

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

OPEN MEETING ITEM



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ARIZONA CORPORATION COMMISSION  
AZ CORP COMMISSION  
DOCKET CONTROL

DATE: SEPTEMBER 26, 2014

2014 SEP 26 AM 9 24

DOCKET NOS.: S-20757A-10-0373

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:

RICHARD M. SCHMERMAN  
(NOTICE OF OPPORTUNITY)

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:

OCTOBER 6, 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:

OCTOBER 16, 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.

Arizona Corporation Commission

DOCKETED

SEP 26 2014

DOCKETED BY 

  
JODI JERICHI  
EXECUTIVE DIRECTOR

1200 WEST WASHINGTON STREET; PHOENIX, ARIZONA 85007-2927 / 400 WEST CONGRESS STREET; TUCSON, ARIZONA 85701-1347  
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This document is available in alternative formats by contacting Shaylin Bernal, ADA Coordinator, voice phone number 602-542-3931, E-mail [SBernal@azcc.gov](mailto:SBernal@azcc.gov).

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**BEFORE THE ARIZONA CORPORATION COMMISSION**

COMMISSIONERS

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

IN THE MATTER OF:  
  
RICHARD M. SCHMERMAN, individually and  
d/b/a Diversified Financial and/or Diversified  
Financial Planners, and Amy Schmerman, husband  
and wife.

RESPONDENTS.

DOCKET NO. S-20757A-10-0373

DECISION NO. \_\_\_\_\_

OPINION AND ORDER

DATE OF PRE-HEARING CONFERENCE:           October 21, and December 16, 2010  
DATE OF STATUS CONFERENCE:                November 17, 2011, March 12, 2012, and March  
6, 2013  
DATES OF HEARING:                             September 30, October 1, and 2, 2013  
PLACE OF HEARING:                            Phoenix, Arizona  
ADMINISTRATIVE LAW JUDGE:                 Marc Stern  
APPEARANCES:                                 Mr. Phong Paul Huynh, Staff Attorney, on behalf  
of the Securities Division of the Arizona  
Corporation Commission.

**BY THE COMMISSION:**

On September 9, 2010, the Securities Division (“Division”) of the Arizona Corporation  
Commission (“Commission”) filed a Notice of Opportunity for Hearing (“Notice”) against Richard  
M. Schmerman d/b/a Diversified Financial and/or Diversified Financial Planners (“Diversified”) and  
Amy Schmerman, husband and wife (collectively “Respondents”), in which the Division alleged  
multiple violations of the Arizona Securities Act (“Act”) and the Investment Management Act (“IM  
Act”) in connection with Respondent Richard M. Schmerman’s practices in business and securities  
matters which allegedly involved mishandling of client funds and misrepresentation.

Amy Schmerman, the spouse of Respondent Richard M. Schmerman, was joined in the action

1 pursuant to A.R.S. §§ 44-2031 and 44-3291 solely for the purpose of determining the liability of the  
2 marital community.

3 The Respondents were duly served with copies of the Notice.

4 On September 20, 2010, a request for hearing was filed by the Respondents.

5 On September 22, 2010, by Procedural Order, a pre-hearing conference was scheduled on  
6 October 21, 2010.

7 On October 21, 2010, at the pre-hearing conference, the Division and Respondents appeared  
8 through counsel. The parties discussed a possible resolution of the issues raised by the Notice, and  
9 agreed that a status conference should be scheduled in approximately 60 days.

10 On October 22, 2010, by Procedural Order, a status conference was scheduled on December  
11 16, 2010.

12 On December 16, 2010, the Division and Respondents appeared through counsel at the status  
13 conference. The parties continued to discuss a resolution of the proceeding and in the interim, the  
14 Division requested that another status conference be scheduled in approximately 60 days.

15 On December 16, 2010, by Procedural Order, a status conference was scheduled on February  
16 23, 2011.

17 On February 22, 2011, the Division and Respondents filed a Joint Stipulation to Continue the  
18 status conference for at least 60 days in order that the parties could continue to review matters and  
19 attempt to resolve the issues raised by the Notice.

20 On February 23, 2011, by Procedural Order, the status conference was continued to April 25,  
21 2011.

22 On April 22, 2011, the Division and Respondents filed another Joint Stipulation to Continue  
23 the status conference for at least 60 days to allow the parties to continue to work towards a settlement  
24 of the issues raised by the Notice.

25 On April 25, 2011, by Procedural Order, the status conference was continued to July 7, 2011.

26 On July 5, 2011, the Division and Respondents filed another Joint Stipulation to Continue the  
27 status conference for at least 60 days to allow the parties to continue to work towards a settlement of  
28 the issues raised by the Notice. Subsequently, by Procedural Order, the status conference was

1 continued to September 8, 2011.

2 On September 7, 2011, the Division and Respondents filed another Joint Stipulation to  
3 Continue the status conference for sixty days or more to allow the parties to review additional  
4 documentation and to discuss a possible resolution of the proceeding. Subsequently, by Procedural  
5 Order, the status conference was continued to November 17, 2011.

6 On November 17, 2011, the Division and Respondents appeared through counsel. The  
7 Division indicated that it was preparing to file a Motion to Amend the Notice adding additional  
8 allegations against Respondents. The Division and Respondents were continuing to discuss a  
9 possible resolution of the proceeding, but in the interim, counsel agreed that an additional status  
10 conference be scheduled in March 2012.

11 On November 21, 2011, by Procedural Order, a status conference was scheduled as agreed on  
12 March 12, 2012.

13 On December 6, 2011, the Division filed a Motion to File Amended Notice ("Motion").

14 On December 12, 2011, the Division and Respondents filed a Joint Stipulation regarding the  
15 Division's Motion. Respondents had no objections to the filing of the Amended Notice and the  
16 parties stipulated that Respondents' initial request for hearing filed September 20, 2010, would be  
17 applicable as to the Amended Notice. Additionally, the parties stipulated that Respondents would  
18 have at least 30 days to file an Answer from the date of a Procedural Order which authorized the  
19 filing of the Amended Notice.

20 On December 14, 2011, the Division was authorized to file the Amended Notice as stipulated  
21 by the parties.

22 On March 12, 2012, at the status conference, the Division and Respondents appeared through  
23 counsel. The Division's counsel indicated that the parties were continuing to negotiate a settlement  
24 of the proceeding, but more time would be required for a resolution of the issues raised by the Notice.  
25 The Division and Respondents agreed that a hearing should commence on June 25, 2012, if a  
26 settlement could not be concluded.

27 On March 13, 2012, by Procedural Order, a hearing was scheduled on June 25, 2012, with the  
28 exchange of documentation scheduled on May 15, 2012.

1 On May 11, 2012, the Division and Respondents filed a Joint Stipulation to Continue the  
2 hearing for at least 60 days and to delay the exchange of documentation until 20 days before the date  
3 of the continued hearing.

4 On May 14, 2012, by Procedural Order, the proceeding was continued as agreed between the  
5 parties, to September 10, 2012.

6 On August 29, 2012, Respondents' counsel filed a Motion to Withdraw and Motion for a  
7 Continuance. Although counsel indicated that Respondents wished to enter into a Consent Order  
8 with respect to the Division's allegations contained in the Amended Notice, it was not made clear as  
9 to why they required a continuance for additional time to conclude a settlement of the proceeding.  
10 Counsel additionally stated that his reasons for withdrawing from the proceeding "would violate  
11 attorney-client privilege," but stated no other reason.

12 On August 31, 2012, the Division responded to the aforementioned motions filed on August  
13 29, 2012, by Respondents' counsel, and urged their denial. The Division stated that the proceeding  
14 was set for hearing in a short time and cited Commission Rule A.A.C. R14-3-104(E) which requires  
15 good cause to be shown for withdrawal from a proceeding, and that by itself, violation of attorney-  
16 client privilege is insufficient cause. Further, the Division described ways for counsel to show good  
17 cause citing Ariz. Rules of Civ. Proc. 5.1(a)(2)(C) which describes the steps to be taken to withdraw  
18 from a proceeding once it has been set for trial, and the Division stated that these steps had not been  
19 followed.

20 On September 5, 2012, a Procedural Order was issued denying the Respondents' Motion to  
21 Withdraw and Motion for a Continuance "unless good cause can be shown." The Procedural Order  
22 further found that the Respondents had not stated a reason to terminate representation consistent with  
23 Rule 1.16 of the Rules of Professional Conduct.

24 On September 6, 2012, the Respondents' counsel submitted to the Commission's Hearing  
25 Division, under seal, a Motion for Reconsideration of Motion to Withdraw and Motion to Continue.  
26 The Assistant Chief Administrative Law Judge undertook an in-camera review of the Motion filed by  
27 Respondents' counsel and concluded that good cause had been stated to grant a 60-day continuance  
28 of the hearing. The request for reconsideration regarding the withdrawal of counsel was taken under

1 further advisement.

2 On September 7, 2012, by Procedural Order, the Respondents' request for a continuance of  
3 the hearing was granted, and the request for withdrawal of counsel was taken under further  
4 advisement.

5 On December 12, 2012, the Division filed a Motion to Set a Status Conference and other  
6 Affirmative Action. There were no responses filed by Respondents or their counsel.

7 On February 6, 2013, by Procedural Order, Respondents' counsel was granted leave to  
8 withdraw.

9 On February 7, 2013, by Procedural Order, a status conference was scheduled on March 6,  
10 2013.

11 On March 6, 2013, at the status conference, the Division appeared with counsel. Respondents  
12 failed to appear. The Division's counsel requested that a hearing be scheduled to allow for continuity  
13 of the proceeding because counsel for the Division estimated that he would call approximately seven  
14 witnesses. Additionally, counsel for the Division stated that he would be involved in a lengthy court  
15 proceeding from early July through the second week of August, and he also would be involved in  
16 another Commission proceeding in mid-September.

17 On March 18, 2013, by Procedural Order, a hearing was scheduled to commence on  
18 September 30, 2013.

19 On September 11, 2013, the Division filed a Motion to Allow Telephonic Testimony of a  
20 witness who was going to be out of town during the scheduled hearing. There were no objections  
21 filed by Respondents.

22 On September 24, 2013, by Procedural Order, the Division's Motion to Allow Telephonic  
23 Testimony was granted.

24 On September 30, 2013, a full public hearing was convened before a duly authorized  
25 Administrative Law Judge of the Commission at its offices in Phoenix, Arizona. The Division  
26 appeared with counsel. Respondents failed to appear. At the conclusion of the proceeding, the  
27 matter was taken under advisement pending submission of a Recommended Opinion and Order to the  
28 Commission.

1 On November 27, 2013, the Division filed a post-hearing brief.

2 \* \* \* \* \*

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

5 **FINDINGS OF FACT**

6 1. Richard M. Schmerman (CRD#1302988), at all relevant times herein was an Arizona  
7 resident and married to Amy Schmerman.

8 2. Diversified Financial and Diversified Financial Planners were trade names owned by  
9 Respondent Schmerman and registered with the office of the Arizona Secretary of State.<sup>1</sup>

10 3. According to documents filed with the Arizona Secretary of State’s office, Diversified  
11 was engaged in tax preparation and provided portfolio management services.

12 4. During the respective time frames described hereinafter, Respondent Schmerman was  
13 acting as an Investment Advisor Representative (“IAR”).

14 5. Respondent Schmerman conducted his business in Maricopa, Arizona.

15 6. Respondent Schmerman was a registered securities salesman from on or about  
16 November 6, 1986 to March 13, 2008, and from May 15, 2008 to March 10, 2010, (CRD #1302988).

17 7. From on or about March 31, 1999 to March 12, 2008, Respondent Schmerman was  
18 registered in Arizona as a securities salesman with Mutual Service Corporation (“MSC”), which was  
19 a registered securities dealer, federally and with the State of Arizona. During that time frame, MSC  
20 was also a federally licensed Investment Advisor (“IA”) and an IA “notice filer” in Arizona.<sup>2</sup>

21 8. From on or about May 15, 2008, to March 10, 2010, Respondent Schmerman was  
22 registered as a securities salesman in Arizona with United Planners Financial Services of America, a  
23 limited partnership (“United Planners”). United Planners is a federally licensed IA and an IA notice  
24 filer in Arizona. United Planners is also a registered securities dealer, federally and with the State of  
25 Arizona.

26  
27 <sup>1</sup> Diversified Financial Planners was organized as a limited liability company by its sole member Respondent Richard  
Schmerman on May 6, 2010. (Ex. S-3)

28 <sup>2</sup> On December 23, 2009, MSC’s federal IA was terminated.

1           9.       From on or about June 3, 2008 to March 10, 2010, Respondent Schmerman was  
2 licensed in Arizona as an IAR in association with United Planners.

3           10.       The Division, in support of its allegations in the Notice, called seven witnesses as  
4 follows: four investors, Burritt Steward, Judy Pellish, Dr. Rolf Vrla, and Elizabeth Aiken Toth;  
5 Gregory Thomsen, a special investigator with the Division; and Sean Callahan, a forensic accountant  
6 with the Division, who qualified as an expert witness.

7           11.       Mr. Burritt Steward, a retired Arizona resident, testified that Respondent Schmerman  
8 handled his investments for approximately 23 years. (Tr. 31:15-14)

9           12.       On September 11, 1995, Respondent Schmerman wrote a letter on Diversified's  
10 letterhead to Mr. Steward and represented that he was an IA. (Ex. S-20a)

11           13.       On March 30, 1996, Mr. Schmerman again wrote a letter to Mr. Steward representing  
12 that he was a registered IA on "Diversified's letterhead." (Ex. S-20b)

13           14.       Mr. Steward employed Mr. Schmerman as an investment advisor from approximately  
14 1995 to 2012.

15           15.       Because Mr. Steward believed Respondent Schmerman was a licensed or registered  
16 IA, he believed that Mr. Schmerman had his best financial interests at heart. (Tr. 36:6-20)

17           16.       In December 2004 and July 2005, Mr. Steward wrote two checks to Diversified in the  
18 amount of \$1,845.00 which he believed were payments for IA fees. (Tr. 38:14-23)(EX. S-21b)

19           17.       Mr. Steward testified that on July 22, 2005, he also wrote a check for \$162,620.54  
20 payable to Diversified and gave the check to Mr. Schmerman, who was to put it into a CD or money  
21 market account until the stock market got better and it could be reinvested. (Tr. 39:8-23)(Ex. S-21b)

22           18.       Mr. Steward stated that he did not give the large check to Respondent Schmerman as  
23 either a loan or a gift. (Tr. 40:16-25)

24           19.       Mr. Steward cashed in stock on May 3, 2006, and he wrote another check to  
25 Diversified for \$86,897.00 and gave the check to Respondent Schmerman, believing it would be  
26 invested. He testified that these funds did not represent either a loan or a gift to Mr. Schmerman, but  
27 were to be invested for Mr. Steward. (Tr. 41-42:1-3)(Ex. S-21b)

28           20.       According to Mr. Steward, in the case of both of the larger checks, Mr. Schmerman

1 was to hold the funds until it was time to reinvest them. (Tr. 42:12-19)

2 21. Mr. Steward testified that he gave the two checks totaling approximately \$250,000 to  
3 Respondent Schmerman because he trusted him and believed that he would invest the money for him  
4 as he said he would. (Tr. 43:14-20)

5 22. Additionally, Mr. Steward testified that he also gave a check for \$100,000.00 to  
6 Respondent Schmerman on or about May 20, 2010, payable to Diversified. This was done with the  
7 understanding that Respondent Schmerman would invest this \$100,000.00 for him with his other  
8 monies. Mr. Steward testified that these funds too did not represent either a personal loan or a gift to  
9 Respondent Schmerman. (Tr. 43-44:21-23)(Ex. S-21b)

10 23. Mr. Steward never consented to allow Respondent Schmerman to use any of his funds  
11 for Respondent Schmerman's personal expenses or to settle any lawsuits against Respondent  
12 Schmerman. (Tr. 45:13-21)

13 24. Mr. Steward stated that he had received statements with respect to his account with  
14 Respondent Schmerman prior to 2006, but after that year he stopped receiving statements on a  
15 regular basis, for approximately 4 years. When he requested them, Respondent Schmerman told him  
16 that some of his records had been burned in a fire and that burglars had damaged his computers. Mr.  
17 Steward further stated that he believes this was a sham by Respondent Schmerman. (Tr. 48-49:7-3)

18 25. According to Mr. Steward, during the time that Respondent Schmerman was acting as  
19 his investment advisor, he paid him about a 1.5% monthly fee on his investments.

20 26. Mrs. Judy Pellish, another Arizona resident, testified that she is Respondent  
21 Schmerman's aunt, and that she had attended Respondent Schmerman's wedding to his wife, Amy.  
22 (Tr. 55:1-22)

23 27. Mrs. Pellish stated that she became an investment client of Respondent Schmerman's  
24 in approximately 1997 when she moved to Arizona. (Tr. 56:4-15)

25 28. In a letter on Diversified stationary dated March 8, 2004, addressed to Mrs. Pellish,  
26 Respondent Schmerman represented himself to be a registered IA. (Ex. S-61)

27 29. According to Mrs. Pellish, Respondent Schmerman told her that since she was a  
28 relative he would not charge her a fee. However, she later found out that "he was actually keeping

1 \$600.00 a year for taking care of my finances ... until I started discovering his crooked things that he  
2 was doing.” (Tr. 57-58:20-4)

3 30. Mrs. Pellish testified that she believed her nephew, Respondent Schmerman, managed  
4 her funds in a Charles Schwab and Company (“Charles Schwab”) brokerage account and that he was  
5 still her IA in 2012. At no time did Mr. Schmerman tell her that he was no longer registered as either  
6 a securities salesman or a licensed IAR. (Tr. 59-60:7-6)

7 31. Based on the record, on June 9, 1997, Ms. Pellish first became a client of Respondent  
8 Schmerman when she gave him two checks. One check was for \$100,000.00 made out to Diversified  
9 and one check was for \$200,000.00 made out to Pershing, another investment company. These funds  
10 represented monies which she had received from the sale of her home in California. (Tr. 61-62:19-  
11 11)

12 32. According to Mrs. Pellish, her nephew was to invest the money for her to provide her  
13 with a set monthly payment until she died, at which time her monies were to be distributed to her  
14 children, who were her beneficiaries. (Tr. 62:12-21)

15 33. In furtherance of this goal, Mrs. Pellish asked Mr. Schmerman to invest in safe  
16 securities, but she said that she never got an answer from him, or any paperwork. (Tr. 64-65:22-7)

17 34. Mrs. Pellish believed that her \$300,000.00 which she had given Respondent  
18 Schmerman would be deposited into an account or some form of security held in her name for her  
19 benefit. (Tr. 65:17-22)

20 35. Although Mrs. Pellish received monthly payments, she did not receive any written  
21 statements. (Tr. 65:22-25)

22 36. Mrs. Pellish testified that initially she received \$1,600.00 a month for approximately  
23 eighteen months, but since she feared she might live longer, she had Mr. Schmerman reduce the  
24 monthly payment to \$1,200.00 a month, believing her funds would last longer. (Tr. 66:9-17)

25 37. Mrs. Pellish further testified that when she requested written statements from  
26 Respondent Schmerman, he would continually make excuses for the lack of statements - saying there  
27 was a fire or he lost some of the files, but he told her not to worry, that her money was safe. (Tr.  
28 67:2-10)

1           38.     According to Mrs. Pellish, Respondent Schmerman had told her that he was going to  
2 create a securities portfolio for her consisting of stocks and bonds. (Tr. 70:1-5)

3           39.     According to Mrs. Pellish's records, after her June 1997 investment of \$300,000.00,  
4 over the next eighteen months she received \$28,800.00 or \$1,600.00 a month, and for the next period  
5 of time from January 1999 to December 2012 she received \$1,200.00 a month, receiving back  
6 approximately \$196,800.00 in payments from Respondent Schmerman. (Tr. 72:8-25)

7           40.     Mrs. Pellish testified that she "had no idea" that Respondent Schmerman was utilizing  
8 her own money which was to have been invested to pay her her monthly "allowance". (Tr. 85:10-16)

9           41.     According to Mrs. Pellish's calculations, from 1997 to 2010 she gave Respondent  
10 Schmerman approximately \$355,000.00 to invest and received back approximately \$259,868.00  
11 leaving an outstanding balance of approximately \$95,132.00 still owed to her. (Tr. 86:14-25)(Ex. S-  
12 62)

13          42.     Mrs. Pellish stated that she only received monthly statements from two brokerages,  
14 MSC and United Planners. (Tr. 88:10-15)

15          43.     Although Mrs. Pellish provided funds to Respondent Schmerman to purchase bonds,  
16 she never received any documentation confirming their purchase. (Tr. 89:1-8)

17          44.     Mrs. Pellish, after not receiving her \$1,200.00 monthly payments, called Respondent  
18 Schmerman and he told her not to worry. Subsequently, in January and February 2012, she went to  
19 see Mr. Schmerman at his house and he reassured her that she would get her money. (Tr. 89:9-22)

20          45.     Mrs. Pellish testified that by June 2012, she had not received anything other than one  
21 or two payments and she confronted Respondent Schmerman, who said that he would give her an  
22 accounting. She said that he put her off again, blaming the fire and other things, but by November  
23 she did not have any more information, and still could not get an accounting. (Tr. 90-91)

24          46.     The last time that Mrs. Pellish received any funds from Respondent Schmerman was  
25 around January 2013 when he deposited \$1,200.00 into her account. (Tr. 92:1-13)

26          47.     Mrs. Pellish testified that although she loaned \$10,000.00 to Respondent Schmerman  
27 as a personal loan, the remaining balance still owed to her was not a gift or any form of loan. (Tr.  
28 93:4-18)

1           48.    Mrs. Pellish testified that she believed that Respondent Schmerman was dishonest  
2 with her in how he handled her financial affairs. (Tr. 96:1-6)

3           49.    Dr. Rolf Vrla, an Arizona resident, testified that a partner in his medical group referred  
4 him to Respondent Schmerman in 2000 when he was looking for an IA. (Tr. 100-101)

5           50.    On September 29, 2000, Respondent Schmerman wrote a letter on Diversified  
6 stationary to Dr. Vrla that stated on the letterhead that Mr. Schmerman was a registered IA. In his  
7 letter, Respondent Schmerman describes the services which he was to provide for Dr. Vrla through  
8 Diversified. (Ex. S-64)

9           51.    Respondent Schmerman's letter to Dr. Vrla stated that Respondent would charge him  
10 1% of the value of Dr. Vrla's investment portfolio by billing his account at Charles Schwab. (Ex. S-  
11 64)

12          52.    Dr. Vrla testified that he employed Respondent Schmerman as his IA until "shortly  
13 after Thanksgiving in 2011." (Tr. 102-103:22-6)

14          53.    Dr. Vrla testified that Respondent Schmerman failed to disclose that after March 2010  
15 he was no longer employed as a registered sales representative with a broker dealer and was no  
16 longer employed as an IAR. (Tr. 111:13-21)

17          54.    Dr. Vrla did not learn that Respondent Schmerman was no longer working as a  
18 registered sales representative or as an IAR until November 28, 2011. (Tr. 111:22-25)

19          55.    According to Dr. Vrla, from March 2010 through the end of 2011, he paid Respondent  
20 Schmerman, who was no longer licensed, approximately \$33,000.00 in fees for advisory services.  
21 (Tr. 120:5-16)

22          56.    Dr. Vrla stated that, after March 2010, when he received checks from Charles Schwab  
23 which were payable to him, following directions from Respondent Schmerman, he deposited the  
24 checks into his personal account and then wrote checks for the corresponding amounts payable to  
25 Respondent Schmerman.<sup>3</sup>

26          57.    After Dr. Vrla learned that Respondent Schmerman was no longer licensed as a  
27

28 <sup>3</sup> Dr. Vrla followed this procedure because Respondent Schmerman had told him that his method of compensation with Charles Schwab had changed.

1 securities salesman or as an IRA, he contacted Charles Schwab in late 2011 to learn why the checks  
2 representing Respondent Schmerman's compensation were being sent to him after March 4, 2010.  
3 Dr. Vrla told Charles Schwab's representative that Respondent Schmerman had "ripped him off" for  
4 over \$30,000.00 and he needed information. (Tr. 129-130:10-25)(Ex. S-65a)

5 58. Dr. Vrla had a conversation with his sister, Ann Draganich, about a similar situation  
6 with Respondent Schmerman. She also had brokerage checks mailed to her and then after depositing  
7 them, she would write checks payable to Mr. Schmerman for the same amounts as were on the  
8 brokerage checks.

9 59. Dr. Vrla learned that Charles Schwab maintained audio files of the voices of the  
10 people who had called in requesting checks to be issued from his account. (Tr. 131:1-7)

11 60. Subsequently, Dr. Vrla listened to a voice recording on a CD which Charles Schwab  
12 sent to the Division. Dr. Vrla denied ever requesting a check from Charles Schwab by telephone, and  
13 identified the voice from the recording as that of Respondent Schmerman. (Tr. 135-136:21-6)

14 61. According to Dr. Vrla, his mother's maiden name had been used for security purposes  
15 on his account with Charles Schwab, but the name provided on the recording was not that of his  
16 mother. (Tr. 138:1-5)

17 62. While listening to the recorded CD, Dr. Vrla repeatedly denied that he had requested  
18 checks telephonically from Charles Schwab, and stated that Respondent Schmerman was the caller.

19 63. Dr. Vrla further testified that, while listening to recordings of another voice, that the  
20 voice was not that of his sister Ann Draganich. (Tr. 140-141:24-1)

21 64. Dr. Vrla stated that he was deceived by Respondent Schmerman when he was billed  
22 for investment advisory services after March 10, 2010, and that Respondent Schmerman had been  
23 dishonest in his handling of Dr. Vrla's account with Charles Schwab. (Tr. 142:11-25)

24 65. Ms. Elizabeth Aiken Toth f/k/a Ms. Elizabeth Aiken, testified that Respondent  
25 Schmerman handled her investments and in 2005 was involved in a transaction for \$175,000.00  
26 involving the Respondent. (Tr. 198-199:7-14)

27 66. Ms. Aiken was present during discussions involving Respondent Schmerman and her  
28 mother, Gloria Aiken, in 2005 when an investment of \$175,000.00 was discussed. (Tr. 199:15-21)

1           67.     According to Ms. Aiken, Respondent Schmerman was to invest her mother's  
2 \$175,000.00 in some kind of a money market account. (Tr. 200:1-12)

3           68.     Ms. Aiken testified that the account was to be in her mother's name, but her mother  
4 never received an account number from Respondent Schmerman or knew where the funds were held.  
5 (Tr. 200:17-20)

6           69.     According to Elizabeth Aiken, her mother, Gloria Aiken, expected to earn interest or  
7 some form of return on her investment. In return for Gloria Aiken's investment, Respondent  
8 Schmerman was to receive a fee or some form of compensation, but Elizabeth Aiken did not recall  
9 the amount or the rate. (Tr. 201:1-7)

10          70.     Ms. Aiken stated that Respondent Schmerman was associated with United Planners at  
11 the time she and/or her mother became clients of Respondent Schmerman. (Tr. 201:15-25)

12          71.     Elizabeth Aiken testified that, according to a letter dated August 14, 2008, from  
13 Respondent Schmerman, a Charles Schwab Institutional Brokerage Account in the name of Gloria  
14 Aiken valued at \$117,204.00 was gifted to Ms. Aiken and deposited into a similar account in  
15 Elizabeth Aiken's name at Charles Schwab. (Tr. 206:1-12)

16          72.     According to Elizabeth Aiken, Respondent Schmerman was to manage that account  
17 and was to be paid a fee. (Tr. 206:13-25)

18          73.     According to a letter dated November 1, 2008 from Respondent Schmerman on  
19 Diversified Financial stationary, he confirmed that he would serve as her investment advisor and  
20 stated that he was changing his affiliation from MSC to United Planners. Ms. Aiken then signed  
21 some documents to switch over with Mr. Schmerman to his new brokerage firm. (Tr. 208:8-22)

22          74.     In the fall of 2009, Ms. Aiken began to experience difficulties with Respondent  
23 Schmerman in getting money from her account and began to send emails to United Planners. (Tr.  
24 208-209:23-7)

25          75.     Due to the difficulties Ms. Aiken was experiencing in dealing with Respondent  
26 Schmerman who was delaying payments to her, she contacted Charles Schwab's offices because she  
27 thought something was wrong. (Tr. 209:21-25)

28          76.     At that point, Respondent Schmerman had not provided her with copies of any

1 statements to show what her outstanding balance was. (Tr. 210:1-3)

2 77. According to Ms. Aiken, she received some interest payments or distributions from  
3 Respondent Schmerman. However, after contacting Charles Schwab to find out the balance of her  
4 account in November or December 2009, Ms. Aiken was told that there was no money in the account.  
5 (Tr. 207-208:6-4)

6 78. Ms. Aiken reviewed documentation contained in a letter from Charles Schwab to the  
7 Division which stated that although an account had been opened in her name in 2008, it had not been  
8 funded and thus there were no statements generated for the account. (Tr. 211:7-19)

9 79. Ms. Aiken had no idea previously that her account at Charles Schwab had not been  
10 funded with the funds which had been gifted to her by her mother and which she thought were being  
11 managed by Respondent Schmerman. (Tr. 212:17-25)

12 80. By the beginning of 2010, Ms. Aiken testified that Respondent Schmerman had  
13 transferred \$105,000.00 to her leaving a balance of approximately \$12,000.00 which was  
14 subsequently paid to her by United Planners. (Tr. 214:22-24)

15 81. Ms. Aiken further testified that she had never loaned or made a gift of any funds to  
16 Respondent Schmerman and she felt deceived by him. (Tr. 216-217:15-5)

17 82. Ms. Aiken believed that Respondent Schmerman had been dishonest in how he  
18 handled her financial affairs and how he handled the funds which had been transferred to her from  
19 her mother. (Tr. 217:6-11)

20 83. As far as Ms. Aiken could recall, she never saw any statements from any brokerage  
21 houses and only received typewritten statements which had been prepared on Diversified stationary.  
22 (Tr. 218-219:16-3)

23 84. Gregory Thomsen, a special investigator with the Division, was involved in the  
24 investigation of Respondent Schmerman and was qualified as a technology expert based on his  
25 background and training with the United States Army.

26 85. According to Mr. Thomsen, based on the Division's investigation, Respondent  
27 Schmerman was married during the entire timeframe of Schmerman's activities in the securities  
28 industry from January 2005 through September 2013. (Tr. 156:14-19)

1           86.     According to Commission records, Respondent Schmerman was a licensed securities  
2 salesman from November 6, 1986, to March 13, 2008 and May 15, 2008 to March 10, 2010. The  
3 Commission records also indicate that from June 3, 2008 to March 10, 2010 Mr. Schmerman was  
4 also licensed with the Commission as an IAR with United Planners. From March 11, 2010, to  
5 August 15, 2012, Respondent Schmerman was not registered with the Commission as a securities  
6 salesman or dealer pursuant to Article 9 of the Act and he had not made a notice filing or obtained a  
7 license with the Commission as an IA or IAR pursuant to Article 4 of the IM Act. (Tr. 158:1-16)(Ex.  
8 S-1a)

9           87.     Mr. Thomsen stated that although Respondent Schmerman filed a U4 application on  
10 May 28, 2010, for licensure as an IAR with Diversified Financial Planners, LLC (“Diversified,  
11 LLC”), that application is still pending. Additionally, according to Commission records, at no time  
12 from November 6, 1986 through August 5, 2012, was Respondent Schmerman registered as a  
13 licensed IA. (Tr. 158-159:17-3)

14           88.     Commission records further indicate that from September 1, 1995 through August 15,  
15 2012, none of the Diversified entities had filed with the Commission a notice pursuant to A.R.S. §  
16 44-1850 of the Act or Article 12 of the IM Act, A.R.S. § 44-3321. Additionally, none of the  
17 Diversified entities had registered securities with the Commission by description pursuant to Article 6  
18 of the Act, A.R.S. § 44-1871, or by qualification pursuant to Article 7 of the Act, A.R.S. § 44-1891,  
19 had registered with the Commission as a dealer pursuant to Article 9 of the Act, A.R.S. § 44-1941,  
20 and had not made a notice filing or licensed with the Commission as an IA pursuant to Article 4 of  
21 the IM Act, A.R.S. § 44-3151. Diversified, LLC, filed a Form ADV application with the  
22 Commission on May 26, 2010, requesting licensure as an IA in Arizona, and that application is still  
23 pending. (Tr. 159-160:9-8)(Ex. S-1b)

24           89.     Mr. Thomsen testified further that none of the Diversified entities was ever registered  
25 or licensed as an IA between September 1995 and August 15, 2012. (Tr. 160:9-16)

26           90.     According to records from the Arizona Secretary of State’s office, the trade name for  
27 Diversified was owned by Respondent Schmerman from June 4, 1986, and was registered on August  
28 6, 2009, as a financial advisory firm. (Ex. S-2a)

1           91.     According to additional records of the Arizona Secretary of State, Diversified was  
2 involved in the tax preparation and portfolio management business beginning in Arizona on February  
3 1, 1986. (Ex. S-2b).

4           92.     In a letter dated March 29, 2010, a Division attorney wrote to the Vice President of  
5 Compliance with United Planners to seek confirmation that United Planners had discharged Mr.  
6 Schmerman from the firm on March 10, 2010, because he had commingled client assets in his  
7 checking account. (Ex. S-7)

8           93.     The Division's investigator, Mr. Thomsen, further testified that Respondent  
9 Schmerman was neither associated nor affiliated with any broker dealer or any investment advisory  
10 firm after March 10, 2010. (Tr. 169:3-10)

11          94.     Mr. Thomsen stated that in a letter dated February 5, 2002, Respondent Schmerman,  
12 on Diversified stationary, represented that he was a registered IA to a client by the name of Mrs. Pat  
13 Olvey. However, in February 2002, Respondent Schmerman was not registered as an IA. (Tr. 174-  
14 175:21-6)

15          95.     Respondent Schmerman stated in his letter to Mrs. Olvey that his annual fee for his  
16 investment advisory services would be 1.5%. (Ex. S-23b)

17          96.     Investigator Thomsen testified that he accessed the Central Registration Depository  
18 ("CRD") which is operated by the Financial Industry Regulatory Authority ("FINRA"), a self-  
19 regulatory organization ("SRO"), and ran a background and registration status check on Respondent  
20 Schmerman. (Tr. 223:5-8)(Ex. S-72a, 72b, and 72c)

21          97.     Mr. Thomsen stated that, according to FINRA's records, a Uniform Application for  
22 Investment Advisor Registration ("Form ADV") was not filed by Respondent Schmerman. (Tr.  
23 226:9-12)

24          98.     Investment advisors are required to provide a copy of a Form ADV to inform clients  
25 about fees, types of investments and how the advisor will handle a client's investments.

26          99.     According to the Division's investigator, some of Respondent Schmerman's clients  
27 had received a version of the Form ADV, but this document had not been filed with FINRA. (Tr.  
28 226:4-11)

1           100. Mr. Thomsen testified that according to the Registration's Summary filed with  
2 FINRA, Respondent Schmerman's latest registration filed for Diversified on May 28, 2010, was  
3 deficient. (Tr. 227:1-16)

4           101. According to Respondent's registration with United Planners, Respondent Schmerman  
5 was employed from May 15, 2008 through March 10, 2010. (Tr. 228:17-21)

6           102. Respondent Schmerman's registration summary states further that he had been  
7 discharged by United Planners because "the firm determined after an investigation, that Mr.  
8 Schmerman commingled client assets with his checking account." (Ex. S-72B)

9           103. According to the FINRA registration summary, Respondent Schmerman's salesman  
10 designation and IAR designation were both terminated by United Planners. (Ex. S-72B)

11           104. According to Respondent Schmerman's Registration Summary, he was employed with  
12 MSC from March 31, 1999 to March 12, 2008, as a salesman and terminated his employment for  
13 voluntary reasons. During Respondent Schmerman's employment with this firm and the other firms  
14 he had been registered with, he had not been registered as a licensed IA. (Ex. S-72B)(Tr. 231:18-22)

15           105. According to the Commission's records, Respondent Schmerman filed a form U4  
16 application on May 28, 2010, to be licensed as an IAR with Diversified, LLC and that application is  
17 still pending. (Ex. S-1a)

18           106. Diversified, LLC filed a Form ADV with the Commission on May 26, 2010, and  
19 requested to be licensed as an IA in Arizona and that application is also still pending. (Ex. S-1b)

20           107. According to the Division's investigator, Respondent Schmerman was only licensed as  
21 an IAR with United Planners for a brief time.<sup>4</sup> (Tr. 233:16-21)

22           108. Mr. Thomsen testified that additional information concerning Respondent  
23 Schmerman's registration was also obtained from the CRD and included information of an allegation  
24 by Elizabeth Aiken concerning the comingling of client assets with Respondent Schmerman's  
25 business bank account. (Tr. 236-238)

26           109. Based on CRD Records, when Respondent Schmerman failed to make distributions  
27

28 <sup>4</sup> From May 15, 2008 to March 10, 2010.

1 when requested in 2010 to Ms. Aiken, she contacted the brokerage firm, United Planners, directly and  
2 learned that Respondent Schmerman had never funded her brokerage account. (Ex. S-72c)

3 110. According to information from the CRD, Respondent Schmerman had returned all of  
4 the investment funds to the Aikens, but he failed to amend his Form U4 to disclose material facts  
5 including tax and judgment liens against him. Additionally, when he completed his member firm's  
6 annual compliance questionnaire, he had "responded 'no' to a question which asked, if in the past  
7 year have any judgments or tax liens been entered against you?" (Ex. S-72c)

8 111. The CRD record concerning Respondent Schmerman states that on August 15, 2011,  
9 Respondent Schmerman consented to a permanent bar from association with any FINRA member in  
10 any capacity. (Ex. S-72C)

11 112. During the course of the Division's investigation, Mr. Thomsen learned that  
12 Respondent Schmerman had been involved with Charles and Patricia Beauvais, who were clients.  
13 Mr. Schmerman dealt with them regarding a trust which they had on or about December 17, 1997,  
14 providing them with investment advisory services, when neither Diversified nor Respondent  
15 Schmerman were registered as either an IA or IAR. (Tr. 244-252)

16 113. The Division also investigated Respondent Schmerman with respect to his dealings  
17 involving another investor, Sandra Robinson. This involved transactions which she had with him  
18 concerning approximately \$377,000 which she had received from a life insurance policy after her  
19 husband's death. (Tr. 252-253)

20 114. According to Mr. Thomsen, Mrs. Robinson had wanted Respondent Schmerman to  
21 invest these funds in a safe investment such as a money market investment, but not in the stock  
22 market. Mrs. Robinson preferred a money market investment so that she could receive a monthly  
23 distribution of about \$2,275.00. (Tr. 253:1- 18)(Ex. S-30)

24 115. The Division contacted an attorney retained by Mrs. Robinson who filed a claim  
25 against Respondent Schmerman and MSC and LPL Financial, LLC, both FINRA registered broker  
26 dealers, with which Respondent Schmerman was affiliated. Mrs. Robinson's claim demanded  
27 arbitration with the Respondents and was filed on September 22, 2011. (Ex. S-30)

28 116. Mrs. Robinson's claim, states that she did not wish to jeopardize the funds which she

1 would have to live on for the rest of her life, and Respondent Schmerman assured her that he would  
2 place the funds in an "institutional account." Subsequently, she never received any statements or  
3 documents related to her investment. Although she received some monthly payments, they were  
4 irregular and varying in amount, and on occasion came from Respondent Schmerman's own bank  
5 account with Wells Fargo. (Ex S-30)

6 117. A copy of a check dated January 3, 2006, from Mrs. Robinson to Diversified in the  
7 amount of \$373,390.00 contains the following memo notation "transfer into investment account."  
8 (Ex. S-30)

9 118. According to Mr. Thomsen, based on his interview with Mrs. Robinson and her  
10 documentation, there was no evidence that Respondent Schmerman, while working as a securities  
11 salesman for MSC, actually invested her funds. (Tr. 258:14-22)

12 119. Investigator Thomsen testified about another Schmerman investor, Bernice Elson, who  
13 had been involved in an investment transaction on or about June 30, 2006, when Respondent  
14 Schmerman sent her a letter on Diversified's stationary representing himself to be a licensed IA. She  
15 provided him with \$125,000.00 for investment purposes in return for a 1% investment management  
16 fee thinking that her funds would be deposited into a Charles Schwab account. However, she never  
17 received proof that the funds were deposited into a Charles Schwab account. (Tr. 259-261)

18 120. Mr. Thomsen stated further that Mrs. Elson later contacted Charles Schwab directly  
19 and learned that she did not have an account in her name. (Tr. 261-262)

20 121. Another investor contacted by Mr. Thomsen was Ms. Ann Draganich, Dr. Vrla's  
21 sister. She dealt with Respondent Schmerman because he had handled her father's accounts and  
22 subsequently hers and her siblings. (Tr. 262-263:22-10)

23 122. Mr. Thomsen stated that Respondent Schmerman charged Ms. Draganich investment  
24 advisory fees or management fees for his services, and in January 2011 she wrote him a check for  
25 \$1,565.00. (Tr. 263:11-23)

26 123. Mr. Thomsen testified that Ms. Draganich told him that Charles Schwab had sent her  
27 checks that she had not requested. After receiving them, she deposited them and wrote corresponding  
28 checks for the same amount to Respondent Schmerman because Respondent Schmerman had told her

1 that it was a new process they had to follow for him to receive his fee payments for advisory services.  
2 (Tr. 263-264:22-11)

3 124. During this period of time, Respondent Schmerman was not licensed or registered as  
4 either a salesman or an IAR and he did not inform Ms. Draganich of his status. (Tr. 264:12-17)

5 125. According to Mr. Thomsen, Ms. Draganich provided the Division with a copy of two  
6 checks that she sent Respondent Schmerman for his investment advisory services using funds derived  
7 from two checks received from Charles Schwab after she was billed by Diversified. (Tr. 265-266:15-  
8 3)(Ex. S-32)

9 126. In a letter to the Division, Ms. Draganich indicated that she spoke to a Charles Schwab  
10 representative and learned that they did not charge advisory fees and that Respondent Schmerman  
11 was not allowed to handle her account. She stated that the Charles Schwab representative told her  
12 that someone with a 602 area code (where Mr. Schmerman's office was located) claimed to be her  
13 and requested both checks be drawn on her account. She further indicated to the Division that the  
14 area codes for her phones was either 773 or 303. (Tr. 266)(Ex. S-32)

15 127. Ms. Draganich provided the Division with a copy of a fee statement from Diversified  
16 upon which Respondent Schmerman's name appeared. She was charged for advisory services  
17 rendered purportedly in 2010 and was to follow the directions on a post-it note attached to the  
18 statement which told her to deposit Charles Schwab checks and to send the respective amounts due  
19 on her personal checks to him. (Tr. 268)(Ex. S-32)

20 128. During the Division's investigation, Mr. Thomsen also received email information  
21 from Ms. Alison Levine, whose parents had been clients of Respondent Schmerman. Ms. Levine told  
22 the Division's investigator that a number of unauthorized withdrawals were made for advisory fees  
23 from her parents' account with Charles Schwab by Respondent Schmerman, totaling \$30,525.00,  
24 even though he had been removed from their account in April 2010. (Tr. 269)(Ex. S-33a)

25 129. Ms. Levine also described an itemized invoice for purported investment advisory  
26 services to an entity known as the Levine Limited Partnership which her parents owned or controlled.  
27 (Tr. 273:13-19)

28 130. The billing dates set forth on this invoice covered a period of time from August 12,

1 2008 through June 30, 2011, which exceeded the date of March 10, 2010, after which Respondent  
2 Schmerman was neither associated with any broker dealer nor was he an IAR. (Tr. 274:10-19)

3 131. Mr. Thomsen spoke with another client of Respondent Schmerman's, Dick Witter,  
4 who told him about his relationship with Respondent Schmerman. He had been his IA for  
5 approximately three (3) years when, in late 2011, Respondent Schmerman phoned him and let him  
6 know that he would be receiving a distribution check from Charles Schwab. (Tr. 274-275:20-15)

7 132. Respondent Schmerman told Mr. Witter to deposit the check into his account and to  
8 write a check to Respondent Schmerman to pay for advisory services. After Mr. Witter received the  
9 check from Charles Schwab in the amount of \$3,415 he wrote a check to Diversified for a like  
10 amount as he was told to do by Respondent Schmerman. (Tr. 275-276:17-16)

11 133. Mr. Thomsen stated that the Division's investigation of Respondent Schmerman also  
12 involved Scott and Shirley Stowe. According to Mrs. Stowe, in 2005 she gave Respondent  
13 Schmerman \$150,000.00 for an investment which was to be deposited into a Charles Schwab  
14 account. As of March 31, 2006, the total account value was \$38,482.39, but there was no indication  
15 that the full \$150,000.00 was actually deposited into the Charles Schwab account. (Tr. 277-280)(Ex.  
16 S-35)

17 134. According to Mr. Thomsen, the Division also investigated transactions between  
18 Respondent Schmerman and Diversified with Peter Kallgren.<sup>5</sup>

19 135. Peter Kallgren's brother, David Kallgren, related in an email to a Division investigator  
20 that his brother Peter sold property on November 9, 2005, for \$255,185.97 and deposited the funds  
21 into his credit union account. On November 18, 2005, Peter Kallgren withdrew \$218,000.00 and sent  
22 \$218,000.00 to Diversified. Subsequently, David Kallgren received a letter from Diversified dated  
23 November 5, 2010, which stated that his brother's account had \$125,418.52 in a money market  
24 account and that a partial payment between \$70,000.00 and \$100,000.00 would be sent to him on or  
25 about November 22, 2010, with the balance to be paid shortly thereafter. Mr. Kallgren was unaware  
26 of what happened to the remaining balance of the funds for the property his brother sold in 2005 and  
27

28 <sup>5</sup> Peter Kallgren died on October 15, 2008.

1 could find no statements or other records regarding the balance of the funds. (Ex. S-36)

2 136. Additionally, the Division submitted evidence consisting of copies of two promissory  
3 notes where Respondent Schmerman borrowed substantial sums of money from his clients and also  
4 copies of a lawsuit by one of Respondent Schmerman's clients that were collected during the course  
5 of the Division's investigation. (Ex. S-37)

6 137. With respect to loans from the clients to Respondent Schmerman, neither MSC nor  
7 United Planners approved Respondent Schmerman borrowing money from his clients.

8 138. Mr. Thomsen testified that in an interview of Richard Rubin, a client of Respondent  
9 Schmerman's, Mr. Rubin told him that he had been a client for at least twenty (20) years and had  
10 made loans to Mr. Schmerman numerous times for in excess of \$200,000.00, and at the time  
11 Respondent Schmerman owed him \$90,000.00. (Tr. 293-294)

12 139. Mr. Thomsen further stated that neither MSC nor United Planners had approved Mr.  
13 Schmerman borrowing any money from his client, Mr. Rubin. (Tr. 294:15-19)

14 140. The Division's investigator testified further that Charles Schwab provided the  
15 Division with a CD which contained the list of accounts that were in the name and/or control of  
16 Respondent Schmerman during the relevant timeframe. (Tr. 295-296:14-5)

17 141. According to information based on the CD and the accompanying documentation, they  
18 described the date upon which Respondent Schmerman was removed or "delinked" from the accounts  
19 listed by Charles Schwab. (Tr. 297:1-8)

20 142. The MSC compliance manual, which any representative of the company would have,  
21 states that representatives should avoid entering into financial transactions with customers to avoid  
22 potential conflicts of interests and describes prohibited practices such as lending money to or  
23 borrowing money from a customer. (Ex. S-18)

24 143. The MSC manual lists among its prohibited financial practices the commingling funds  
25 or securities with those of customers, and the borrowing of money or securities from any client.  
26 These practices are strictly prohibited by the brokerage. (Ex. S-18)

27 144. Mr. Thomsen further stated that, after reviewing the Charles Schwab audio files, he  
28 had found that Respondent Schmerman's audio signature could be identified with certain recordings

1 made by Charles Schwab of an individual purporting to be Dr. Rolf Vrla. (Tr. 310:18-24)

2 145. Mr. Sean Callahan, a forensic accountant for the Division, qualified as an expert  
3 witness and testified concerning the Division's investigation of the Respondents.

4 146. Mr. Callahan testified that he reviewed financial and nonfinancial documents during  
5 his investigation utilizing bank statements which detailed deposits, checks, wire transfers and debit  
6 card activity. (Tr. 315:5-20)

7 147. Mr. Callahan stated that the documents he reviewed were obtained by subpoena from  
8 banks such as USBank, Wells Fargo and Sun West Federal Credit Union ("Sun West") along with  
9 transactional information from Charles Schwab and MSC. (Tr. 315-316:23-6)

10 148. Based on Mr. Callahan's analysis of a trust in the name of Charles and Patricia  
11 Beauvais connected to an account held by the Beauvais' at Sun West, Mr. Callahan was able to  
12 identify Mr. Schmerman's signature which added himself as a signer on the account approximately a  
13 week after Mrs. Beauvais passed away on July 22, 2007. This was long after Mr. Beauvais' death on  
14 April 30, 1996.<sup>6</sup>

15 149. According to the terms of the Beauvais' trust, if neither Mr. nor Mrs. Beauvais could  
16 act as the trustee, Respondent Schmerman was named as the sole trustee as first successor trustee.  
17 This was according to an amendment of the trust dated July 5, 2005, and signed by Mrs. Beauvais as  
18 trustee.

19 150. As Mr. Callahan continued his investigation, he found a transaction for the sale of a  
20 residence owned by either Mrs. Beauvais or the trust which took place on May 20, 2009, according to  
21 the Settlement Statement. The house sold for \$399,000 and the document concluding the sale by the  
22 successor trustee was signed by Respondent Schmerman as the trustee. The final net balance due to  
23 the seller was \$368,645.17 and these funds were deposited into the Beauvais' Sun West account  
24 where, in 2009, Respondent Schmerman was the only signer on the account since Mrs. Beauvais had  
25 been dead for two years.

26

27 <sup>6</sup> Mr. Callahan was able to identify Respondent Schmerman's signature from reviewing other documents with his  
28 signature. Mr. Schmerman signed trust documents as the trustee and he was named a beneficiary of the trust after Mrs.  
Beauvais' death.

1           151. A schedule attached to the trust actually lists out the individuals that the trust was to  
2 pay out upon Mrs. Beauvais' death and Respondent Schmerman's name was not listed on that  
3 schedule.

4           152. Mr. Callahan testified that he created a summary of receipts and disbursements for  
5 Diversified for the period January 1, 2005 to April 30, 2011. (Tr. 331:7-20)(Ex. S-55)

6           153. Mr. Callahan's analysis of Diversified's cash flow from January 1, 2005, to April 30,  
7 2011, indicated that Respondent Schmerman's bank account at Wells Fargo in that time frame had  
8 deposits of \$5,025,495.00 with a like amount disbursed. (Ex. S-55)

9           154. Approximately 82% of all of the funds came from either investors or what Mr.  
10 Callahan termed were "individuals and trusts".

11           155. According to Mr. Callahan's analysis, out of the \$5,025,495.00 only \$48,953.00 or 1%  
12 was disbursed in what Mr. Callahan termed "investing activity." (Tr. 336:1-7)

13           156. Mr. Callahan's analysis of the disbursements from the Diversified account revealed  
14 that between withdrawals and transfers or payments to himself, Respondent Schmerman received in  
15 excess of \$3.2 million dollars or approximately 65% of the funds that were received by Diversified.  
16 (Tr. 336-337:11-17)

17           157. Mr. Callahan further testified that although investors were repaid \$695,424.00 or  
18 13.8% of the monies received, the investors were being paid by Mr. Schmerman using other  
19 investors' money. (Tr. 337:2-5)

20           158. Further testifying, Mr. Callahan stated that, in one instance, cash from the Beauvais'  
21 trust at Sun West controlled by Mr. Schmerman was deposited in the form of a \$191,420 cashier's  
22 check into Mr. Schmerman's bank account. (Tr. 345:3-18)

23           159. Mr. Callahan prepared a summary of receipts and disbursements for the Beauvais trust  
24 controlled by Respondent Schmerman after Mrs. Beauvais died covering a period of time December  
25 1, 2006 to April 30, 2011, and it showed total deposits of \$659,714.00 of which the proceeds from the  
26 sale of the home, \$368,645.00, constituted 55.9% of the total deposits. (Ex. S-56)

27           160. The second largest area of receipts for the Beauvais' trust was from investing activity  
28 totaling \$233,800.00 or 35.4% of the receipts which came from proceeds from Charles Schwab after

1 assets were sold and then transferred to the Sun West account. (Tr. 348-349:23-12)

2 161. According to Mr. Callahan, Respondent Schmerman and his company Diversified  
3 were the largest beneficiaries of the trust receiving almost 77% of the cash or approximately  
4 \$506,000.00. (Tr. 349:13-23)

5 162. Mr. Callahan stated that in August 2007, \$50,000.00 from the Beauvais' Charles  
6 Schwab account was deposited into the trust account at Sun West. Subsequently, Mr. Schmerman had  
7 a cashier's check issued to either himself or Diversified and deposited the funds into his personal  
8 account. (Tr. 352:9-15)

9 163. Mr. Callahan also traced additional funds going from the Beauvais' Charles Schwab  
10 account which were deposited into the Sun West account after which Mr. Schmerman then wrote  
11 himself a check payable to Diversified in September 2007.

12 164. Mr. Callahan stated that, in essence, the entire balance of the monies from the sale of  
13 the Beauvais' residence were funneled through the Beauvais' trust to either Mr. Schmerman directly  
14 or to Diversified. (Tr. 358:6-23)

15 165. Mr. Callahan further testified that of \$373,000 that Mrs. Sandra Robinson provided to  
16 Mr. Schmerman on January 4, 2006, only \$25,000 of that sum was invested with Charles Schwab, but  
17 not in her personal account. This sum was deposited into an industrial or institutional account for  
18 Respondent Schmerman's master brokerage account. (Tr. 371:5-12)

19 166. Based on his analysis, Mr. Callahan concluded that Respondent Schmerman utilized  
20 his clients' funds for his own personal benefit. (Tr. 393:4-7)

21 167. Mr. Callahan stated that Respondent Schmerman's typical method of misusing his  
22 clients' funds would be to deposit monies from his clients into Diversified's account and then he  
23 would transfer the funds to his personal account. (Tr. 394:5-14)

24 168. According to Mr. Callahan, many of these transactions were simply cash withdrawals  
25 by Respondent Schmerman. (Tr. 394:15-17)

26 169. Based on Mr. Callahan's analysis of the funds received from the sale of the Beauvais  
27 residence, after the funds were deposited into the Sun West account, these funds, \$368,645.17 were  
28 utilized for Respondent Schmerman's personal benefit. (Tr. 395:18-24)

1           170. Mr. Callahan testified that investor funds were repeatedly deposited into the  
2 Diversified account controlled by Respondent Schmerman, and none of these funds were used to  
3 purchase securities. (Tr. 396:1-13)

4           171. Mr. Callahan repeatedly described numerous instances in which funds entrusted to  
5 Respondent Schmerman and deposited into the Diversified account were then either withdrawn in the  
6 form of cash or misused by Respondent Schmerman for purposes other than investments for his  
7 clients. (Tr. 398:1-18)

8           172. Mr. Callahan further described how \$162,000.00 was given to Respondent  
9 Schmerman on July 22, 2005 for investment purposes, but five days later the funds were taken out in  
10 the form of a cashier's check payable to "The Estate of Ruth Gunston" to repay Respondent  
11 Schmerman's debt to what was termed the Gunston Estate. (Tr. 399-400:24-8)

12           173. Mr. Callahan testified that on a number of occasions, Respondent Schmerman had  
13 cashier's checks made out to other entities or individuals and then deposited the checks into his own  
14 personal account. (Tr. 401:3-10)

15           174. Mr. Callahan testified further about a deposit of \$100,000.00 of an investor's funds  
16 (Burritt Steward) into the Diversified account on May 20, 2010. Subsequently, in a period of 8 days,  
17 the \$100,000.00 was reduced to \$93.86 after Respondent Schmerman paid out the balance of the  
18 funds in cashier's checks to other investors and took the remaining \$26,000.00 in cash withdrawals.  
19 (Tr. 402:1-13)

20           175. Mr. Callahan stated that of Mr. Steward's \$100,000.00 deposited into the Diversified  
21 account, none of the funds were utilized for purchasing stocks or investments for his benefit. (Tr.  
22 402:14-17)

23           176. Mr. Callahan reviewed the fate of Peter Kallgren's \$218,000.00 investment deposit on  
24 November 22, 2005, into the Diversified account. Mr. Callahan stated that none Mr. Kallgren's  
25 funds were utilized for the purchase of stocks or securities or any investments to benefit Mr.  
26 Kallgren, except for the possibility of a Charles Schwab payment of \$20,000.00 with a cashier's  
27 check. However, Mr. Callahan testified that these funds may have gone into Diversified's main  
28 account. Of the remaining funds, there were four transfers to Respondent Schmerman's personal

1 account and numerous cash withdrawals on the account which only Mr. Schmerman had access to.  
2 (Tr. 402-404)(Ex. S-71c)

3 177. In the case of another investor, Bernice Elson, on July 28, 2006, \$233,103.97 was  
4 deposited into the Diversified account controlled by Mr. Schmerman with a subsequent deposit on  
5 September 30, 2008, of \$125,000 for Ms. Elson. By the end of August 2006, the remaining amount  
6 of her initial investment was approximately \$75,000 with very little of the funds being used for  
7 investment purposes for securities or for Ms. Elson's benefit. The vast majority of these funds were  
8 utilized in the form of cash withdrawals or transfers to Respondent Schmerman's personal account.  
9 All told, according to Mr. Callahan, only approximately \$61,000.00 of the more than \$350,000.00  
10 deposited into the Diversified account were utilized for Ms. Elson's benefit. (Tr. 404-407)

11 178. Mr. Callahan further testified that in an analysis prepared for Diversified's account for  
12 January 2006, it showed a significant deposit of \$373,390.00 for Sandra Robinson, an investor.  
13 However, during the month, there were minimal investments on behalf of Mrs. Robinson and the  
14 funds were not used for her benefit. According to Mr. Callahan, bank checks to other investors and  
15 cash withdrawals for Mr. Schmerman made up the balance of the funds utilized from the Robinson  
16 deposit. (Tr. 408-410)(Ex. S-71e)

17 179. Mr. Callahan also performed an analysis on Respondent Schmerman's personal  
18 account during the month of January 2006 and after a transfer of \$54,000.00 from the Diversified  
19 account, Mr. Schmerman immediately wrote a check for \$54,333.00 to another individual.  
20 Additionally, after depositing \$40,000.00 from the business account he immediately wrote a check to  
21 another investor, Eldon Diamond for \$30,239.00. (Tr. 411-412)(Ex. S-71e)

22 180. Mr. Callahan further testified that on August 17, 2005, an investor, Scott Stowe,  
23 provided Respondent Schmerman with \$150,000.00 for investment purposes. These funds were  
24 deposited into the Diversified account and during the following month, the balance of the funds were  
25 either withdrawn or transferred to Respondent Schmerman's personal account. The funds were not  
26 used for investment purposes or for Mr. and Mrs. Stowe's benefit. (Tr. 414:16-19)

27 181. Mr. Callahan prepared a six page restitution document for Respondent Schmerman's  
28 investors and also included a section addressing the issue of fees collected for investment advisory

1 services after Mr. Schmerman was no longer licensed as an IAR with United Planners.<sup>7</sup>

2 182. Mr. Callahan concluded that Respondent Schmerman's actions were similar to those  
3 of a Ponzi Scheme in that Mr. Schmerman used later investors' funds to pay off the earlier investors.  
4 (Tr. 432:16-24)

5 183. Mr. Callahan further testified that after a slight revision to the restitution worksheet  
6 based on recalculating certain investor funds as of the date of the hearing, he determined that  
7 restitution in the amount of \$3,009,173.32 was owed to investors. (Ex. S-58b)

8 184. Based on the record, and the overwhelming preponderance of the evidence against  
9 Respondents, we find that a multiplicity of violations of both the Act and the IM Act have been  
10 established during these proceedings. Additionally, there is abundant evidence that fraud was  
11 committed by Respondent Schmerman in his dealings with his clients over a period of years in that he  
12 committed multiple violations of the anti-fraud provisions of the Act, which also carried over to his  
13 actions as an IAR and during the period when he no longer was a licensed IAR. Accordingly,  
14 Respondents should be ordered to cease and desist, and Respondents should make restitution of the  
15 amount established by the Division's evidence and also pay an administrative penalty. Further, based  
16 on the aforementioned violations of the Act and the IM Act, Respondent Schmerman's securities  
17 salesman's license and IAR license should be revoked and any pending application by Respondent  
18 Schmerman should be denied. Because there was no evidence to the contrary, the marital community  
19 should also be held liable for these violations.

#### 20 CONCLUSIONS OF LAW

21 1. The Commission has jurisdiction of this matter pursuant to Article XV of the Arizona  
22 Constitution and A.R.S. §§ 44-1801, et seq and 44-3101, et seq.

23 2. Respondent Richard M. Schmerman violated A.R.S. §§ 44-1962(A)(10) and 44-  
24 3201(A)(13) by engaging in dishonest and unethical practices in the securities industry.

25 3. Respondent Schmerman A.R.S. §§ 44-1962(A)(12) and 44-3201(A)(14) by engaging  
26 in dishonest and unethical practices in business or financial matters.

27  
28 <sup>7</sup> This was the period from March 11, 2010 through August 15, 2012.



1 IT IS FURTHER ORDERED that the license of Richard M. Schmerman as an Investment  
2 Advisor Representative is hereby revoked pursuant to A.R.S. § 44-3201.

3 IT IS FURTHER ORDERED that pursuant to A.R.S. § § 44-3201 and 44-3202, the  
4 application of Richard M. Schmerman for a license as an Investment Advisor Representative is  
5 hereby denied.

6 IT IS FURTHER ORDERED that pursuant to the authority granted to the Commission under  
7 A.R.S. §§ 44-2036, 44-3201 and 44-3296, Richard M. Schmerman and Amy Schmerman shall pay  
8 jointly and severally as and for administrative penalties for the violations of the Act and the IM Act  
9 the sum of \$200,000. The payment obligation for the administrative penalties shall be subordinate to  
10 any restitution and shall become immediately due and payable only after restitution payments have  
11 been paid in full or upon Respondents' default with respect to Respondents' restitution obligations.

12 IT IS FURTHER ORDERED that pursuant to the authority granted to the Commission under  
13 A.R.S. §§ 44-2036, 44-3201(B) and 44-3296, that Respondents Richard M. Schmerman and Amy  
14 Schmerman jointly and severally shall pay the administrative penalties ordered hereinabove in the  
15 amount of \$200,000.00, payable by either cashier's check or money order payable to the "State of  
16 Arizona" and presented to the Arizona Corporation Commission for deposit in the general fund for  
17 the State of Arizona.

18 IT IS FURTHER ORDERED that if Respondents Richard M. Schmerman and Amy  
19 Schmerman fail to pay the administrative penalties hereinabove, any outstanding balance plus interest  
20 at the rate of the lessor of 10 percent per annum or the rate per annum that is equal to one percent  
21 plus the prime rate as published by the Board of Governors of the Federal Reserve System of  
22 Statistical Release H.15 or any publication that may supercede on the date that the judgment is  
23 entered may be deemed in default and shall be immediately due and payable, without further notice.

24 IT IS FURTHER ORDERED that pursuant to the authority granted to the Commission under  
25 A.R.S. §§ 44-2032, 44-3201 and 44-3292, Respondents Richard M. Schmerman and Amy  
26 Schmerman shall jointly and severally make restitution in the amount of \$3,009,173.32 pursuant to  
27 A.A.C. R14-4-308, subject to any legal set-offs by the Respondents and confirmed by the Director of  
28 Securities with said restitution to be made within 60 days of the effective date of this Decision.

1 IT IS FURTHER ORDERED that the restitution ordered hereinabove shall bear interest at the  
2 rate of the lesser of 10 percent per annum or at a rate per annum that is equal to one percent plus the  
3 prime rate as published by the Board of Governors of the Federal Reserve System of Statistical  
4 Release H.15 or any publication that may supersede on the date that the judgment is entered.

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

7 IT IS FURTHER ORDERED that pursuant to the authority granted to the Commission under  
8 A.R.S. §§ 44-2031(C) and 44-3291(C) the marital community of Respondents Richard M.  
9 Schmerman and Amy Schmerman shall be jointly and separately liable to the extent allowable  
10 pursuant A.R.S. § 25-215 for restitution in the amount of \$3,009,173.32 and administrative penalties  
11 in the amount of \$200,000.00.

12 IT IS FURTHER ORDERED that default shall render Respondents Richard M. Schmerman  
13 and Amy Schmerman liable to the Commission for its costs of collection and interest at the rate of the  
14 lesser of 10% per annum or at a rate per annum that is equal to 1% plus the prime rate as published  
15 by the Board of Governors of the Federal Reserve System of Statistical Release H.15 or any  
16 publication that may supercede on the date that the judgment is entered.

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

25 IT IS FURTHER ORDERED that if Respondents Richard M. Schmerman and Amy  
26 Schmerman fail to comply with this Order, the Commission may bring further legal proceedings  
27 against Respondent(s) including application to the Superior Court for an order of contempt.

28 IT IS FURTHER ORDERED that pursuant to A.R.S. § 44-1974, upon application, the

1 Commission may grant rehearing of this Order. The application must be received by the Commission  
2 at its offices within twenty (20) calendar days after entry of this Order and, unless otherwise ordered,  
3 filing an application for rehearing does not stay this Order. If the Commission does not grant  
4 rehearing within twenty (20) calendar days of the filing of the application, the application is  
5 considered to be denied. No additional notices will be given of such denial.

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

7 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.  
8  
9

10 CHAIRMAN \_\_\_\_\_ COMMISSIONER

11  
12 COMMISSIONER \_\_\_\_\_ COMMISSIONER \_\_\_\_\_ COMMISSIONER

13  
14 IN WITNESS WHEREOF, I, JODI JERICH, Executive  
15 Director of the Arizona Corporation Commission, have  
16 hereunto set my hand and caused the official seal of the  
17 Commission to be affixed at the Capitol, in the City of Phoenix,  
18 this \_\_\_\_\_ day of \_\_\_\_\_ 2014.

19 \_\_\_\_\_  
20 JODI JERICH  
21 EXECUTIVE DIRECTOR

22 DISSENT \_\_\_\_\_

23 DISSENT \_\_\_\_\_  
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SERVICE LIST FOR:

RICHARD M. SCHMERMAN, individually and d/b/a  
Diversified Financial and/or Diversified Financial  
Planners, and Amy Schmerman, husband and wife.

DOCKET NO.:

S-20757A-10-0373

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