OPEN MEETING ITEM

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COMMISSIONERS
BOB STUMP – Chairman
GARY PIERCE
BRENDA BURNS
BOB BURNS
SUSAN BITTER SMITH

ARIZONA CORPORATION COMMISSION

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AZ CORP COMMISSION
DOCKET CONTROL

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Arizona Corporation Commission
DOCKETED
JUN 30 2014
DOCKETED BY

DATE: JUNE 30, 2014

DOCKET NO.: S-20864A-12-0439

ORIGINAL

TO ALL PARTIES:

Enclosed please find the recommendation of Administrative Law Judge Marc E. Stern. The recommendation has been filed in the form of an Opinion and Order on:

MARK DANA HUGHES AND DOLLY HUGHES; AND
LEGACY FINANCIAL ADVISORS, L.L.C.

Pursuant to A.A.C. R14-3-110(B), you may file exceptions to the recommendation of the Administrative Law Judge by filing an original and thirteen (13) copies of the exceptions with the Commission's Docket Control at the address listed below by **4:00** p.m. on or before:

JULY 9, 2014

The enclosed is NOT an order of the Commission, but a recommendation of the Administrative Law Judge to the Commissioners. Consideration of this matter has tentatively been scheduled for the Commission's Open Meeting to be held on:

JULY 22, 2014 and JULY 23, 2014

For more information, you may contact Docket Control at (602) 542-3477 or the Hearing Division at (602) 542-4250. For information about the Open Meeting, contact the Executive Director's Office at (602) 542-3931.

JODI JERICH
EXECUTIVE DIRECTOR

This document is available in alternative formats by contacting Shaylin Bernal, ADA Coordinator, voice phone number 602-542-3931, E-mail SABernal@azcc.gov.

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

BOB STUMP - Chairman
GARY PIERCE
BRENDA BURNS
BOB BURNS
SUSAN BITTER SMITH

IN THE MATTER OF: MARK DANA HUGHES, CRD # 1843511, and DOLLY A. HUGHES, husband and wife, and LEGACY FINANCIAL ADVISORS, L.L.C., CRD # 114029, an Arizona limited liability company, Respondents.	DOCKET NO. S-20864A-12-0439 DECISION NO. _____ **OPINION AND ORDER**

DATE OF PRE-HEARING CONFERENCE:	November 20, 2012
DATE OF STATUS CONFERENCE:	February 14, 2013
DATES OF HEARING:	August 26 and 27, 2013
PLACE OF HEARING:	Phoenix, Arizona
ADMINISTRATIVE LAW JUDGE:	Marc E. Stern
APPEARANCES:	Ms. Aikaterine Vervilos, Staff Attorney, on behalf of the Securities Division of the Arizona Corporation Commission.

BY THE COMMISSION:

On October 17, 2012, the Securities Division ("Division") of the Arizona Corporation Commission ("Commission") filed a Notice of Opportunity for Hearing ("Notice") against Mark Dana Hughes and Dolly A. Hughes, husband and wife, and Legacy Financial Advisors, L.L.C. ("LFA") (collectively "Respondents"), in which the Division alleged multiple violations of the Investment Management Act ("IM Act") in connection with Mark Hughes' conduct as an Investment Adviser Representative while not licensed or in compliance with the IM Act and by committing fraud in the provision of services.

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Dolly Hughes, the spouse of Respondent Mark Hughes, was joined in the action pursuant to A.R.S. § 44-3291 solely for the purpose of determining the liability of the marital community.

The Respondents were duly served with copies of the Notice.

On November 2, 2012, a request for hearing was filed on behalf of the Respondents.

On November 6, 2012, by Procedural Order, a pre-hearing conference was scheduled on November 20, 2012.

On November 20, 2012, at the pre-hearing conference, the Division appeared through counsel. Mr. Hughes appeared on his own behalf, and indicated that his spouse had a scheduling conflict with the proceeding and could not attend. At that time, counsel for the Division stated the parties were discussing a possible settlement of the proceeding.

On December 10, 2012, the Division filed a request for a status conference to be scheduled because Mr. and Mrs. Hughes had filed a voluntary Chapter 13 reorganization petition for bankruptcy in the United States Bankruptcy Court on December 5, 2010, in Tucson, Arizona. Respondent LFA was not identified as a petitioner in the bankruptcy filing. The Division indicated that it had attempted to contact Respondents concerning settlement, but had not received any response.

On January 24, 2013, by Procedural Order, a status conference was scheduled on February 14, 2013.

On February 14, 2013, at the status conference, the Division appeared and requested that a hearing be set. Respondents failed to appear. The presiding Administrative Law Judge ("ALJ") directed the Division to attempt to contact the Respondents to inquire if they intended to present a defense and to file a Status Report by March 1, 2013.

On February 28, 2013, the Division filed a Status Report and Request for Hearing Dates. The Division indicated that it had both mailed and e-mailed Respondents and received no responses. The Division's counsel stated that on February 25, 2013, she received a letter from the Hughes' bankruptcy attorney who did not enter an appearance in this proceeding. He maintained that the Division's action was stayed by the federal Bankruptcy Code, and that Respondents would seek a federal injunction against the Division if it proceeded against his clients with its action at the Commission.

The Division stated that on February 26, 2013, its counsel informed Respondents' bankruptcy counsel by letter that he had misinterpreted the law and that government agencies are exempt from the automatic stay in the exercise of their police and regulatory powers.

On March 6, 2013, by Procedural Order, a hearing was scheduled to commence on August 26, 2013.

On August 26, 2013, a full public hearing was convened before a duly authorized ALJ of the Commission at its offices in Phoenix, Arizona. The Division appeared with counsel. Respondents failed to enter an appearance. At the conclusion of the proceeding, the Division's counsel indicated that a post-hearing brief would be filed. The matter was taken under advisement pending submission of a Recommended Opinion and Order to the Commission.

On October 15, 2013, the Division filed its closing brief which recommends that disciplinary action be ordered against Respondents including an order of restitution in the amount of $340,806.30.

* * * * * * * * * *

Having considered the entire record herein and being fully advised in the premises, the Commission finds, concludes, and orders that:

FINDINGS OF FACT

1. Mark Dana Hughes (CRD #1843511), at all relevant times herein was an Arizona resident and married to Dolly A. Hughes, his spouse.

2. LFA was initially owned and operated as a sole proprietorship by Respondent Mark Hughes. LFA became licensed as an Investment Advisor ("IA") in Arizona on or about April 7, 2008. On December 8, 2009, Respondent Hughes organized LFA as an Arizona limited liability company with its principal place of business in Tucson, Arizona. (Ex. S-3A and Ex. S-3B)

3. After LFA was incorporated as a limited liability company, Mr. Hughes did not obtain a license as an Investment Advisor Representative ("IAR").

4. The Division, in support of its allegations in the Notice called six witnesses as follows: Robin Jones and Henry J. Masek, two investors; Steve Steger and Cathryn Mayers, Division Financial Institution Examiners; Denise Fritz, a Division Forensic Accountant; and Paul J. Litteau, an expert in the securities industry.

5. Mrs. Robin Jones, the Executive Vice-President of Clovis Community College, in Clovis, New Mexico, testified that she became familiar with Respondent Mark Hughes and LFA around 1990 when the company her husband worked with, Clovis Anesthesia & Associates ("CAA"), engaged Respondent Hughes to pursue investment opportunities for CAA employees.[1] (Tr. 27-29:9-6)

6. Mrs. Jones and her husband determined the amount of funds that they could invest with Respondents and Respondent Hughes analyzed their financial position to facilitate their ultimate investment goals and objectives.

7. On December 26, 1999, Mrs. Jones and her husband signed what was termed "Investment Policy Statement for the Royce Jones Profit Sharing Plan" which described their investment objectives in greater detail. (Ex. S-15)

8. Mrs. Jones stated that she and her husband's retirement plans were for him to work until he was somewhere between 62 and 65 and she planned to retire one year later with a goal of retiring with the same standard of living as when they were working. Their goal was to amass $1 million in assets. (Tr. 17-22)

9. When the Joneses began meeting with Mr. Hughes, they had no investment experience. (Tr. 32:4-6)

10. Mrs. Jones testified that during the "early years" of their investing with Respondents, Mr. Hughes would send them a quarterly statement and visit with them at least once a year in person. (Tr. 34:1-6)

11. According to Mrs. Jones, Mr. Hughes selected all of the investments in their portfolio.

12. Mrs. Jones testified that Respondent Hughes had completed a client profile and risk assessment which contained a risk assessment questionnaire that described their investment objective as moderate to moderately aggressive.

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[1] Mrs. Jones' husband, Royce, worked as a certified nurse anesthetist for CAA.

13. Mrs. Jones testified that in August 2008 she and her husband experienced a change in circumstances when he had a heart attack and had to have surgery for a quadruple bypass. (Tr. 38:18-25)

14. Subsequently, Mrs. Jones contacted Mr. Hughes and told him that she did not believe that her husband could return to work and they needed to be much more conservative with their investments. However, after that conversation, she never received an updated investment policy statement or risk profile or anything similar. (Tr. 38-39)

15. Mrs. Jones testified that after her husband's heart attack she became concerned that their investment portfolio with Respondents not lose any more money, because at one time it had been worth more than $800,000 and its value had gone down to less than $400,000. Mrs. Jones stated that she had communicated her thoughts to conserve the value of the Jones' portfolio to Mr. Hughes. (Tr. 40:1-22)

16. Mrs. Jones further testified that she, rather than her husband, primarily communicated with Mr. Hughes. After her husband's heart attack, she and her husband maintained three CDs with a total value of approximately $120,000 because she didn't trust the investments in their portfolio. (Tr. 41-42:12-5)

17. When Mrs. Jones reviewed trading statements from TD Ameritrade and Scottrade, the brokerages utilized by Respondents as custodians on behalf of their clients, she testified that she did not understand them. (Tr. 43)

18. Mrs. Jones further stated that she had no idea what a leveraged Exchange Traded Fund ("ETF") was. (Tr. 44:12-14)

19. Mrs. Jones was unable to state whether the investments made by Respondents for the Jones' accounts fit within their level of risk tolerance. (Tr. 44:18-22)

20. It was apparent that Mrs. Jones did not know what was going on within their portfolio. Mrs. Jones stated that she and her husband trusted Respondents because at one time the value in their portfolio had reached approximately $800,000. (Tr. 45: 14-25)

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21. While the Jones' portfolio was going up in value, they heard from Respondent Hughes "all the time," but when their accounts started to lose money they would only receive a quarterly statement or an email or she would have to check with him by telephone. (Tr. 46:12-22)

22. After their portfolio began to lose money, Mrs. Jones testified that she questioned Respondent Hughes about how they were going to recover what had been lost.

23. Shortly after Mrs. Jones' husband's heart attack, she was in email contact with Respondent Hughes concerning whether to switch their holdings into CDs that would maintain their value, but Respondent Hughes communicated with her to "hold the course." (Tr. 48:8-24)

24. On June 29, 2012, Respondent Hughes emailed Mrs. Jones and informed her that he was having some health issues and was going to take a sabbatical. As a result, he stated that he had invested their portfolio in three or four investments to produce income while the economy slowly improved and interest rates increased. (Tr. 50:1-11)

25. Mrs. Jones testified that, according to a new financial planner that Mr. and Mrs. Jones had subsequently begun dealing with, their investments with Respondents were too aggressive and trades had been done incorrectly. (Tr. 50-51:12-24)

26. According to Mrs. Jones, she and her husband could not afford to lose the money that they had entrusted to the Respondents to manage and as a result she will have to work much longer than planned.

27. Mrs. Jones further testified that when Mr. Hughes informed her that he would no longer handle the Jones' portfolio, it was worth only approximately $170,000 after initially investing approximately $161,000 and further investing approximately $24,000 a year for 20 years with the Respondents.[2] (Tr. 53:8-19)

28. Mrs. Jones testified that at no time did she realize that Mr. Hughes was placing the Jones' entire portfolio at substantial risk because of his investment maneuvers. (Tr. 54:1-10)

29. In concluding her testimony, Mrs. Jones testified that Mr. Hughes had total control over the Jones' portfolio while they were his clients. (Tr. 56:1-15)

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[2] The total amount invested by Mr. and Mrs. Jones with Mr. Hughes was approximately $540,000.

30. Mr. Henry Masek, a retired police officer from the City of Tucson, testified that he became a client of Mr. Hughes and LFA in approximately March 2011 when he transferred his State of Arizona Public Safety Pension Account from the State Retirement System to Respondents' management and control. (Tr. 58-59)

31. Mr. Masek testified that he does not understand "financial stuff at all" and at the time he initially met with Respondent Hughes he took his son, who was a graduate of Eller Business College at the University of Arizona to act "kind of as an interpreter." (Tr. 59:14-23)

32. According to Mr. Masek, his goal in investing was to have enough income from his portfolio to pay his current monthly mortgage payments as they became due. (Tr. 60:7-19)

33. Mr. Masek testified that he was 60 years old when he first met with Respondent Hughes and filled out a questionnaire with respect to his risk tolerance. Mr. Masek explained that he knew nothing about investing, and "needed to hire somebody to take care of it" and thought that he could be a moderate investor. (Tr. 61-63)

34. During the hearing, Mr. Masek reviewed an Investment Policy Statement ("IPS") which had been prepared for him by Respondent Hughes. Mr. Masek stated that Respondent Hughes did not review the entire document with him. (Tr. 64:6-15)

35. Mr. Masek's IPS' summary stated that he had approximately $241,000 in total assets. (Tr. 65:14-18) (Ex. S-21)

36. According to Mr. Masek's IPS, his risk tolerance was termed "Mod Conservative." (Ex. S-21)

37. Mr. Masek testified that he did not tell Respondent Hughes what percentage of stocks, bonds, or other forms of investment should be in his portfolio because he had hired Mr. Hughes to handle his portfolio after he had been referred to him by a person whom he trusted (his tax advisor). (Tr. 67-68:21-3)

38. Mr. Masek further testified that since he was not knowledgeable about financing, he was relying on Mr. Hughes with respect to the investment allocations in his investment portfolio. (Tr. 68:7-15)

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39. Mr. Masek stated that he mainly looked at the bottom line of his statement which came from Scottrade to review the valuation of his portfolio each month. (Tr. 69:18-25)

40. When Mr. Masek turned over the management of his investment portfolio to Respondent Hughes, it contained slightly less than $200,000, and after he began to receive his statements, he began to notice that his balance kept going down. (Tr. 70:4-22)

41. Initially, Mr. Masek indicated that he was not concerned because he understood that investments in stocks versus a bank savings account had a risk of their value going down, but he hoped that his investments would return to a higher level. (Tr. 71:1-9)

42. Mr. Masek testified how Respondent Hughes, in his dealings with him, explained what Mr. Hughes termed a "seven year curve" how stocks "would go up . . . and then maybe go down." Respondent Hughes explained that it was his job to monitor these things and to make adjustments. (Tr. 71:10-19)

43. Mr. Masek further stated that when "my money was dropping, dropping, dropping," Mr. Hughes told him to remember the seven year curve and to not look at his monthly statement. (Tr. 71-72:20-8)

44. Mr. Masek testified further that when reviewing his statements from Scottrade, he had no idea what the transactions represented and whether a sale or purchase of a security was conservative, moderate or aggressive because his attention to the statements centered on the "bottom line" to determine the value of his portfolio. (Tr. 74:4-11)

45. Mr. Masek employed the Respondents from October 2011 until June 2012 when he terminated Mr. Hughes and closed his account with only $119,345.74 remaining from his original $200,000 investment. (Ex. S-22)

46. When Mr. Masek met with his father-in-law's financial advisor, he was told by the advisor that the investments were so "high risk" that he would not have placed a conservative or moderate conservative investor in such stocks. (Tr. 76-77:11-8)

47. Based on the record, Mr. Masek's portfolio dropped in value approximately $80,000.

48. Mr. Masek had never asked Respondent Hughes to change his risk tolerance to a more aggressive form of investing.

49. Mr. Masek stated that his losses in his portfolio greatly affected him because he had worked his entire career to purchase his home and it was very important to him that the money in the account which he had transferred to the management of Mr. Hughes had only approximately $119,000 left in it to pay off a $150,000 mortgage and he feared for the loss of his property. (Tr. 79-80:21-7)

50. According to Mr. Masek, Respondent Hughes was "taking more risks than I could afford." (Tr. 84:13-15)

51. Ms. Cathryn Mayers, a financial institutions examiner with the Division, testified that it was her job to conduct field examinations of licensed-broker/dealers and investment advisors and their representatives by conducting audits of their business practices, their sales practices and their books and records. (Tr. 86-87:20-4)

52. The Division's examiner testified further that she had been involved in the investigation of the Respondents and had spoken with several investors, Chris Johns and Sanda and Harry Clark. (Tr. 87:14)

53. Ms. Mayers testified that Mr. Johns had told her that he met Respondent Hughes through his church and that he had been a good friend to his family. Based on this relationship, Mr. Johns trusted him and Mr. Hughes developed an investment plan for Mr. Johns. (Tr. 88:13-20)

54. According to Ms. Mayers, Mr. Johns hoped to retire in his 50's and at one time had been aggressive in his investing strategy, but starting around 2008 or 2009 he had instructed Mr. Hughes that he wanted to be a more conservative investor. After Mr. Johns lost his job in 2009 he gave Mr. Hughes $50,000 to invest and told him to be very conservative with his investing. (Tr. 88-89:21-8)

55. The Division's examiner testified that Mr. Johns told her that his $50,000 investment decreased in value to approximately $30,000 and his relationship with Respondent Hughes deteriorated, but Mr. Hughes told him to "stay the course." (Tr. 89:9-21)

56. According to Ms. Mayers, Mr. Johns was an unsophisticated investor and he did not know what type of securities Mr. Hughes had invested in for him. His remaining funds had been transferred to Chase Bank after his wife took a job there. (Tr. 89-90:23-9)

57. Ms. Mayers spoke with Mrs. Sanda Clark in July 2012 and Ms. Mayers was told that the Clarks had a very negative investment experience with a prior firm and moved their account to Mr. Hughes because of their previous experience. They told him that they wanted to be very careful and conservative with their investments. (Tr. 90:15-25)

58. The Clarks were in their early 60's and did not have any form of pension and they were relying on their investment with Mr. Hughes, along with social security for their retirement.

59. Based on the record, the Clarks had very little investment experience and invested mainly in mutual funds previously.

60. Ms. Mayers further testified as with Mr. Johns, the Clarks were also told to "stay the course" because a market crash was going to come along and then they would really "make some money." (Tr. 91-92:16-5)

61. This sounded like gambling to the Clarks and they eventually closed their account with Mr. Hughes.

62. Another Division Financial Institutions Examiner, Mr. Steve Steger, who is also a Certified Fraud Examiner, testified that his duties include examining the books and records of financial institutions, broker/dealers and investment advisors.

63. Mr. Steger testified that he also participated in the investigation which involved the Respondents. (Tr. 97:12-19)

64. Mr. Steger testified that LFA was licensed by the state as an IA in April 2008. (Tr. 99:2-4) (Ex. S-3B)

65. According to the Commission's records, LFA was organized as a limited liability company in Arizona on December 8, 2009. (Ex. S-3A)

66. At the time of LFA's formation, according to Commission records, Respondent Hughes was its sole member and acted as its manager. (Ex. S-3B)

67. The Central Registration Depository ("CRD") which is maintained by the Financial Industry Regulatory Authority ("FINRA) contained records which showed that LFA terminated its registration on July 6, 2012 with the State of Arizona. (Ex. S-2)

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68. Mr. Steger testified that with respect to Respondent Hughes' personal registration summary he was not registered with any current employers and was last registered with American Express Financial Advisors in June 1998. (Tr. 100-101:19-6)

69. Mr. Steger testified that there were no records that Mr. Hughes was registered with LFA. (Tr. 101:7-11)

70. According to Commission records, Respondent Hughes was not registered with the Commission between January 1, 2009 and July 5, 2013 as either a securities salesman or dealer pursuant to Article 9 of the Act. Additionally, Mr. Hughes had not made a notice filing or been licensed with the Commission as an IA or IAR pursuant to Article 4 of the IM Act. (Tr. 101-102:19-5)

71. LFA's Uniform Application for Investment Adviser Registration ("Form ADV"), was filed on February 6, 2008. (Ex. S-5A)

72. The second portion of LFA's Form ADV is a multi-page document in which the IA is required to give to all prospective customers and to provide to their clients on an annual basis. This document states the advisor's business model. (Ex. S-5B)

73. LFA's business plan states that LFA was to provide investment advisory services for 80 percent of its activities, 10 percent for additional consultations, 5 percent in matters not involving securities and 5 percent furnishing advice about securities in any manner not previously described. (Ex. S-5B)

74. LFA's Form ADV provides that "individuals associated with LFA will provide its investment advisory services. These individuals are appropriately licensed, qualified, and authorized to provide advisory services on behalf of the firm. Such individuals are known as IARs." (Ex. S-5B)

75. LFA's Form ADV provides further that accounts will be traded according to the client's objectives such as maximum capital appreciation, growth or income, and with respect to trading, will utilize strategies consistent with the degree of risk which the client had specified. (Ex. S-5B)

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76. LFA's Form ADV provides that LFA or Mr. Hughes will be sure to maintain the client's account in a fashion to ensure that there is no conflict of interest with his own issues. (Ex. S-5B)

77. LFA's Form ADV also provides for aggregate trading to provide commission savings on transactions. (Ex. S-5B)

78. If aggregate trading was engaged in by LFA, allocation statements were to be prepared describing how LFA would allocate the order among its clients. (Ex. S-5B)

79. Mr. Steger testified that when he reviewed LFA's client files he did not observe any allocation statements. (Tr. 107-108:25-2)

80. On February 19, 2010 a Form ADV was filed by LFA with the CRD by Respondent Hughes acting as LFA's Chief Compliance Officer. (Ex. S-6A)

81. According to Mr. Steger, the responses for LFA's Form ADV were consistent with the Form ADV filed earlier by Respondent Hughes for LFA prior to its organization as a limited liability company.

82. During Respondent Hughes' Examination Under Oath ("EUO") Mr. Hughes acknowledged that he did not prepare, before entering an aggregated order for a group of clients, a written statement/allocation statement which specified the participating client accounts and how funds would be allocated between the clients. (Ex. S-56)

83. Although Mr. Hughes had testified during his EUO that he had a personal bank account at Vantage West Credit Union and also a business banking account with the same credit union, in response to a Division subpoena, Respondent Hughes' credit union stated that it had no records or accounts for LFA. (Ex. S-79)

84. Based on the evidence received in response to the Division's subpoena, the joint owner of Respondent Mark Hughes' credit union account was Respondent Dolly A. Hughes. (Ex. S-79)

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85. LFA's Investment Advisor Compliance Manual and Written Supervisory Procedures specifies that no IAR shall solicit potential business from a prospective advisory client nor render any advice unless registered in the client's state of residence, unless exempt from registration. However, Respondent Hughes was not registered as an IAR in Arizona. (Ex. S-13)

86. According to Mr. Steger, the Division's financial institution examiner, although LFA's Investment Advisory Compliance Manual and Written Supervisory Procedures was extensive, "it was a template" which was purchased by Respondent Hughes who "tweeked it to his own firm." (Tr. 121:1-5)

87. Mr. Steger testified that he had received a Financial Planning Contract dated June 23, 2009, an Investment Management Agreement dated August 7, 2009 and an Investment Policy Statement dated September 1, 2009 from Mr. Hughes that were related to Mr. and Mrs. Clark. According to these documents, the Clarks had a moderate risk tolerance. (Tr. 122:6-17)

88. During the course of the Division's investigation, it was able to secure trading statements from the records custodians of TD Ameritrade and Scottrade including account statements and applications, updates and agreements for LFA and Respondent Hughes which utilized these firms as custodians for their clients' accounts. (Tr. 122-123:18-17)

89. Mr. Steger testified that upon reviewing the Ameritrade statement with respect to Mr. Jones, the leveraged ETF in some instances was a "bull" indicating that it was planned to go up, and that because these funds were highly leveraged, they could increase in value by three times; however, the same could happen if the fund was a "bear" and was to decrease in value because of the leverage factor and could lose three times the invested amount. (Tr. 124-125:19-15)

90. Mr. Steger stated that with investments being made in highly leveraged ETFs it was like "rolling dice." (Tr. 126:19-22)

91. Mr. Steger testified that the majority of the trades which were reflected in the TD Ameritrade statement for Mr. Jones were leveraged either "bear" or "bull" shares usually leveraged three times. (Tr. 129:2-11)

92. Based on the evidence, Mr. Jones' Scottrade account handled by the Respondents was also very speculative. (Ex. S-19)

93. Mr. Steger testified that he also reviewed the records of the Scottrade account of Hank Masek and this account also reflected trading in the highly speculative leveraged ETFs. (Tr. 130:11-21) (Ex. S-22)

94. According to Mr. Steger, since Respondents charged a fee for managing their clients accounts, even when the trades were losing money, Mr. Hughes still made a fee based on the percentage charged for the funds under his management. (Tr. 131:4-15)

95. Mr. Steger further stated that when he reviewed Harry Clark's Roth IRA, he found that it was all speculative trading involving leveraged ETFs. (Tr. 131-132:19-2) (Ex. S-25)

96. Mr. Steger testified further that Mrs. Clark's IRA reflected the same speculative trading in leveraged ETFs. (Tr. 132:13-24)(Ex. S-25)

97. Mr. Steger testified that he reviewed a number of the Clarks' accounts from Scottrade and TD Ameritrade and they were all similar leveraged ETFs in that they were "somewhat aggressive small capitalization companies." (Tr. 133, 134, and 135)

98. Mr. Steger stated that upon review of Chris and Jean Johns' IRA accounts with TD Ameritrade, they were all similar types of investments, "'bulls' and 'bears' ETFs, three times leveraged." (Tr. 136: 3-20) (Ex. S-34, S-35 and S-36)

99. Mr. Steger further testified that he had reviewed the accounts of Respondents Mark and Dolly Hughes and that these accounts reflected the same types of investments which Mr. Hughes made for his clients in the leveraged ETFs. (Tr. 137:5-11)

100. Mr. Steger stated that he had reviewed summaries of the different funds whose shares were traded by the Respondents for his clients and these summaries contained language to the effect that these funds were riskier than other alternatives that are not leveraged, because their objective was to magnify the performance of the index of the fund and it was recommended that these forms of securities should not be held for longer than a day. (Tr. 138-139:5-24)

101. Mr. Steger read from a summary prospectus for the Direxion Daily Financial Bull 3X Shares which stated "the fund is different and much riskier than most exchange-traded funds. The fund is designed to be utilized by knowledgeable investors who understand the potential consequences of seeking daily leveraged investment results, understand the risks associated with the

use of leverage and are willing to monitor their portfolios frequently. The fund is not intended to be used by, and is not appropriate for, investors who do not intend to actively monitor or manage their portfolios." (Tr. 140:3-18)

102. The summary also stated that an investor could lose three times what they could in a normal investment because of the amount of exposure an investor could experience if the investment is held for more than one day.

103. Mr. Steger confirmed that after reviewing other leveraged ETF summary prospectuses, they were all consistent in pointing out that leveraged ETFs could expose the investor to greater risks due to the nature of the investments.

104. According to Mr. Steger, LFA had a written policies and procedures manual. As an investment advisor, LFA was required by the Division to adhere to its policies, which included acting solely in the best interest of the client and to make full disclosure of all material facts and to render disinterested and impartial advice and to make suitable recommendations in light of the clients' needs and investment objectives. (Tr. 166-167)

105. Mr. Paul Litteau, who formerly worked for the National Association of Securities Dealers ("NASD") for approximately seven years, was called as an expert witness by the Division. Mr. Litteau had been the supervisor of examiners in the NASD Chicago office, and was familiar with sales practices, and financial and operational conditions, as well as examinations for cause.

106. Mr. Litteau testified that he had examined the various accounts of the clients of Respondents LFA and Mr. Hughes with respect to the allegations made by the Division in the notice. (Tr. 172:8-13)

107. Mr. Litteau stated that his primary focus during his review was in the area of suitability and the recommendations made to the client in light of their investment objectives, financial resources, time horizon, age, tax considerations, and various other factors such as risk orientation and risk variability. (Tr. 172-173:18-4)

108. Mr. Litteau described the difference between a retail account which is nondiscretionary where every recommendation should be appropriate and the client makes the ultimate investment decision, and a managed account for a client such as with a financial advisor

such as LFA that has discretionary power to make investment decisions for the client, but they have to be consistent with the projections on the investment and the needs of that client. (Tr. 173:5-15)

109. Mr. Litteau testified that an investment advisor has a fiduciary duty of responsibility and the highest standard of care on behalf of their clients. (Tr. 173-174:19-3)

110. Mr. Litteau described the characteristics of ETFs by stating that the characteristics of the ETFs are that they are portfolios of securities or other instruments that are constructed to provide a return that is either positively or negatively correlated to an underlying index or benchmark which can either be a one time correlation or a multiple correlation.

111. Based on Mr. Litteau's review of the various prospectuses of the leveraged ETFs involved in this proceeding, it was obvious that they were not intended to be held for extended periods of time, but instead should have been traded on a daily basis if they were used at all for investment purposes, due to their speculative nature.

112. Mr. Litteau further stated that the risks to Respondents' clients were magnified the longer the holding period of the particular investment in the leveraged ETFs.

113. According to Mr. Litteau, the various funds held in Mr. Jones' portfolio were held for periods of up to three months. (Tr. 180:11-14)

114. Mr. Litteau testified further that in his opinion, Respondents' client, Mr. Royce Jones, whose risk tolerance was moderate to moderately aggressive, should not have been invested in leveraged ETFs at all, unless Mr. Jones' investment objective had been aggressive or speculative.

115. Mr. Litteau stated further that if Mr. Jones' investment objective changed from moderate to moderately aggressive to conservative, the actions taken in his portfolio were even more inappropriate. (Tr. 181:11-18)

116. Mr. Litteau testified that the securities in Mr. Jones' account were not suitable for him and that the way they were traded amplified this problem. (Tr. 181:19-25)

117. Mr. Litteau testified about Respondent Hughes' email of June 29, 2012, sent to his client Robin Jones where he informed her that he was no longer going to be managing the portfolio and made three or four investments that "could be held for the forseeable future." Mr. Litteau testified that was not an accurate statement because these investments were not meant to be held for a

long period of time, and returning the management of a portfolio to the client who may not understand the risks results in the client being unprotected and was inappropriate. (Tr. 183-184)

118. Mr. Litteau stated that the IRA statement of Hank Masek, who had a risk tolerance of being moderately conservative, contained an asset allocation chart that was consistent with being moderately conservative; however, the trading in the account became very aggressive using leveraged ETFs. (Tr. 186-187)

119. Mr. Litteau stated that at no time was the trading consistent in Mr. Masek's account for an individual with a risk tolerance of being moderately conservative. (Tr. 188:4-7)

120. In Mr. Litteau's opinion, the level of activity and the securities traded in the Masek account were not suitable for an individual such as Mr. Masek. (Tr. 189-190:22-2)

121. According to Mr. Litteau, the trading activity in Chris Johns and his wife's accounts was consistent with the trading activity in Respondents' other clients accounts with a mix of short term holdings in cash and money, but with very heavy utilization of the leveraged ETFs.

122. Mr. Litteau specifically stated that for someone in Mr. Johns' position who had lost his job and had approximately $50,000 in assets, these investments would be unsuitable investments for an investor with an objective to have security for the principal amount that was invested. (Tr. 194:1-10)

123. Mr. Litteau stated that the type of individual who invested in ETFs would be a very "sophiscated professional trader, a very aggressive speculator, a very wealthy person who has the risk bearing ability and is willing just to take very short term, or in this case, longer term bets on the direction of the market." (Tr. 196:4-14)

124. Accordingly, Mr. Litteau stated that none of the clients of the Respondents fit the type of person which he described as investing in these forms of investments. (Tr. 196:15-18)

125. Ms. Denise Fritz, a forensic accountant for the Division, qualified as an expert witness and testified concerning the Division's investigation of the Respondents.

126. Ms. Fritz stated that from January 1, 2009 through December 31, 2010, there was a decrease in Royce Jones 401(K) account by $220,000 as a result of Respondents' trading activity. (Tr. 209:6-11) (Ex. S-64)

127. According to Ms. Fritz, the Royce Jones IRA lost over $400,000 in value from December 31, 2008 to June 30, 2012 when Respondents were managing the account. (Tr. 213:5-10) (Ex. S-64)

128. Ms. Fritz reviewed the Scottrade account for Mr. Masek for the period of January 1, 2009 through June 30, 2012. This account reflected the trading of the ETFs similar to Mr. Jones' account and showed that Mr. Masek's account decreased in value by $66,720.00. (Ex. S-66)

129. Ms. Fritz stated that after reviewing three IRA accounts for Mr. and Mrs. Johns with TD Ameritrade, the largest loss occurred in Mr. Johns' conventional IRA but the total decrease in value was $29,280.00. (Tr. 219:10-13)

130. Ms. Fritz reviewed the accounts of the Clark family that contained ETFs which were traded through Ameritrade and Scottrade from January 1, 2009 to June 30, 2012. (Ex. S-68 and S-72)

131. According to Ms. Fritz, the various Clark accounts experienced a total decrease of $10,487.97 during the relevant time frame. (Ex. S-73)

132. Ms. Fritz further testified that she also created the same type of reports for Respondent Hughes' accounts for the time frame of January 1, 2009 through June 30, 2012 involving the ETFs which were similar to Respondents' other accounts for his clients. Both Ameritrade and Scottrade accounts were utilized for both Mr. and Mrs. Hughes, but in the case of the Hughes accounts they increased in value by $340,139.06. (Tr. 224:16-19)

133. Ms. Fritz testified that she did not know why the Hughes accounts gained in value as against the accounts of Mr. Hughes' clients, whose accounts lost money. (Tr. 225:3-9)

134. Based on the record, a preponderance of the evidence establishes that Respondents committed multiple violations of the IM Act with respect to licensing violations. When LFA was organized as a limited liability company, Respondent Mark Hughes became an unlicensed IAR and therefore LFA's license should be revoked. Additionally, both LFA and Respondent Mark Hughes violated the anti-fraud provisions of the IM Act by misrepresenting that Respondent Hughes was a licensed IAR and by repeatedly placing his client's investments at risk by investing in leveraged ETFs which were risky investments and contrary to the clients' investment objectives. Therefore, Respondents should be subject to a cease and desist order, an order of restitution and an order for the

payment of administrative penalties. Additionally, based on the record, the marital community of Respondent Mark Hughes and that of his spouse should be jointly and severally liable for the payment of restitution and administrative penalties.

CONCLUSIONS OF LAW

1. The Commission has jurisdiction of this matter pursuant to Article XV of the Arizona Constitution and A.R.S. § 44-3101, et seq.

2. Respondent Mark Hughes acted as an unlicensed IAR in violation of A.R.S. § 44-3151(A).

3. LFA employed Respondent Mark Hughes, an unlicensed IAR, in violation of A.R.S. § 44-3151(C).

4. LFA engaged in dishonest and unethical conduct by misrepresenting that it would employ a licensed investment advisor.

5. Respondent LFA has violated the IM Act and should cease and desist pursuant to A.R.S. §§ 44-3201 and 44-3292 and from any future violations of the IM Act.

6. The actions and conduct of Respondent LFA caused multiple violations of the IM Act and are grounds for the revocation of its IA license, restitution and administrative penalties pursuant to A.R.S. §§ 44-3201 and 44-3292.

7. Respondents LFA and Mark Hughes engaged in dishonest or unethical practices and committed fraud in the provision of investment advisory services by employing a scheme to defraud, making untrue statements of material facts, misrepresenting professional qualifications and engaging in a course of business that would operate as a fraud or deceit in violation of A.R.S. § 44-3241.

8. Respondent Mark Hughes has violated the IM Act and should cease and desist pursuant to A.R.S. § 44-3292.

9. The actions and conduct of Respondent Mark Hughes constitute multiple violations of the IM Act and are grounds for an order of restitution pursuant to A.R.S. § 44-3292 and administrative penalties pursuant to A.R.S. § 44-3296.

10. The marital community of Mark Hughes and Dolly Hughes should be included in any order of restitution and penalties ordered herein pursuant to A.R.S. § 44-3291.

ORDER

IT IS THEREFORE ORDERED that pursuant to the authority granted to the Commission under A.R.S. §§ 44-3201, 44-3241, and 44-3292 Respondent Legacy Financial Advisors, LLC and Mark D. Hughes shall cease and desist from their actions described herein in violation of the IM Act.

IT IS FURTHER ORDERED that the license of Legacy Financial Advisors, LLC as an investment advisor shall be revoked pursuant to A.R.S. § 44-3201.

IT IS FURTHER ORDERED that pursuant to the authority granted to the Commission under A.R.S. §§ 44-3201(B) and 44-3296, Respondents Legacy Financial Advisors, LLC and Mark D. Hughes shall pay jointly and severally as and for administrative penalties for their violations of the IM Act the sum of $50,000.

IT IS FURTHER ORDERED that the payment obligation for the administrative penalties shall be subordinate to any restitution and shall become immediately due and payable only after restitution payments have been paid in full or upon Respondents' default with respect to Respondents' restitution obligations.

IT IS FURTHER ORDERED that pursuant to the authority granted to the Commission under A.R.S. §§ 44-3201(B) and 44-3292, Respondents Legacy Financial Advisors, LLC and Mark D. Hughes shall jointly and severally make restitution in the amount of $340,806.30 subject to any legal set-offs by the Respondents and confirmed by the Director of Securities with said restitution to be made within 60 days of the effective date of this Decision.

IT IS FURTHER ORDERED that pursuant to the authority granted to the Commission under A.R.S. § 44-3291(C) the marital community of Respondents Mark D. Hughes and Dolly A. Hughes shall be jointly and severally liable with Legacy Financial Advisors, LLC to pay restitution in the amount of $340,806.30 and administrative penalties in the amount of $50,000 pursuant to A.R.S. § 44-3291(C) to the extent allowable pursuant to A.R.S. § 25-215.

IT IS FURTHER ORDERED that default shall render Respondents Legacy Financial Advisors, LLC, Mark D. Hughes and Dolly A. Hughes liable to the Commission for its costs of collection and interest at the rate of the lessor of 10 percent per annum or at a rate per annum that is equal to one percent plus the prime rate as published by the Board of Governors of the Federal

Reserve System of Statistical Release H.15 or any publication that may supercede on the date that the judgment is entered.

IT IS FURTHER ORDERED that pursuant to the authority granted to the Commission under A.R.S. §§ 44-3201(B) and 44-3296, that Respondents Legacy Financial Advisors, LLC, Mark D. Hughes and Dolly A. Hughes jointly and severally shall pay the administrative penalties ordered hereinabove in the amount of $50,000, payable by either cashier's check or money order payable to "The State of Arizona" and presented to the Arizona Corporation Commission for deposit in the general fund for the State of Arizona.

IT IS FURTHER ORDERED that if Respondents Legacy Financial Advisors, LLC, Mark D. Hughes and Dolly A. Hughes fail to pay the administrative penalties hereinabove, any outstanding balance plus interest at the rate of the lessor of 10 percent per annum or the rate per annum that is equal to one percent plus the prime rate as published by the Board of Governors of the Federal Reserve System of Statistical Release H.15 or any publication that may supercede on the date that the judgment is entered may be deemed in default and shall be immediately due and payable, without further notice.

IT IS FURTHER ORDERED that all restitution payments as ordered hereinabove shall be deposited into an interest bearing account(s), if appropriate until distributions are made.

IT IS FURTHER ORDERED that the Commission shall disburse the funds on a pro-rata basis to the investors shown on the records of the Commission. Any restitution funds that the Commission cannot disburse because an investor refuses to accept such payment, or any restitution funds that cannot be disbursed to an investor because an investor is deceased and the Commission cannot reasonably identify and locate the deceased investors' spouse or natural children surviving at the time of distribution shall be disbursed on a pro-rata basis to the remaining investors shown on the records of the Commission. Any funds that the Commission determines that it is unable to or cannot feasibly disburse shall be transferred to the general fund of the State of Arizona.

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IT IS FURTHER ORDERED that if Respondents Legacy Financial Advisors, LLC, Mark D. Hughes and Dolly A. Hughes fail to comply with this Order, the Commission may bring further legal proceedings against Respondent(s) including application to the Superior Court for an order of contempt.

IT IS FURTHER ORDERED that pursuant to A.R.S. § 44-1974, upon application, the Commission may grant rehearing of this Order. The application must be received by the Commission at its offices within twenty (20) calendar days after entry of this Order and, unless otherwise ordered, filing an application for rehearing does not stay this Order. If the Commission does not grant rehearing within twenty (20) calendar days of the filing of the application, the application is considered to be denied. No additional notices will be given of such denial.

IT IS FURTHER ORDERED that this Decision shall become effective immediately.

BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

CHAIRMAN COMMISSIONER

COMMISSIONER COMMISSIONER COMMISSIONER

IN WITNESS WHEREOF, I, JODI JERICH, Executive Director of the Arizona Corporation Commission, have hereunto set my hand and caused the official seal of the Commission to be affixed at the Capitol, in the City of Phoenix, this _____day of _____ 2014.

JODI JERICH
EXECUTIVE DIRECTOR

DISSENT _____

DISSENT _____
MES:tv

SERVICE LIST FOR: MARK DANA HUGHES, CRD # 1843511, and DOLLY A. HUGHES, husband and wife, and LEGACY FINANCIAL ADVISORS, L.L.C., CRD # 114029, an Arizona limited liability company

DOCKET NO.: S-20864A-12-0439

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