Scams by crooked planners spur calls for changes in law

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Credit varies.

"W e thought it was a great idea to have someone help us plan our finances," says a 40-year-old victim of a financial planning scheme, "but everything we invested in with him went bad and we lost approximately $85,000."

The victim, a flight attendant married to an electrical engineer, said they were new to San Diego. A neighbor had given their name to the financial planner, who called for an appointment to discuss their finances.

Harold H. Burke, a retired wheat farmer from Fallbrook, "knew a woman who worked for a guy that did financial planning." Burke received a financial plan that included investments in Coastal Equities which, according to court records filed by the bankruptcy trustee, was a "$50 million Ponzi scheme."

These are only a few examples of the investment schemes involving financial planners.

Crooked investment schemes of all sorts amounted to more than $570 million during a recent three-year period, according to the North American Securities Administrators Association, which represents state regulators, and the Better Business Bureau. Of that total, more than $90 million is tied directly to financial planners, asserts the BBB.

San Diego's share of the national problem is "tremendous," according to Judith Hayes of the state attorney general's major fraud unit here. "I have seen more than $40 million in fraud come across my desk in the last year, and I'm only one person. Other agencies, like the district attorney and U.S. attorney, have the same amount," said Hayes.

The unlucky flight attendant invested with a company called Common Sense Capital Corp., which went bankrupt. The financial planner involved, Kenneth H. Williams, was recently charged with state securities violations along with two attorneys and other financial planners. Williams has pleaded guilty to the felonies, according to court records.

These scams and others have spurred calls on both the state and federal levels for regulation of financial planners.

The number of people claiming to be financial planners varies widely, and depending on who gives the estimates ranges from 50,000 to 200,000. Regardless of the true figure, many experts agree that the majority are honest, providing legitimate service to the financially confused public.

Authorities disagree, however, over the best way to handle the problem -- a problem made more complex by arguments over defining what a financial planner is. "Anyone can wake up tomorrow and decide to be a financial planner and damage his first hundred clients," says Charles M. Shackelford, an attorney who is registered as an investment adviser with the SEC.

In addition, the SEC and the state Corporations Department also regulate "investment advisers." Both government agencies agree that most financial planners are covered under regulation of investment advisers.

A state legislative study, however, states that the laws are "widely ignored," by financial planners. The planners argue they do not fall under the technical definition of an investment adviser.

The SEC and the state Corporations Department are in charge of regulating the sale of securities. A security, defined broadly, includes not only stock but also limited partnership interests, trust deeds and other investments denoting ownership of an enterprise.

State Sen. Joseph B. Montoya, D-North Whittier, has introduced legislation which defines a financial planner and seeks to regulate those claiming the appellation. (The legislation has already passed the Senate.) Financial planning organizations support the legislation, according to Chuck Forman, a San Diego financial planner.

But, the Corporations Department is opposed to the bill, according to William Kenefick, legislative liaison for the department. Kenefick said the bill will "create a pseudo- profession without a course of study or examination."

The department reiterates most financial planners are covered by current regulations for "investment advisers" and earlier this year issued stronger regulations to leave no question, according to Raymond Burg, of the department in San Diego.

Kenefick criticizes the Montoya bill on the grounds that it attempts to regulate only those calling themselves financial planners and not those who refer to themselves as "financial advisers," "financial counselors" or those who prepare "financial blueprints" and "financial programs," even though they do the same thing as financial planners.

Furthermore, says Kenefick, the department "does not want to administer a program that is defective and bear the brunt of criticism when it fails."

Kenefick recommends legislation that would put "some teeth" into enforcement and ease a victim's ability to recover damages in a civil suit.

Another dispute arises over the generation of fees for financial planners. The majority of planners generate fees from selling investment products.

Shackelford, the registered investment adviser, says commissions from selling investment products are his, "only source of compensation." He defends the practice saying implementation of a plan is as important as the plan itself. "I personally bought a plan that was interesting to read but then it sat on a shelf gathering dust."

Corporations counsel Burg disagrees. He says "one problem we have found is that people think they are getting independent advice when the planner has a relationship with the issuer (of the security.)"

Congress, trying to find a better way to regulate financial planners on a national level, recently held committee hearings on the subject. The congressmen heard testimony from several victims who lost retirement savings or proceeds from a spouse's life insurance after dealing with financial planners.

The committee identified a lack of staffing at the SEC as a problem since the number of those registering as "investment advisers" has nearly doubled in the past five years, while the staffing of SEC enforcement has remained the same.

No particular legislation is pending on the federal level, according to Rep. Jim Bates, D-San Diego, who sits on the subcommittee studying the problem.

Locally, Roger Young, director of the San Diego Crime Commission, has coordinated a seminar given by experts to warn people of the investment dangers. Young said a poll taken at the seminar indicated a majority of those there were scam victims.

"There is no professional effort to educate people on the red flags of investment fraud," said Young. "The area was very poorly regulated until recently, and the investigative agencies are not in a position to blow the whistle," he said.

Burg said the Corporations Department has "not given a high priority to the problem until recently. Previously, we only looked to the issuer (person actually producing the security) when there was a problem, now our investigators are looking at who got the person into the investment in the first place."

"The financial-planning organizations are also working hard to regulate their own industry," said Burg. "They have asked us to speak to them on the rules and regulations."

-- Crowley is a San Diego attorney engaged in private practice

Credit: Special to The Tribune | Crowley is a San Diego attorney engaged in private practice

Abstract (Document Summary)

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