Member had knowledge that:
  - (i) The client was single, retired and when she first met C in September 2001 64 years of age;
  - (ii) The client's funds for investment were \$375,000 as at 30 September 2001 (being a matrimonial property settlement) reducing to approximately \$270,000 from about December 2005 due to the purchase of a new house;
  - (iii) The client was a conservative investor;
  - (iv) The client wanted to preserve all the investment funds available for investment for future income.
- (c) By providing the recommendations of the investments referred to in (a) with the knowledge he had, the Member did not:
  - (i) Provide recommendations that were appropriate to the client's needs and circumstances after taking account of her wishes; and/or
  - (ii) Ensure that his advice was appropriate and in the best interests of the client.

The Member pleaded not guilty to the charges as laid and admitted the first two sets of particulars but denied the third set noted in (c) above.

#### Jurisdiction

The Member asserted at the hearing that the Committee had no jurisdiction to hear charges against him on the grounds that by reason of his non-payment of his subscriptions he was deemed to be non financial and therefore his membership of IFA had ceased. At the hearing the chairman advised that the Committee had recently ruled on the same issue in another case and ruled that the hearing would continue on the basis that the Committee's written determination would give reasons on the jurisdictional determination and the member would be given time to make application to take the decision on review to the High Court. The written decision gave detailed reasons.

## **Submissions for the prosecution**

Included in the submissions for the Institute were representations that:

- The client invested in products offered by ten different entities. With one exception all the entities were finance companies. There were exposures of sometimes around 50% of total investments to one single company;
- C presented the investment products in terms of rates of return;
- The client had no appreciation that high rates of return go hand in hand with risk and C never advised her of this;
- She was not told it was prudent to diversify her risk;
- She was never presented with an investment plan;
- C has advised the Institute in his response to the complaint that he relied on investment grade ratings, audited financial statements, adviser information releases and in the case of Bridgecorp the presumed loan loss cover available through Lloyds of London;
- It was inappropriate for C to advise this client to place upwards of 70% into finance companies of any description.

Whilst the total amount of the complainant's investment loss is dependent on the ultimate payout from the insolvencies of Bridgecorp and Capital + Merchant Finance it is very clear that she has suffered significant financial loss and emotional pain and stress. It was submitted that all of this has arisen from C's failure to observe the standards set by his professional body.

## **Submissions by C on the charges**

C said that before endeavouring to resign from the Institute by letter dated 16 June 2008 he had been a member for 8 years and this is the first complaint against him. He said he no longer provides investment advice. Although C disputed the factual accuracy of some of the complainant's assertions he did not present evidence to support his position.

In his closing statement, C advised the Committee:

- (a) He understood his obligations during his time as a member and did not breach the rules;
- (b) He comprehensively briefed the complainant and obtained such information as was necessary to understand her needs;
- (c) He undertook careful research to understand the risk profiles of the companies he put forward and his research confirmed that those companies met her requirements as a conservative investor;
- (d) He gave the complainant detailed information as to the nature of the investment product and the return and associated risk;
- (e) The charges against him are without merit and he took into account the complainant's wishes and provided advice that was appropriate to her needs and circumstances. At all times he considered he acted in what he reasonably believed to be in the complainant's best interests.

## **Committee's decision on the charges**

The decision of the Committee with relation to the charges was:

"The Committee acknowledges that this is a matter of considerable importance to the complainant. The Committee acknowledges the stress, pressure and emotional pain it now finds C's actions have caused. However, the process is about the IFA acting on a complaint about a member, to ensure maintenance of proper standards and actions by its members and not to compensate a complainant for losses incurred."

"There were differences in the factual assertions made by the complainant and by C. We prefer the representations of the complainant in most instances where facts were in dispute. Generally, C has not been able to refute the representations of the complainant."

"C sought to explain his actions when giving advice to his client and in responding to the charges that he did not follow the Institute's rules or appropriate practices by asserting that he made it clear to the complainant that 'he was not a Financial Planner and that a Financial Plan

was not requested as the complainant's requirement was for fixed interest investments that would provide a regular flow of income over and above what the Banks were paying to top up her National Super'. He told the Committee that 'I made it clear that I was not a Financial Planner and that our services were limited to presenting her with investment options that were based on her description of her needs.' We find that argument is not helpful to C. In response to questions from the Committee he acknowledged that he was giving investment advice and we find that it follows from that, that in being a member and agreeing to comply with the Constitution and bylaws of the IFA he is in breach. Where membership of a professional body brings obligations a member cannot escape membership obligations by saying 'I was providing advice in a different manner'."

"We find on the explanations and information provided that the assertions made by C in his own defence are largely without merit. They did not have documentary support and were unconvincing in contrast to the complainant's explanations."

The Disciplinary Committee found the particulars the Member had denied to be proven and the Member guilty of the charges as laid.

### **Penalty**

With regard to penalty the decision of the Disciplinary Committee was:

"The Committee had taken into account C's representation that he is financially impecunious, his marriage had failed, his house had been sold by mortgagee sale and he had been forced to sell his advisory business. He is currently working for wages with a company, which he named. The Committee sees no sound reason for levying a fine. It would be in the interests of the Institute for the Member to continue working as an insurance adviser and pay off the costs that should be fully recoverable."

"In the circumstances of this case the Committee considers the Member should be appropriately penalised but not to the extent that his livelihood will be impaired. Publication of the Member's name was likely to do that. C should be entitled to earn a living working for another industry participant, but he should be required to be supervised."

The Committee ordered that C:

- (a) be censured;
- (b) is to meet the costs to the Institute of the disciplinary process in the amount of \$25,575 inclusive of GST;
- (c) undertakes and submits and continues to submit to the supervision by a person nominated by and on terms approved by the Compliance Officer in relation to any activities he might undertake, whether as an employee or in his own name, which involves the giving of professional financial advice C may give in the 24 month period following the date of taking effect of this decision (this date to be communicated to C by the Compliance Officer);
- (d) undertakes to advise his present employer and all future employers within the 24-month supervision period, immediately of the supervision requirement and undertakes to provide forthwith the employer's written confirmation that he has done so to the Compliance Officer;
- (e) undertakes not to provide financial planning or investment advice unless he has obtained and proves to the Institute the relevant qualification as per the Institute's or statutory requirements.

No advice was received from the Member within the time allowed by the Committee for an application to take the Committee's decision on jurisdiction on review .

### **Case 7. March 2009**

This case relates to risk insurance (Member Z).

### **Factual background**

In 2003 the complainant consulted the Member about insurance cover that she wished to take out for medical and income protection cover to include events arising from a prior medical condition. The

complainant's evidence was that she disclosed full details of her relevant medical history to the Member.

The member recommended a specific policy and insurance company and completed a proposal form for the complainant. The completed proposal form failed to disclose:

- (i) the complainant's prior medical condition;
- (ii) the medical documentation the complainant had provided;

and the Member had not advised the complainant that she would not be covered by the policy for her prior condition.

The complainant signed the proposal form as requested but was not asked to read the form and its contents and was not informed that it was important for all relevant information to be disclosed in the proposal and declaration.

A similar procedure was followed in 2005 with regard to a new policy for medical and income protection insurance.

Z failed to provide his client with appropriate documentation including an up to date written analysis of her financial needs and failed to present and review with the client a fully completed "Advice on replacement business" disclosure document.

When the client's previous medical condition returned she claimed under her insurance cover and the insurers denied liability.

#### **At the hearing**

At the commencement of the hearing, Z pleaded guilty to the charges and admitted all the particulars. He made a statement to the Committee and to the complainant. He acknowledged that by his actions he had caused significant emotional pain to the complainant and expressed considerable regret and remorse and his apology. Z explained that over the weekend preceding the hearing a settlement had been negotiated with the complainant and he had agreed to pay her a significant sum in recognition of the distress his actions had caused. He reiterated his belief that had he acted in the manner he now acknowledged he should have, the complainant would not have suffered the emotional anguish arising from her belief she was covered for insurance, but expressed the view that had the indemnifier been advised of the complainant's pre-existing medical condition cover the required cover would not have been available.

Both the Member and the complainant confirmed that the settlement was the end of the differences between them. The Disciplinary Committee accepted that the quantum of the settlement should remain confidential.

#### **Committee's views**

The Committee acknowledged the stress, pressure and emotional pain Z's actions have caused. However, the process is about the IFA acting on a complaint about a member, to ensure maintenance of proper standards and actions by its members. The Committee was pleased that the process has culminated in agreement between the parties with a settlement, but as the Committee observed during the hearing it is not the role of the disciplinary process to achieve compensation. The Committee considers it is commendable that Z has pleaded guilty and admitted all the particulars, but account has been taken of the fact that Z was very late in doing so. The Committee considered Z's expressions of remorse were helpful.

The Committee had taken account of all of the issues and especially the total cost to Z. Z will be financially penalised by the amount of any fine, the amount of an order for costs and his own legal costs. This, together with the agreed settlement payment to the complainant, could come to [a very significant sum]. There was no evidence of deliberate intent on Z's part. His lack of attention to detail and his failure to follow basic procedures had given rise to very unfortunate circumstances. Z did not follow normal processes with regard to the completion of insurance proposals and obtaining information necessary for an up to date written analysis of the client's financial needs; and provide the client a fully completed "Advice on replacement business" disclosure document.

In the circumstances of this case the Committee considers the Member should be appropriately penalised but not to the extent that his livelihood will be impaired. Publication of the Member's name was likely to do that.

### **Decision**

The Committee ordered that Z:

- (a) be censured;
- (b) pay a fine of \$2,000 to the Institute;
- (c) meets the costs to the Institute of the disciplinary process in the amount of \$25,575 inclusive of GST;

and that the circumstances of this case and the Committee's determination may be published by the Institute without disclosure of the Member's and the complainant's names and locations.

### **Case 6. March 2009**

Mr X, a member of the Institute of Financial Advisers has pleaded guilty to two charges following receipt of a complaint from a client. The Member has pleaded guilty to the charges that:

- (a) he breached clause 1.2 of the Institute's Code of Ethics "Members must provide recommendations that are appropriate to the client's needs and circumstances after taking into account the clients wishes";
- (b) he breached clauses 10.1 and 10.4 of the Code of Ethics in that he failed to provide a written statement stating the type of services to be offered and failed to present a comprehensive financial plan.

This is a matter that relates to advice given by the Member in his capacity as a financial adviser in 2001. The client was recommended to invest with Bridgecorp and St Johns Property Fund (which has now been purchased by St Laurence) and in following the advice ended up with investments of \$60,000 in Bridgecorp and \$20,000 in St. Laurence. The client suffered loss.

The guilty plea followed the filing of evidence by the Institute including that of an expert witness.

### **Submissions on penalty and costs**

In the submission for the Institute counsel did not seek a specific penalty but sought such penalty as would be a sufficient disincentive to other members from involving themselves in and recommending investment products which are not suitable for clients and failing to undertake comprehensive planning. It was submitted that the penalty should not only deter members from undertaking the same breaches but also ensure that the public has confidence in the IFA and its members.

For the Member, counsel advised that the Member was devastated about the complaint and has ceased providing investment advice. It was submitted that the Member's advice was not causative of the complainant's loss and that given the relatively small amount available for investment a greater diversity was unlikely. It was submitted that the Committee should take into account a previously blameless career and that appearing before the Institute is substantial penalty in itself. Counsel submitted for a modest fine, non publication of the member's name and made no submission as to costs.

### **Determination and orders**

The Committee has considered the charges and the guilty plea, the original evidence and submissions and the further information and submissions. Having regard to all of the issues the Disciplinary Committee determines and makes the following orders:

THAT the Member Mr X having pleaded guilty to the charges made against him:

1. be and is hereby censured;
2. be fined \$2,000;
3. be ordered to meet the costs of the investigation and determinations of the Institute and this Committee in the amount of \$17,500 plus GST; and THAT

4. the facts and circumstances of this case and the orders as to penalty and costs be published in the Institute's newsletter to members and appropriately on the Institute's website, but without reference to the Member's name or locality.

#### **Cases 4 and 5. March 2009: Disciplinary Committee determinations on its jurisdiction**

The Disciplinary Committee recently made two determinations concerning its jurisdiction. Both cases were similar though they involved two different Members subject to unrelated complaints. This report covers both cases. What follows is a summary of the background and provides quotes from the key aspects of the Committee's determinations.

#### **Background**

Before any substantive hearing of formal charges against the Members and as part of the defence process legal counsel for the parties asserted the Disciplinary Committee did not have jurisdiction. This was based upon the argument that since neither Member had paid their subscription by 30 September 2008, they were "non-financial" so their memberships had ceased and they were no longer subject to IFA's disciplinary bylaws.

After exchange of legal submissions, the Disciplinary Committee issued a determination on the jurisdictional issue, and set down a date for the substantive hearing of the two cases.

#### **Provisions in the IFA Constitution and Bylaws**

The IFA Constitution and Membership and Certification Bylaws have provisions preventing a Member from resigning while they are the subject of a complaint, until the complaint has been dealt with. In these two cases, the Members were seeking to rely upon a separate provision relating to lapse of membership for non-payment of subscription.

[Note: At the November 2008 Council meeting, there were amendments to both the Constitution and the Membership and Certification Bylaws to ensure that failure to pay a subscription did not result in a Member subject to a complaint having their membership lapse. Obviously, these changes could not apply retrospectively to these two cases.]

#### **The Committee's analysis**

The Disciplinary Committee said as part of its determination "The Committee members have carefully considered the submissions and other material submitted for the parties. We have a clear preference for the analysis and arguments presented for the Institute. We think the analysis presented for [the Member] is an attempt to avoid exposure to the disciplinary process that the member agreed to submit to contractually for the good of the profession, the maintenance of standards and the protection of the public. We cannot accept that, whereas the contract documents applicable at the time of the alleged breaches provided that a member should not be able to avoid the disciplinary process by resigning, the member should nevertheless be able to avoid the process by simply not paying a subscription.

The Committee considered the wording of letters of resignation from the Members and said " we consider [the Member's] "decision to not pay the subscription was an implicit declaration of an intention to resign which resignation was otherwise an ineffective method of avoiding the disciplinary process."

"Most importantly we consider the charge in the Constitution at clause 5.2 as being an insurmountable obstacle to [the Member].

- 5.2 This Constitution is to be given such wide and liberal interpretation as is necessary to give effect to the objects of the Institute.

"It is inconceivable that the failure of the language of the Constitution to prevent the non-payment of subscriptions from allowing a Member who is the subject of a complaint and charges to escape the proper disciplinary process could have been intended. A wide and liberal interpretation as is

necessary to give effect to the objects of the Institute ... necessarily imputes the intention to prohibit that effect."

### **The Determination**

The Disciplinary Committee determined that it "has jurisdiction to hear charges against a person who was a Member and subject to the Constitution and Bylaws of the Institute at the date the actions complained about took place. This is notwithstanding the subsequent non-payment of membership subscriptions that otherwise renders a Member non-financial and thus not a Member. We consider the appropriate interpretation of the Constitution and therefore the contract (between the Member and the IFA) is that any notice of resignation, whether explicitly in writing, or implicitly by way of non payment of subscriptions, cannot take effect until the hearing of the complaint or the disciplinary proceedings and related appeals have been disposed of and any resulting action or disciplinary measure, fine or penalty has been settled."

In both cases the charges will now proceed to substantive hearing.

### **Case 3. December 2008**

Mr X, a member of the Institute of Financial Advisers has pleaded guilty to two charges following receipt of a complaint from a client. The Member has pleaded guilty to the charges that:

- (c) he breached clause 1.2 of the Institute's Code of Ethics "Members must provide recommendations that are appropriate to the client's needs and circumstances after taking into account the clients wishes";
- (d) he breached clauses 10.1 and 10.4 of the Code of Ethics in that he failed to provide a written statement stating the type of services to be offered and failed to present a comprehensive financial plan.

This is a matter that relates to advice given by the Member in his capacity as a financial adviser in 2001. The client was recommended to invest with Bridgecorp and St Johns Property Fund (which has now been purchased by St Laurence) and in following the advice ended up with investments of \$60,000 in Bridgecorp and \$20,000 in St. Laurence. The client suffered loss.

The guilty plea followed the filing of evidence by the Institute including that of an expert witness.

### **Submissions on penalty and costs**

In the submission for the Institute counsel did not seek a specific penalty but sought such penalty as would be a sufficient disincentive to other members from involving themselves in and recommending investment products which are not suitable for clients and failing to undertake comprehensive planning. It was submitted that the penalty should not only deter members from undertaking the same breaches but also ensure that the public has confidence in the IFA and its members.

For the Member, counsel advised that the Member was devastated about the complaint and has ceased providing investment advice. It was submitted that the Member's advice was not causative of the complainant's loss and that given the relatively small amount available for investment a greater diversity was unlikely. It was submitted that the Committee should take into account a previously blameless career and that appearing before the Institute is substantial penalty in itself. Counsel submitted for a modest fine, non publication of the member's name and made no submission as to costs.

### **Determination and orders**

The Committee has considered the charges and the guilty plea, the original evidence and submissions and the further information and submissions. Having regard to all of the issues the Disciplinary Committee determines and makes the following orders:

THAT the Member Mr X having pleaded guilty to the charges made against him:

- 5. be and is hereby censured;
- 6. be fined \$2,000;

7. be ordered to meet the costs of the investigation and determinations of the Institute and this Committee in the amount of \$17,500 plus GST; and THAT
8. the facts and circumstances of this case and the orders as to penalty and costs be published in the Institute's newsletter to members and appropriately on the Institute's website, but without reference to the Member's name or locality.

## **Case. 2 November 2008**

This is a summary of a decision by the Disciplinary Committee of the Institute of Financial Advisers. The Committee ordered publication of the details of the charge and the Committee's decision but suppressed publication of the identities of those involved. In this report the member is referred to as Mr A and the complainants as Mr and Mrs B or the Bs.

### **The charge**

The charge was that Mr A, breached Rule 1.2 of the then applicable Code of Ethics and Professional Conduct "Members must provide recommendations that are appropriate to the client's needs and circumstances, after taking into account the client's wishes", in that when he recommended to Mr and Mrs B that they invest \$502,000 in secured debentures with Bridgecorp Limited and Propertyfinance Securities Limited, he:

- knew that the Bs were risk averse and wished to preserve their capital although generating a higher than bank return;
- failed to provide recommendations that were appropriate to the B's needs and circumstances.

### **Brief facts**

The Bs migrated to New Zealand in 2004. Mr A assisted them with the transfer of funds and then placed part of those funds on a short term basis while they had a new house built. Their funds were available when required and there is no complaint about those investments.

The charge related to the balance of their funds intended to provide a retirement income to supplement the B's overseas pensions. Mr A recognised their position when he wrote to them on 17 September 2004, recording that:

"You are risk adverse (sic) having effectively retired and wish to preserve your capital yet generate a higher than bank return."

Mr A advised them that the available amount be invested in two equal sums (one for two years and another for three) in two of a number of finance companies which he nominated. In accordance with that advice, the Bs invested \$251,000 in Bridgecorp Limited for two years and \$251,000 in Propertyfinance Securities Limited for three. Although the latter recommendation did not form part of the charge, it was accepted by the defence that Mr A recommended to the Bs that they reinvest the Bridgecorp investment when it matured with that company.

Bridgecorp Limited was placed in receivership on 2 July 2007 and Propertyfinance Securities Limited on 29 August 2007. There were obviously serious financial losses to the Bs. The extent of those losses has not yet been crystallised.

The evidence showed, and Mr A accepted, that he had failed to advise the claimants appropriately in that:

- there were other investments available and suitable for their requirements, even taking into account what he believed to be their aversion to investing in equities or equity based products;
- their investments should have been diversified; and particularly that their funds should be diversified within the fixed interest sector;
- the advice did not have regard to the risks of the investments proposed.

## **Mitigating factors**

Mr A expressed concern for the Bs and contrition at the position in which his advice had left them. His concern appeared to the Committee to be genuine and expressed honestly.

The Committee took account of a number of other factors presented in submission by the member.

The Committee believed that Mr A could remain a useful member of the profession and that in the circumstances neither expulsion nor suspension was appropriate. A period of supervision should be imposed in his own and in the profession's interests.

The Committee considered that the imposition of a fine was called for but his breach did not call for the maximum level of \$10,000.

## **Penalties**

The committee determined the following penalties:

- a. Mr A was censured, that censure being expressed to him at the hearing;
- b. The Committee ordered that Mr A's practice, personally and through his company, be supervised for a period of two years by a senior Certified Financial Planner practitioner, not a member of the group within which the practice is conducted. The supervisor is to be approved by the Institute, to which the supervisor is to report six monthly. The Committee looks to the Institute to monitor the supervision, which will be at Mr A's cost in all respects. The period of supervision will run from the date on which the Institute approves the supervisor.
- c. Mr A was ordered to pay a fine of \$5,000
- d. Mr A was ordered to pay the Institute's costs which totalled \$14,631, within one month of the figure being fixed.
- e. The Committee ordered publication of the details of the charge and the decision but with suppression of the identities of the parties.

## **Disciplinary Committee – further comments**

In the 21 November newsletter to members the Institute reported on a decision of the Disciplinary Committee. In referring to the charges for which the member was found guilty and the penalties made, that report stated 'The Committee took account of a number of other factors presented in submission by the member'. The Disciplinary Committee has asked that further explanation be made; namely that the issues in mitigation included the fact that the member who was found guilty of the charges was under mentorship, and had chosen the names of the companies which he had recommended to the clients from a range of investments in the fixed interest section approved by the relevant committee of the organisation within which he practised. The Disciplinary Committee considers that there is argument that suggests the mentor and members of the relevant committee approving the investments might properly have been investigated for failure to meet professional standards.

## **Case 1. May 2008**

The member had been convicted and jailed for a criminal offence unrelated to their role as a financial adviser, but criminal convictions are considered to be part of whether a person is considered "fit and proper" to be a member. The Disciplinary Committee terminated membership.