**BEFORE THE ARBITRAL TRIBUNAL OF THE**
**FINANCIAL INDUSTRY REGULATORY AUTHORITY**

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| **LORETTA DEHAY,**<br><br>**CLAIMANT,**<br>**v.**<br><br>**SAGEPOINT FINANCIAL, INC.**<br><br>**RESPONDENT.** | **STATEMENT OF CLAIM** |

Claimant Loretta DeHay ("Loretta," "Claimant") seeks damages in this arbitration from SagePoint Financial, Inc. ("SagePoint") regarding the unsuitable investment recommendations of its registered representative, Daniel Dillard ("Dillard").

This case arises out of Respondent's failure to make suitable recommendations to Claimant. Respondent's recommendations to Claimant led to an over concentration of alternative investments and annuities in her portfolio. This was clearly dangerous to the wellbeing of her assets. As a result, Claimant has suffered significant losses and has not reaped the benefits of investing her funds during what was a historic bull market.

Due to the notable percentage of Claimant's portfolio that was put into high commission products, Claimant believes that these recommendations were clear commission grabs by Respondent and its representative, Dillard. The recommendations do not make sense unless viewed with their commissions in mind. Such conduct is in direct violation of the trust Claimant held in Respondent and the duties owed to her. This conduct is also in violation of FINRA's rules of suitability and rules requiring brokers and broker-dealers to conduct themselves with high standards of commercial honor.

Pursuant to FINRA Rule 12213, Claimant request that this arbitration hearing be in Houston, Texas because Houston is the hearing location "closest to the customer's residence at the time of the events giving rise to the dispute..."

Due to Claimant's advanced age, she asks that this proceeding be granted expedited hearing status.

## II. THE PARTIES

### A. Claimant Loretta DeHay

Loretta is a 62-year-old attorney who lives in Pflugerville, Texas. She met Daniel Dillard through a credit union through which she banked back in 2008. She and her husband started investing through Dillard on or about that time. They trusted Dillard and Loretta ultimately followed him when he left LPL Financial for SagePoint.

Over time, Dillard advised Loretta to invest in a number of high commission, unsuitable investments. Among others, Loretta suffered losses due to Dillard's advice to purchase Vereit. She and her husband were also advised to purchase annuities with her husband's insurance and retirement assets. Dillard also advised Loretta to churn the annuity funds into new annuities in 2018. This was inappropriate. Making this sale even more clearly unsuitable is that the retirement assets were already growing on a tax-deferred basis, which is normally the primary benefit to the purchase of an annuity.

In 2018, Dillard advised Loretta to purchase $100,000 in GPB Automotive Portfolio. Had Loretta been aware of how risky this investment was, or the failures of SagePoint to adequately conduct due diligence on GPB, she would never have invested in it. Loretta is distraught with what she has learned regarding her GPB investment. Over the course of the last year, multiple lawsuits have been filed and regulatory matters initiated alleging that GPB Capital has been

engaged in wrongdoing. Most notably, former GPB Holdings operating partner, Patrick Dibre alleged that "losses occasioned by GPB were in fact caused by a very complicated and manipulative Ponzi scheme." Broker-dealers that sold GPB have also been investigated by FINRA and the SEC. State regulators have announced investigations. GPB has failed to produce audited financial statements. Loretta does not anticipate that she will receive any value out of her GPB investment and understands her investment to be worthless.

Loretta has suffered significant losses from the investment advice received from Respondent and Dillard in an amount to be determined at a hearing.

**B. Respondent SagePoint**

Respondent SagePoint (CRD# 133763) is a FINRA registered brokerage firm with its main office in Phoenix, Arizona. SagePoint does business in 53 U.S. states and territories. According to its broker check report, SagePoint has been the subject of 14 regulatory events and 11 arbitration awards. Important to this arbitration, SagePoint has repeatedly struggled with their supervisory structure. Between 2010 and 2018, in six instances, SagePoint was fined a combined amount of over $2 million for failure to reasonably supervise its registered representatives. Most recently, SagePoint was fined $300,000 in June 2020 for failing to establish and maintain a supervisory system.

**C. Non-Party Daniel Dillard**

Daniel Dillard (CRD# 4289333) has been in the financial services industry since 2000 when he passed the Series 7 and Series 66 exams. He has also passed the Series 24 and SIE exams.

Daniel Dillard was registered with Merrill Lynch, Pierce, Fenner & Smith Incorporated from December 2000 to April 2002. He was then registered with CUNA Brokerage Services, Inc. from May 2002 to July 2004. He was registered with LPL Financial LLC from July 2004 to May

2013. He was then registered with SagePoint Financial from May 2013 to April 2019. He then became registered with Union Capital Company in April 2019 until July 2019. His office was located in Austin, Texas.

In 2013, Dillard was discharged from LPL Financial for submitting altered documents regarding his commission split. As Dillard registered with Respondent SagePoint after this event, the firm was well aware of the risk it was accepting by hiring him and the importance to its clients in its supervision of him. Highlighting the significance of this event, Dillard was thereafter subject to FINRA regulatory action involving a three-month suspension and a $5,000 fine arising from the incident.

Additionally, Dillard has been subject to an IRS tax lien amounting to almost $60,000. Respondent SagePoint had every reason to supervise Dillard's sales to clients, particularly sales of high commission products given his employment, regulatory, and financial history. Instead, Respondent SagePoint benefitted financially by turning a blind eye to Dillard's actions while failing to protect their customer.

## III. JURISDICTION

This case is arbitrable pursuant to the Federal Arbitration Act and the Arbitration clauses contained in (a) the Licensing Agreement between Respondent and FINRA, (b) the NASD Code of Arbitration, including Rule 12200 of the Code, and (c) the client agreement between Claimant and Respondent.[1] Moreover, all of the arbitrability requirements are satisfied in this case. Respondent is a broker-dealer and FINRA member; and this dispute arises in connection with

[1] "[T]he NASD Code constitutes an agreement in writing under the Federal Arbitration Act, 9 USCS 2," which binds the member to submit an eligible dispute to arbitration upon a customer's demand. *Liberte Capital Group, LLC v. Capwill*, 148 Fed. Appx. 413, 416 (6th Cir. 2005) (*quoting Washington Square Secs., Inc. v. Aune*, 385 F.3d 432, 435 (4th Cir. 2004)).

Respondent's business activities. Therefore, Respondent is bound by the NASD Code to arbitrate this dispute.

## IV. LEGAL BASES UPON WHICH RELIEF CAN BE GRANTED

### A. VIOLATIONS OF FINRA RULE 2010.

Rule 2110 mandates that broker-dealers, in the conduct of their business, "observe high standards of commercial honor and just and equitable principles of trade." NASD Rule 2110. FINRA has stated that broker-dealers:

> have an obligation of fair dealing in actions under the general anti-fraud provisions of the federal securities laws. The Commission bases this obligation on the principle that when a securities dealer opens his business he is, in effect, representing that he will deal fairly with the public… Usually, any breach of the obligation of fair dealing as determined by the Commission under the anti-fraud provisions of the securities laws could be considered a violation of the Association's Rules.

IM-2310-2(d) (Fair Dealing with Customers).

Securities industry regulators have warned that violations by broker-dealers of SEC or NASD rules or regulations are inconsistent with the just and equitable principles of trade and have found that such violations also constitute violations of NASD Conduct Rule 2110. *See Alvin W. Gebhart*, Exch. Act Rel. No. 53136, 2006 SEC LEXIS 93, at *54 n.75 (2006), *rev'd and remanded in part on other grounds sub. nom Gebhart v. SEC*, 2007 U.S. App. LEXIS 27183 (9th Cir. 2007).

Ignoring FINRA and SEC rules, through their registered representatives, Respondent recommended the overconcentration of alternative investments in Claimant's portfolio. Respondent did so with an eye on commissions, but not on the suitability of the underlying allocation that was being set up in Claimant's accounts. As a direct and proximate result of Respondent's conduct, Claimant has been damaged in an amount to be determined at the hearing of this case and is entitled to compensation.

## B. VIOLATIONS OF FINRA RULE 2111: RECOMMENDING AND SELLING SECURITIES WITHOUT ADEQUATE DUE DILIGENCE AND WITHOUT A REASONABLE BASIS.

Respondent violated FINRA Rule 2111 by recommending and selling securities to Claimant without first conducting adequate due diligence and gaining a reasonable basis to make such recommendations and sales. FINRA Rule 2111 mandates that securities broker dealers:

> must have a *reasonable basis* to believe that a recommended transaction … involving a security … is suitable for the customer, based on the information obtained through the *reasonable diligence* of the member or associated person to ascertain the customer's investment profile. A customer's investment profile includes, but is not limited to, the customer's age, other investments, financial situation and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs, risk tolerance, and any other information the customer may disclose to the member or associated person in connection with such recommendation.

FINRA Rule 2111(a) (*emphasis supplied*).

FINRA has admonished its members that their suitability duties are comprised of "three main obligations: reasonable-basis suitability, customer-specific suitability, and quantitative suitability." FINRA Rule 2111.05 (Supplementary Material). It explained the three obligations as follows:

> (a) The reasonable-basis obligation requires a member or associated person to have a reasonable basis to believe, based on reasonable diligence, that the recommendation is suitable for at least *some* investors. In general, what constitutes reasonable diligence will vary depending on, among other things, the complexity of and risks associated with the security or investment strategy and the member's or associated person's familiarity with the security or investment strategy. A member's or associated person's reasonable diligence must provide the member or associated person with an understanding of the potential risks and rewards associated with the recommended security or strategy. The lack of such an understanding when recommending a security or strategy violates the suitability rule.
>
> (b) The customer-specific obligation requires that a member or associated person have a reasonable basis to believe that the recommendation is suitable for a particular customer based on that customer's investment profile, as delineated in Rule 2111(a).

> (c) Quantitative suitability requires a member or associated person who has actual or de facto control over a customer account to have a reasonable basis for believing that a series of recommended transactions, even if suitable when viewed in isolation, are not excessive and unsuitable for the customer when taken together in light of the customer's investment profile, as delineated in Rule 2111(a). No single test defines excessive activity, but factors such as the turnover rate, the cost-equity ratio, and the use of in-and-out trading in a customer's account may provide a basis for a finding that a member or associated person has violated the quantitative suitability obligation.

FINRA Rule 2111.05 (*emphasis in the original*).

Thus, FINRA Rule 2111.05 makes clear that the first prong of the suitability analysis – *before a product is even presented to a customer* – requires a broker-dealer firm to conduct reasonable due diligence as to the product. *Id*. Only after the broker-dealer, following such reasonable due diligence, has acquired a reasonable basis to believe that the product "is suitable for at least *some* investors," id., is the broker-dealer allowed to present that opportunity to its customer and proceed with the other steps of the suitability analysis. In other words, the first step of the suitability analysis – which must occur before the broker-dealer determines whether or not to present the product to the customer – is *focused on the product, not the customer*. The second and third steps of the suitability analysis are focused on the customer – i.e. on his or her investment risk profile and the appropriate concentrations of various investments in the customer's portfolio.

Respondent recommended unsuitable investments that would have been unsuitable for any investor let alone an individual approaching retirement. The GPB and other investments in Claimant's portfolios should not have been recommended by Respondent to anyone. Respondent's failures to conduct due diligence on these investments caused Claimant to suffer substantial losses.

Investing a significant portion of Claimant's portfolios in high commission investments was also unsuitable. The incredibly high expense load and fee structure created by the overconcentration of these investments made it very difficult for Claimant to take advantage of a

great bull market. Claimant's objectives and goals were barely a consideration if they were considered at all. This conduct is a systemic violation of Rule 2111.

As a direct and proximate result of Respondent's conduct, Claimant has been damaged in an amount to be determined at the hearing of this case and are entitled to compensation.

### C. NEGLIGENCE

Respondent was negligent in reviewing, agreeing to sell, recommending, and selling unsuitable and high commission alternative investments to Claimant. Such negligence arose directly out of Respondent's failure to adequately investigate these securities prior to approving its sales to Claimant in breach of Respondent's due diligence duties towards its client and vicariously out of the unlawful sales to Claimant by its registered representative.

Respondent owed Claimant duties to act as a reasonable broker-dealer would do under the same or similar circumstances, in connection with its review, recommendation, and sales of securities to Claimant. Respondent also had duties to act reasonably in reviewing, recommending, and selling other investment products to Claimant, and breached those duties when it continued to recommend and sell risky and high commission investment products. Respondent's supervision of its representatives in general was negligent as well as their supervision of specific transactions.

### D. MISREPRESENTATIONS AND OMISSIONS OF MATERIAL FACTS

Respondent made numerous misrepresentations and omissions of material fact to Claimant regarding alternative investments without a reasonable basis to recommend such products.

The Restatement (Second) of Torts has described the claim of misrepresentation as follows:

> (1) One who, in the course of his business, profession or employment, or in any other transaction in which he has a pecuniary interest, supplies false information for the guidance of others in their business transactions, is subject to liability for pecuniary loss caused to them by their justifiable reliance upon the information, if he fails to exercise reasonable care or competence in obtaining or communicating the information.

Restatement (Second) of Torts § 552(1), (2) (1977).

Respondent served as Claimant's broker-dealer and investment advisor. Respondent understood and accepted the trust and reliance reposed in it by Claimant and specifically understood that she looked to Respondent to select suitable investments. Claimant justifiably followed advice stemming from Respondent's material omissions and negligent misrepresentations when Claimant purchased the investments suggested by Respondent.

As a direct and proximate result of her acceptance of Respondent's negligent misrepresentations in connection with the investment products, Claimant has been damaged in an amount to be demonstrated at the hearing.

### E. BREACH OF FIDUCIARY DUTY

Respondent, who acted as Claimant's financial advisors, breached their fiduciary duties when they induced her to invest in the alternative investments and annuities. Brokers who approach their customer and recommend that the customer purchase an investment have a fiduciary duty to independently investigate that investment before recommending it. *See SEC v. Glt Dain Rauscher, Inc.*, 254 F.3d 852, 857-858 (9th Cir. 2001) (stating that a financial professional "had a duty to make an investigation that would provide him with a reasonable basis for a belief that the key representations in the statements provided to the investors were truthful and complete."). Claimant's relationship with Respondent was one of a fiduciary based on contract, her relationship with Respondent, and the reliance she placed on Respondent to offer sound, unconflicted financial advice.

Respondent held the entire trust and confidence of Claimant on the subject of investments. Respondent failed to adequately investigate the investments, recklessly ignored a plethora of red flags and problems surrounding the offerings which Respondent had a duty to investigate,

concealed from Claimant material information regarding the investments, and actively, unreasonably, and illegally induced Claimant to invest her money in a way that led to guaranteed and unearned profit for Respondent, but hindered Claimant's portfolio growth in a clear conflict of interest. As a direct and proximate result of Respondent's breaches of the fiduciary duties owed to Claimant in connection with its alternative investments and other recommendations, Claimant has been damaged in an amount to be determined at the hearing.

**RELIEF REQUESTED**

As a result of the course of conduct outlined above, Respondent is liable to Claimant as follows:

(1) for all losses of principal suffered by Claimant;

(2) for all interest, commissions and fees paid by Claimant;

(3) for the loss of income that would have been received had Claimant's accounts been managed properly, as well as other losses, foreseeable or not, that Claimant has suffered, including non-pecuniary losses;

(4) for attorneys' fees, costs and other expenses;

(5) for interest, both pre-judgment and post-judgment;

(6) for all other sums Claimant is entitled to at law or equity; and

(7) for punitive damages.

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Respectfully Submitted,

*/s/ Gavin Rush*

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