

BEFORE THE ARKANSAS SECURITIES COMMISSIONER  
CASE NO. S-09-037

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IN THE MATTER OF:

ORDER NO. S-09-037 ARKANSAS SECURITIES DEPT.

APPLE TREE INVESTMENTS, INC.  
JOHN STEVEN KIEFER  
MITCHUM WILHITE TAPSON

RESPONDENTS

CONSENT ORDER

This Consent Order (the "Order") is entered pursuant to the Arkansas Securities Act, Ark. Code Ann. §§ 23-42-101 through 23-42-509 (the "Act"), the Rules of the Arkansas Securities Commissioner (the "Rules"), and the Arkansas Administrative Procedures Act, Ark. Code Ann. §§ 25-15-101 through 25-15-219, in accordance with an agreement by and between the Staff of the Arkansas Securities Department ("Staff") and Respondents, Apple Tree Investments, Inc. ("Apple Tree"), John Steven Kiefer ("Kiefer"), and Mitchum Wilhite Tapson ("Tapson").

**I. INTRODUCTION**

1. Apple Tree is a broker-dealer registered in Arkansas with a Central Registration Depository ("CRD") number of 144444.
2. Kiefer is a broker-dealer agent and investment advisor representative registered in Arkansas with an individual CRD number of 4428904. Kiefer was and is President of Apple Tree, with the exception of time from September 2008 through February 2009, when another Designated Principal served as President of Apple Tree. Kiefer was and is a Designated Principal of Apple Tree, with the exception of time from April 16, 2008, through February 2009, when Kiefer shared the responsibilities of supervising all registered representatives with another Designated Principal who was also the Office of Supervisory Jurisdiction Supervisor ("OSJS").

Kiefer was and is the Chief Compliance Officer of Apple Tree. Apple Tree and Kiefer may be collectively referred to herein as the “Apple Tree Respondents.”

3. Tapson was a registered agent of Apple Tree from February 27, 2008, to August 31, 2009, with an individual CRD number of 5344558.

4. The Staff has conducted an investigation into Respondents’ activities in connection with the marketing and sale of Class B shares and Class C shares of mutual funds.

5. Respondents have cooperated with the Staff by responding to inquiries, meeting with the Staff in person, providing documentary evidence and other materials, and providing regulators with access to facts relating to the investigation.

6. Respondents have advised the Staff of their agreement to resolve the investigation relating to the marketing and sale of Class B and Class C shares of mutual funds in this Consent Order (“Order”).

7. Respondents admit the jurisdiction of the Act and the Arkansas Securities Commissioner (“Commissioner”) and permanently waive any right to a hearing and appeal under the Arkansas Securities Act, Ark. Code Ann. §§ 23-42-101 through 23-42-509, and the Arkansas Administrative Procedures Act, Ark. Code Ann. §§ 25-15-201 through 25-15-218, with respect to this Order.

8. Respondents, without admitting or denying the Statement of Facts and Conclusions of Law contained in this Order, and solely for purposes of this proceeding, consent to the entry of this Order and agree to abide by its terms.

NOW, THEREFORE, the Arkansas Securities Commissioner, as administrator of the Arkansas Securities Act, hereby enters this Order:

## II. STATEMENT OF FACTS

### A. Multi-Class Mutual Funds: Class A, Class B, and Class C Shares Generally

1. Generally, a mutual fund, may offer more than one “class” of its shares to investors. Each class represents a similar interest in the mutual fund's portfolio. The principal difference between the classes is that the mutual fund will charge different fees and expenses depending on the “class” of investment chosen. Mutual fund shares are typically designated as Class A, Class B, or Class C shares. Class A shares are commonly referred to as “front-end load funds” and charge the investor a sales commission at the time the investment is made. Other classes (e.g., Class B, Class C, etc.) are commonly referred to as “back-end load funds” and have different sales charge and expense characteristics. Class B and C shares only charge the investor a sales commission at the time the mutual fund is sold. In the case of Class B shares, there is a declining sales charge (e.g. 6%, 5%, 4%, etc.) imposed over a fixed period of time, typically six years. This sales charge is known as a Contingent Deferred Sales Charge (“CDSC”). The CDSC is calculated based upon the balance of the fund at the time of sale. In the case of Class C shares, the investor will pay a 1% CDSC if the Class C shares are sold within one year of purchase.

2. The total of mutual fund costs borne by investors ultimately falls into two categories: the sales charges collected directly from shareholders for specific transactions (such as a purchase, redemption, or exchange) as described above and fees and operating expenses imposed continuously on the fund assets.<sup>1</sup> When an investor buys shares with a front-end load,

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<sup>1</sup> Annual operating expenses are not charged directly to investors but are deducted from fund assets. These expenses include the management fee, an ongoing charge paid to an investment adviser who manages the fund's assets and selects its portfolio of securities. Some funds charge a Rule 12b-1 fee, named for the rule under the Investment Company Act of 1940 that authorizes mutual funds to pay for distribution expenses, including sales charges used to compensate sales professionals for selling fund shares, directly from a fund's assets. In addition, a fund may also pay a service fee to compensate sales professionals, or other service providers, for ongoing services to investors or their accounts. In addition, all mutual funds incur brokerage and other transaction-related costs that are borne indirectly by the investors in the funds.

the front-end load portion of the offering price is not invested in the fund, but instead is paid to the fund's principal underwriter or distributor. When the purchase is made through a broker-dealer, the fund's principal underwriter or distributor pays a part of the front-end load amount to the broker-dealer that sold the fund shares to the investor. When an investor buys a "back-end load" fund with a CDSC, all of the investor's money is invested in the mutual fund at the time of purchase.

3. Mutual funds that sell Class A shares with a front-end load usually offer discounts at certain pre-determined levels of investment, which are called "breakpoints." For example, a mutual fund might charge an investor 5.75% of the sales price for purchases of less than \$50,000, but reduce the sales charge to 4.75% for investments between \$50,000 and \$99,999. An investor can usually procure discounts on sales charges at investment levels of \$50,000, \$100,000, \$250,000, and \$500,000. At the \$1 million investment level, generally there is no sales charge.

4. The specific terms and conditions under which breakpoint discounts may become available are determined by the mutual funds and can vary from fund to fund. Generally, an investor can procure a breakpoint discount through either a single purchase large enough to reach a breakpoint or multiple purchases in a single mutual fund or any of the funds in a family of funds, the aggregate value of which is large enough to reach a breakpoint. In reaching a breakpoint, an investor is typically permitted to aggregate transactions made by certain family or household members and transactions in certain other related accounts, e.g., retirement accounts. An investor may aggregate purchases over time to meet applicable breakpoint thresholds through a "right of accumulation" ("ROA") or "letter of intent" ("LOI"). An investor may be eligible for a discount through an ROA by aggregating the amount of his or her current purchase with the

amount of certain prior purchases. An LOI is a written statement of intent by the investor to purchase a certain amount of mutual fund shares in the future, typically within a thirteen-month period.

5. Mutual funds are required to disclose to the investor the schedule of available breakpoints in their prospectuses and disclose how an investor may qualify for breakpoints either in the prospectuses or in their statements of additional information, both of which are filed with the U.S. Securities and Exchange Commission (“SEC”) on Form N-1A. Mutual funds generally incorporate by reference into their prospectuses the information included in their statements of additional information.

6. Broker-dealers who sell fund shares to retail customers must disclose breakpoint discount information to their customers and must have procedures reasonably designed to ascertain information necessary to determine the availability and appropriate level of breakpoints. A failure to do so can result not only in the customer being deprived of a benefit to which he or she is entitled, but also may result in the broker-dealer and representative receiving increased commissions at the customer's expense.

7. As in Class A shares, mutual fund companies pay brokers a concession, or commission, at the point of sale for Class B shares, usually four percent of the amount invested. To recover the cost of the concession, Class B shares carry a higher, continuous, asset-based Rule 12b-1 fee than is charged for an equivalent purchase of Class A shares. Thus, Class B shares have higher annual operating expenses than Class A shares. However, since there is no “front-end load” sales charge on Class B or C shares, 100% of a customer’s funds are invested in the particular mutual fund at the time the investment is made. Additionally, most mutual funds allow a customer to convert Class B Shares into Class A shares after a 5-year holding period,

which would eliminate the CDSC and give the investor the benefit of lower annual operating expenses.

8. For investors, breakpoints and higher expenses generally have a direct and significant impact on a mutual fund investment's return. The significance of these differences is that, at certain dollar levels and holding periods, an equal investment in Class A shares, as opposed to Class B shares, may be in the best interest of the investor depending on the term the investor stays invested in the particular mutual fund.

9. A registered representative receives an immediate commission credit when fund shares are purchased, regardless of the share class. However, there is a difference in the amount of commission credit a registered representative receives for selling Class B versus Class A shares of the same fund. As breakpoints are reached in the sales of Class A shares, the representative's sales commission is reduced as the amount of the gross sales charge is reduced. On Class A share purchases, the net sales commission to the broker is generally 50 basis points, or 0.5%, less than the gross sales charge to the investor.<sup>2</sup> However, in the sale of Class B shares, the commission percentage paid to the representative remains constant at 4%. As a result, depending on the amount invested in a particular mutual fund by a customer, a representative may receive a higher commission by recommending the purchase of more costly Class B shares instead of less-expensive, breakpoint-discounted Class A shares.

10. Class C shares may be a suitable investment vehicle when certain specific criteria are met, such as a need for short-term liquidity. Thus, the suitability of Class C shares depends on the investor's individual circumstances. A back-end load - although small - is typically charged if funds are withdrawn within the first year. Class C shares have higher annual

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<sup>2</sup> For example, if the mutual fund charges the investor a 5.5% gross sales charge on the total amount invested, the broker will receive a net commission of 5%. Likewise, if the gross sales charge is 3.5%, the broker would receive a net commission of 3% of the total amount invested, and so on.

operating expenses than Class A shares. Also, Class C shares cannot be converted into Class A shares, which would allow the eventual benefit of a lower expense ratio. Finally, Class C shares do not offer breakpoint and other discounts when the account reaches certain levels. In general, Class C shares are not suitable for investors with a long-term investment horizon. Due to the higher expenses and fees associated with Class C shares, returns will be reduced the longer an investor holds Class C shares as the expenses and fees accumulate over time.

**B. The Regulatory Environment Regarding Mutual Fund Sales Practices.**

11. On December 23, 2002, the National Association of Securities Dealers<sup>3</sup> issued a written “Notice to Members” (“NTM”) warning firms that mutual fund transactions must be effected on the terms most advantageous to the customer and that the customer must receive the benefit of all available discounts to which they are entitled. *See* NASD Notice to Members dated December 23, 2002. According to the notice:

In order for a customer purchasing a mutual fund through an NASD member firm to incur the most beneficial (the lowest) front-end sales charge percentage, complete information relating to the customer and certain related accounts is necessary. The required information relates to the customer’s account and related and linked accounts and includes the dollar size of the pending transaction, the dollar size of anticipated transactions, and amounts previously invested in the specific fund and other related funds, valued as specified in the prospectus.

\* \* \*

After consultation with SEC staff, NASD is issuing this Notice to Members to alert members to this important issue and to specify appropriate member action that must be taken immediately to ensure that their customers receive the advantage of breakpoints to which the customers are entitled, namely, a reduction in the sales charges commensurate with the size and nature of the customers’ transaction.

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<sup>3</sup> The National Association of Securities Dealers (“NASD”) is now known as the Financial Industry Regulatory Authority (“FINRA”), which was created in July 2007 through the consolidation of the NASD and the member regulation, enforcement and arbitration functions of the New York Stock Exchange (“NYSE”). FINRA is a self-regulatory organization (“SRO”) made up in part of broker-dealer member firms.

12. Prior to this NTM, on November 10, 1998, the Securities and Exchange Commission approved amendments to the NASD Interpretive Memorandum (“IM”) 2830-1 in order to clarify the application of the mutual fund breakpoint sales rule to modern portfolio investment strategies. NASD Rule IM-2830-1 (now FINRA Rule 2342) prohibits the sales of mutual fund shares in amounts below breakpoints only if such sales are made so as to share in higher sales charges.

13. The amendments specify more precisely those facts and circumstances that FINRA will consider when examining whether trades that miss breakpoints, but are made pursuant to bona fide asset allocation programs, may have violated FINRA Rule 2342. The application of the standard in FINRA Rule 2342 depends on the facts and circumstances of particular transactions to determine whether a member executed a transaction for the purpose of earning a higher sales charge. In making such determinations, FINRA will consider, among other things: (a) whether a member has retained records that demonstrate that the trade was executed in accordance with a bona fide asset allocation program that the member offers to its customers which is designed to meet their diversification needs and investment goals; and (b) whether the member disclosed to its customers that they would not qualify for breakpoint reductions that were otherwise available.

### **C. Apple Tree’s Written Compliance Procedures**

14. The duties of disclosure applicable to the sale of multi-class mutual funds are thoroughly covered in Apple Tree’s own compliance manual, titled “Apple Tree Investments, Inc.: Written Supervisory Procedures” (“Compliance Manual”). The Compliance Manual designates Respondent Kiefer as the “designated principal” responsible for supervising “mutual

funds.” See Compliance Manual, p. 3. The Compliance Manual further designates Kiefer as the Chief Compliance Officer of Apple Tree. See *id.*

15. The Compliance Manual contains a specific section on mutual funds. See Compliance Manual, pp. 33-42. According to the Compliance Manual, Kiefer “is responsible for the review and approval of each mutual fund transaction conducted by the Representatives....” See Compliance Manual, p. 34. According to the Compliance Manual, the specific transactions Kiefer is required to “detect and prevent” include: (a) Unsuitable Transactions; (b) Breakpoints Missed; (c) Letter of Intent Not Used; (d) Rights of Accumulation Not Exercised; and (e) Improper Use of Mutual Fund Share Classes. See *id.*

16. The Compliance Manual contains the following discussion of mutual fund share classes:

*Clients must be aware of the differences among the classes of shares available from the mutual fund companies. These include front-end load, back-end load and level load. Furthermore, clients must be made aware that all funds pay 12b-1 fees (trails). A mutual fund prospectus providing details must be provided to the client prior to or at the time of purchase of a new fund.*

Class A shares (front-end load): Generally impose a front-end sales load and no (or a low) ongoing fee to pay for sales and marketing expenses (Rule 12b-1 fees). Usually the front-end sales load will decrease at certain breakpoints depending on the size of the purchase and whether the purchase qualifies for a letter of intent or rights of accumulation which also may result in a lower sales charge. A front-end sales charge means a portion of the customer’s funds are not invested and instead pay the front-end charge. The sales charge may be reduced if the amount invested is greater than certain pre-determined levels, which are referred to as breakpoints (discussed further below). *If investments are divided between fund families, the breakpoints may not be realized which may result in higher expenses. Multiple fund families may not be used unless there is benefit to the client which is documented and approved by a Designated Principal.*

Class B shares (back-end load): Generally do not impose a front-end sales charge but may impose a contingent deferred sales charge (CDSC) on share redemption and relatively high 12b-1 or other asset-based fees. The amount of the CDSC usually declines the longer the shares are held. Class B shares often automatically convert to Class A shares (with lower asset-based fees) after a period of time,

usually after the CDSC declines to zero. All of the customer's funds are invested at the time of purchase. These funds may not be referred to as no-load funds since they impose a back-end contingent charge.

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Additionally, some mutual funds offer other classes that impose no front-end or back-end sales charges and relatively low asset-based fees. These may be offered to limited types of purchasers such as retirement plans or institutional investors. In making a suitability determination, the RR should:

- understand the advantages and disadvantages of different mutual fund classes
- consider these differences based on the customer's investment objectives, amount to be invested, and the customer's time horizon for the investment
- *consider that B or C shares generally should not be recommended to customers making purchases in large amounts that may qualify for lower costs because of breakpoints, letters of intent, or rights of accumulation available through the purchase of A shares*

*Clients must sign a statement acknowledging understanding of above prior to an order being placed.*

See Compliance Manual, pp. 35-36 (emphasis added).

17. Additional sections of the Compliance Manual for which Kiefer was directly responsible include:

On a daily basis, based on the order records and daily transaction report the Designated Principal is to review mutual fund purchase transactions for potential breakpoint sales. Items to look for include:

- Purchases near but below common breakpoint levels (\$25,000, \$50,000, \$100,000, etc.)
- Multiple purchases of mutual funds that, if aggregated, would have qualified the customer for a breakpoint if one or fewer funds were purchased
- *For purchases where it appears the customer would have been better served by purchasing an additional amount or where purchasing fewer funds would have qualified for the breakpoint[.]*

For some mutual funds, front-end sales charges decrease as the dollar amount invested increases. These thresholds for reduced sales charges are called breakpoints. Different fund families establish different opportunities to link accounts, transactions, and share classes to qualify purchasers for reduced sales charges. The RR has an obligation to disclose the existence of breakpoints to enable the customer to evaluate the desirability of making a qualifying purchase. The RR also must indicate on the mutual fund order if the customer qualifies for a breakpoint because of linked accounts, transactions, or share classes or other basis for meeting a breakpoint by linking the customer's transaction with another. *“Improper breakpoint sales” is a term that denotes selling mutual funds to maximize commissions earned, i.e., selling an amount close to but below a breakpoint. The customer will, therefore, pay a higher sales charge. This practice is prohibited. Recommending diversification among several funds with similar investment objectives, particularly if sales occur in amounts just below the breakpoints of one or more funds sold, may not be in the best interests of the customer[.]*

With the advent of automated processing and settlement systems in the mutual fund industry, such as Fund/SERV, it is essential for members to enter correctly into these systems the breakpoint information pertaining to customer transactions. *Members must have procedures reasonably designed to ascertain all information necessary to establish the correct breakpoint level; training and procedures to ensure that personnel understand the proper steps for inputting the information correctly into the automated processing and settlement system; and supervisory procedures that reasonably ensure compliance in this area.* Due to the fact that automated processing and settlement systems may not disclose to the mutual fund company the identity of the members customer, members cannot rely on the mutual fund company to allocate the correct breakpoint to a transaction or override the member's failure to do so.

The Firm recognizes its responsibility in ascertaining that it is able to identify “linked accounts” in order to ensure that mutual fund customers receive the proper discount on breakpoint sales. Specifically, the representative will ascertain that the following questions are satisfactorily addressed:

1. Does the customer already hold shares of any funds within the same fund family in his account?
2. Does the customer hold shares of any funds within the same fund family in any other accounts outside the firm?
3. Do related parties of the customer hold shares of any funds within the same fund family in accounts at this broker/dealer, other broker dealers, or in other platforms, such as 401(k) plans or 529 plans?

4. How much is the current purchase?
5. What are the customer's total holdings that may be counted toward determining breakpoint eligibility?
6. Determine whether the customer is entitled to a breakpoint based upon his total holdings and the holdings of all related parties.
7. Does the customer have a letter of intent on file that would entitle the customer to a further discount?

*The Designated Principal shall ensure that the representative ascertains that a customer entitled to a volume discount is accorded the lower sales charge. It is the duty of the Representative to ensure that the customer is informed about the next available quantity discount breakpoint upon which the consequent reduced sales charge would be based on. The Representative should be aware that selling of mutual fund shares just below the breakpoint in order to receive the higher sales charge is prohibited. It is therefore crucial for the Registered Representative to ascertain that a customer understands the whole concept of breakpoint before making any large purchases—at what point breakpoint takes place, the savings implications, as well as the opportunity to purchase additional shares for a lesser sales charge.*

The Firm recognizes that dramatic growth in the number of fund families, share classes, and, to a lesser extent, customer account types, has underscored the need to assure that breakpoints are applied appropriately. Breakpoint schedules, and the conditions under which discounts are available, differ among fund families, as noted above. For example, different fund families establish different opportunities to link accounts, transactions, and share classes. Sales charge discounts related to reinstated transactions and exchanges also differ among fund families. *It is the Designated Principal's responsibility to ascertain that Representatives are fully aware that they are to ensure that the customers are made aware of sales charges discounts as and when applicable.*

See Compliance Manual, pp. 37-39 (emphasis added).

#### **D. Respondents' Unsuitable Mutual Fund Sales**

18. The Rules of the Arkansas Securities Commissioner require that a registered representative, before recommending the purchase, sale, or exchange of any security, "have reasonable grounds for believing that the recommendation is suitable for such customer upon the basis of the facts, if any, disclosed by such customers as to his other security holdings and financial situation and needs." See Rule 308.01.

19. In late 2008, the Staff began audits of Apple Tree customer accounts. These audits revealed issues with the amount of Class B and Class C shares being sold to Apple Tree customers with total available funds for investment in excess of \$50,000.

20. Pursuant to their investigation, the Staff believes that Kiefer and Tapson have made numerous unsuitable recommendations for the purchase of securities to Apple Tree customers. Specifically, Kiefer and Tapson sold several million dollars of Class B and Class C mutual fund shares to Apple Tree customers without disclosing to said customers the economic advantages of purchasing Class A mutual fund shares.

21. Kiefer and Tapson solicited customers through group seminars and radio and television marketing campaigns that introduced an investment program entitled the “Kiefer Method.” Kiefer and Tapson represented to customers that the “Kiefer Method” was designed to achieve maximum asset allocation and diversification, particularly for investors who were retired or planning for retirement.

22. While the specific facts regarding each mutual fund customer vary, the “Kiefer Method” involved a recommendation that a new customer: (a) liquidate his or her portfolio with his or her current broker and bring the proceeds to Apple Tree for re-allocation, or (b) agree to a complete asset transfer, liquidation, and re-allocation of the entire portfolio.

23. Once the customer’s funds were ready to be invested in accordance with the “Kiefer Method,” Kiefer and Tapson would typically divide the customers total investment proceeds into smaller “blocks” of cash, and place the customer in multiple mutual funds (typically as many as 8 to 12 different funds) spread over multiple mutual fund families (typically 6 to 10 different mutual fund families).

24. A typical account scenario is as follows. Customers AR1 and AR2, who are related and live in the same household, opened two accounts through Kiefer at Apple Tree. The first account was opened on or about March 17, 2008. AR1 and AR2 transferred \$186,586.61 worth of various investments from Citigroup Smith Barney, which included closed end mutual funds, bonds, and a small amount of cash. Approximately one week later, Kiefer liquidated the account and commenced purchasing \$159,998.29 of Class B mutual fund shares. Kiefer divided the proceeds into 6 blocks ranging from \$15,000 to \$34,999.18. Kiefer invested these “blocks” into Class B shares of six different mutual funds over five different mutual fund families. AR1 and AR2 paid no sales commission at the time of purchase, but Keifer received a 4.0% sales commission from the mutual fund.

25. Subsequently, on or about April 15, 2008, AR1 and AR2 transferred \$629,344.52 in cash to a new IRA account at Apple Tree. Commencing on or about April 28, 2008, Kiefer purchased \$301,807.00 in Class B shares of eight different mutual funds over six different mutual fund families. AR1 and AR2 paid no sales commission at the time of purchase, but Keifer received a 4.0% sales commission from the mutual fund.

26. Within three months, Kiefer invested AR1 and AR2 in \$461,805.29 of Class B shares of ten different mutual funds spread over seven different mutual fund families. In spite of the fact that it is common knowledge throughout the mutual fund industry that Class A shares offer numerous discounts and long term investment performance advantages for purchases of this magnitude, Kiefer failed to disclose those material facts to AR1 and AR2 and failed to recommend suitable securities to these customers.

27. Another example account involves Customers AR3 and AR4, who are related and live in the same household. AR3 and AR4 transferred approximately \$1,086,666 to Apple Tree in April of 2008 and opened four separate accounts. AR3 and AR4 were solicited by Kiefer.

28. Once the cash proceeds were transferred to Apple Tree, Kiefer invested approximately 53% of AR3 and AR4's total investment proceeds into mutual funds. However, of the 53% allocated to mutual funds, Kiefer allocated 73% to Class B shares. Specifically, Kiefer purchased \$453,990.00 of Class B shares in seven different mutual funds over six different mutual fund families. AR3 and AR4 paid no sales commission at the time of purchase, but Kiefer received a 4.0% sales commission from the mutual fund.

29. Simultaneous with the Class B purchases, Kiefer invested AR3 and AR4 in \$129,416.00 of Class C shares of two mutual funds from two mutual fund families. AR3 and AR4 paid no sales commission at the time of purchase, but Kiefer received a 1.0% sales commission from the mutual fund. Kiefer recommended these purchases even though AR3 and AR4 had no short-term liquidity needs and had a five to ten year investment horizon.

30. Within a few short months, Kiefer invested AR3 and AR4 in \$583,406.00 of Class B and Class C shares in nine different mutual funds spread over eight different mutual fund families. Even though it is common knowledge throughout the securities industry that Class A shares offer numerous discounts and long term investment performance advantages for purchases of this magnitude, Kiefer failed to disclose those material facts to AR3 and AR4 and failed to recommend suitable securities to AR3 and AR4.

31. Similar facts regarding the application of the "Kiefer Method" are repeated over and over in numerous accounts handled by Kiefer and Tapson at Apple Tree. These accounts

with “multi-fund” and “multi-family” Class B and Class C purchases range in size from \$75,000 to approximately \$875,000.

32. In recommending that these customers purchase Class B and/or Class C mutual fund shares, Kiefer and Tapson did not adequately disclose the differences in mutual fund share classes, including information about commissions and annual expenses, and that an equivalent investment in Class A shares could yield a higher return as a result of applicable breakpoint discounts and reduced ongoing expenses.

33. Kiefer and Tapson did adequately disclose that the customers were not going to pay any “front-end load” sales charges.

34. In recommending that these customers purchase Class B and/or Class C shares, Kiefer and Tapson failed to disclose a conflict of interest present in their recommendation due to the direct financial benefit Kiefer and Tapson received as a result of the Class B and/or Class C transactions. In all of these instances, the net sales commission to Keifer and Tapson could have been less than the commission each earned, with the actual difference depending on several factors, including the amount of funds invested by the customer in the particular mutual fund and/or particular mutual fund family and the ultimate holding period by the customer. These facts were not adequately explained to the Apple Tree customers.

35. Kiefer and Tapson recommended and sold Class B and Class C shares of mutual funds in multiple mutual fund families to customers who, depending on the amount of the investment and the holding period, generally would have benefited had they instead purchased Class A shares in fewer fund families. Specifically, these customers purchased Class B and Class C shares in multiple mutual funds which, had they purchased Class A shares, could have

qualified for breakpoints beginning at the \$50,000 level, through single purchases, aggregating multiple purchases, employing rights of accumulation, or utilizing letters of intent.

36. As a result of these customers' purchases of Class B shares, Kiefer and Tapson received greater commissions from these transactions than they would have earned had they sold Class A shares.

37. There were no reasonable grounds for Kiefer and Tapson to believe that the recommendations that these customers purchase Class B and/or Class C shares were suitable for said customers.

#### **E. Respondent Tapson's Unsuitable Mutual Fund Switching**

38. Mutual fund switching is the selling or redemption of one mutual fund with a sales charge to buy another mutual fund with a sales charge. Mutual fund switching has been held to violate the antifraud provisions of the federal securities laws when registered representatives, in order to increase their compensation, induce investors to incur the costs associated with redeeming shares of one mutual fund and purchasing the shares of another fund and the benefit to the customer does not justify those costs.

39. Tapson made several unsuitable "switch" recommendations to customers of Apple Tree for the purchase of Class B shares. One example of an unsuitable "switch" recommendation by Tapson involved customer AR5, who transferred a portfolio of six mutual funds to Apple Tree with an approximate value of \$75,000. All of the transferred mutual funds were in Class A shares, which means that AR5 had already paid a front-end load charge in acquiring the shares. All of the transferred shares were in the "American Funds" family, which is consistently regarded as one of the best mutual fund companies with some of the highest

performing individual funds. Three of the funds held by AR5 were rated “3 Stars” by Morningstar. Two of the funds were rated “4 Stars” and one fund was rated “5 Stars.”

40. On or about August 20, 2008, Tapson liquidated all of AR5’s Class A mutual fund shares with the single exception of the Class A shares of the American Funds EuroPacific Growth mutual fund.

41. Over a period of months commencing on or about August 22, 2008, Tapson then purchased Class B shares of 7 different mutual funds and Class C shares of one mutual fund, all spread across five separate mutual fund families.

42. Even though AR5 already held Class A shares in American Funds EuroPacific Growth when the account was first opened at Apple Tree, Tapson also purchased Class B shares of American Funds EuroPacific Growth for AR5. There was no reasonable basis for purchasing Class B shares of a mutual fund when the customer already holds Class A shares of the same mutual fund.

43. Tapson’s switch recommendations caused AR5 to incur renewed CDSC holding periods for all of the Class B mutual funds purchased and prevented AR5 from taking advantage of the opportunity for cost free exchanges between existing mutual fund families. Tapson further failed to obtain industry standard “switch letters” that would have notified AR5 of the implications of the mutual fund switch transactions.

44. There was no benefit to AR5 in the mutual fund switch transactions recommended by Tapson. Tapson recommended the switch transactions without performing any substantive analysis of AR5’s current mutual fund holdings. Tapson had no reasonable basis to believe the switch recommendations were suitable for AR5.

45. Tapson failed to disclose material facts to AR5 regarding the switch transactions and failed to recommend suitable securities to AR5.

46. Tapson engaged in the unsuitable mutual fund switch transactions on behalf of AR5 for the sole purpose of generating commissions.

47. Similar facts regarding the unsuitable mutual fund switch transactions by Tapson are repeated in other accounts handled by Tapson at Apple Tree. The Staff believes Tapson failed to disclose to the mutual fund “switch” customers numerous material facts including, but not limited to: (1) the historical total return of each fund; (2) a comparison of the expense ratios; (3) the sales charge, if any, to be incurred where an applicable Class B Share CDSC holding period had not expired; (4) the implication and application of a new Class B Share CDSC holding period; (5) the eventual conversion of shares currently held to a class of shares with lower operating expenses; (6) the convertibility of shares in the new fund to classes with lower operating expenses; and (7) the opportunity to switch to other mutual funds within the same family of funds through a cost free exchange.

48. Tapson made these unsuitable switch recommendations without performing an adequate analysis of the current mutual fund holdings. Tapson had no reasonable basis to believe the switch recommendations were suitable for the customers.

49. In making the unsuitable switch recommendations, Tapson failed to disclose to the customers a material conflict of interest present in the recommendation due to the direct financial benefit Tapson received as a result of the switch transactions.

**F. Apple Tree and Kiefer's Failure to Supervise**

50. Apple Tree failed to reasonably supervise Kiefer and Tapson in order to detect or prevent the violations of the Act and Rules as are generally described herein.

51. Although there was another Designated Principal at Apple Tree from April 16, 2008 to February 2009, Kiefer, as a Designated Principal of Apple Tree, was also required to exercise direct supervision of the purchase and sale of securities at Apple Tree. *See* Ark. Code Ann. § 23-42-301(e). Kiefer also held additional supervisory responsibilities at Apple Tree, including, but not limited to, the review and approval of each mutual fund transaction conducted by registered agents of Apple Tree. *See* Compliance Manual at pp. 3 and 34. Kiefer failed to reasonably supervise Tapson in order to detect or prevent the violations of the Act and Rules described herein.

**III. CONCLUSIONS OF LAW**

1. The Arkansas Securities Commissioner has jurisdiction over this matter pursuant to Ark. Code Ann. §§ 23-42-205 and -308.

2. The conduct of Respondents described herein constitutes a willful violation of Rule 308.01 of the Rules of the Arkansas Securities Commissioner which subjects Respondents to sanctions pursuant to Ark. Code Ann. § 23-42-308(a)(2)(B).

3. The conduct of Respondents described herein operates as a fraud and deceit in connection with the offer, sale, and purchase of a securities in violation of Ark. Code Ann. § 23-42-507.

4. The conduct of Respondents Apple Tree and Kiefer described herein constitutes failure to supervise which subjects Respondents Apple Tree and Kiefer to sanctions pursuant to Ark. Code Ann. § 23-42-308(a)(2)(J).

5. The Arkansas Securities Commissioner finds the following relief appropriate and in the public interest.

#### **IV. ORDER**

On the basis of the Statement of Facts, Conclusions of Law, and Respondent's consent to the entry of this Order, IT IS HEREBY ORDERED:

1. This Order concludes the investigation by the Arkansas Securities Department and any other action that the Arkansas Securities Department could commence under applicable Arkansas law on behalf of the state of Arkansas relating to the marketing and sale of Class B and Class C mutual fund shares by Respondents through September 1, 2009, provided however, that excluded from and not covered by this paragraph are any claims by the Arkansas Securities Commissioner and/or Arkansas Securities Department relating to the "Order" provisions contained herein.

2. Respondents will CEASE AND DESIST from violating the Arkansas Securities Act and will comply with the Arkansas Securities Act.

3. Respondents, through their execution of the attached Consents to Entry of Order, voluntarily waive their right to a hearing on this matter and to judicial review of this Order under the Arkansas Securities Act and the Arkansas Administrative Procedures Act.

4. Respondents Kiefer and Apple Tree Investments, Inc. shall pay a total civil fine of fifty thousand dollars (\$50,000). Such amount shall be due and payable within ten (10) business days from date of entry of this Order. Respondents Kiefer and Apple Tree Investments, Inc. are jointly and severally liable and responsible for payment of the civil fine.

5. Respondent Kiefer will not act in a supervisory capacity at any broker-dealer for a period of one (1) year unless specific approval is granted by the Arkansas Securities Department

("Department"), provided however, that the Department may extend this provision of the Order for an additional year after examination of the performance of Apple Tree supervisory procedures during this period of time.

6. Within 30 days of the date of entry of this Order, Apple Tree shall name a designated principal who shall have direct supervision over the purchase and sale of securities in Arkansas in accordance with Ark. Code Ann. § 23-42-301(e).

7. Respondent Kiefer shall be suspended from registration with Apple Tree for a period of 14 days, with the suspension commencing 10 days after Apple Tree formally names a new designated principal in accordance with Section IV, Paragraph 6, above.

8. Within 20 days of the date of entry of the Order, the Apple Tree Respondents shall prepare a "Mutual Fund Disclosure" that includes complete disclosures concerning mutual fund share classes and the differences in fees and expenses connected with the purchase of different mutual fund share classes.<sup>4</sup>

9. The Staff will review the Mutual Fund Disclosure and notify the Apple Tree Respondents in writing of any deficiencies. Any such notice shall include a reasonable deadline for the Apple Tree Respondents to cure any deficiencies and re-submit the Mutual Fund Disclosure for approval by the Staff.

10. Within 10 days of final approval of the Mutual Fund Disclosure by the Staff, the Apple Tree Respondents shall place the Mutual Fund Disclosure on the home page of their website(s) for a minimum of one year and send the Mutual Fund Disclosure to all current and

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<sup>4</sup> FINRA has published a sample Written Disclosure Statement regarding mutual fund breakpoint discounts. See <http://www.finra.org/Industry/Issues/Breakpoints/P010539>. The FINRA notice regarding the sample disclosure states: "Although FINRA believes that use of this Written Disclosure Statement will facilitate the full and accurate delivery of breakpoint discounts, members are reminded that registered representatives must understand the terms upon which mutual funds offer breakpoints, including the rules regarding rights of accumulation, letters of intent, and valuation, to ensure the delivery of breakpoint discounts. *Thus, use of this Written Disclosure Statement does not diminish members' obligation to train and supervise registered representatives who sell mutual funds.*" See *id.* (emphasis added).

former customers of Apple Tree Investments, Inc. and current customers of Apple Tree Asset Management, Inc. who were formerly customers of Apple Tree, via United States Mail. An accompanying cover letter shall explain why the mailing is taking place and include a prominent reference to this Order entered with the Department. The cover letter shall be submitted to the Staff for review and approval prior to the mailing.

11. Within 10 days of completion of the mailing of the Mutual Fund Disclosure and cover letter, Respondent Kiefer shall provide the Staff with a sworn affidavit certifying that a complete copy of the final version of the Mutual Fund Disclosure and cover letter were mailed to each and every current and former customer of Apple Tree Investments, Inc. and current customers of Apple Tree Asset Management, Inc. who were formerly customers of Apple Tree via United States Mail with sufficient postage to ensure delivery.

12. Following final approval of the Mutual Fund Disclosure by the Staff, the Apple Tree Respondents shall provide the Mutual Fund Disclosure to all new customers of Apple Tree Investments, Inc. at the time of opening a new account. The Apple Tree Respondents shall provide the Mutual Fund Disclosure to all customers of Apple Tree Investments, Inc. thereafter on an annual basis.

13. Upon the entry of this Order, the Apple Tree Respondents will commence an evaluation of all policies and procedures regarding the sale of multi-class mutual funds. Within 90 days of the entry of this Order, the Apple Tree Respondents shall submit a written report to the Staff (the "Report") detailing new written policies and procedures for daily supervision and review of mutual fund purchase transactions that will assist in ascertaining information relevant to the suitability determination for each transaction, including, but not limited to: (a) applicable breakpoint levels for each fund; (b) whether the customer already holds mutual funds within the

same fund family in his or her account; (c) whether the customer would be better served by purchasing fewer funds or funds in the same mutual fund family; (d) whether the customer (or members of the customers household) own any accounts which could be “linked” for breakpoint purposes; (e) the amount of the customer’s total holdings that may be accumulated and counted towards breakpoint eligibility; (f) whether the customer is entitled to a breakpoint based upon his or her total holdings and the aggregated holdings of other related parties; (g) whether a letter of intent would entitle the customer to a further discount; (h) the amount of the customer’s total intended or planned purchases over time which could affect any of the factors listed in this paragraph; (i) any issues regarding the customer’s investment time horizon that would affect share class considerations; and (j) the specific liquidity needs of the customer.

14. The Apple Tree Respondents shall prepare new written forms and reports for the purpose of documenting the internal supervision and review of each mutual fund transaction and the assessment of the factors listed in Section IV, Paragraph 13, above. Copies of these new forms and reports shall be provided with the Report.

15. The Apple Tree Respondents shall prepare new written training materials for registered agents, representatives, and other personnel engaged in mutual fund transactions. Copies of these training materials shall be provided with the Report.

16. The Apple Tree Respondents shall work in good faith with Apple Tree’s clearing firm to establish automatic exception reports to assist in the detection of potential breakpoint and share class suitability issues. The Report shall list and describe in detail each new exception report instituted with the clearing firm.

17. Within 30 days of receipt of the Report, the Staff shall notify The Apple Tree Respondents in writing of any deficiencies in the Report and/or failure to comply with the terms

of this Order relating to the Report. The Apple Tree Respondents shall have 30 days following any written notice to cure any deficiencies. In the event the deficiencies are not cured within 30 days of the written notice, the Apple Tree Respondents shall be deemed to be in violation of this Order.

18. Upon entry of this Order, the Apple Tree Respondents shall revise all formal and informal policies for presenting investment proposals and portfolio projections to potential customers. Upon entry of this Order, all investment proposals and portfolio projections prepared by the Apple Tree Respondents shall include a specific identification of each separate proposed security or mutual fund (by name and symbol) and shall further indentify, for each separate proposed mutual fund, the share class of the fund. The Apple Tree Respondents shall provide a hard copy of all portfolio projections and proposed investment programs (including all charts, graphs, spreadsheets, and PowerPoint presentations) to all prospective customers prior to commencing the purchase of any securities on behalf of a new customer.

19. Respondent Tapson is ordered to pay a civil fine of five-thousand dollars (\$5,000). Such amount shall be due and payable within ten (10) business days from date of entry of this Order.

20. For a period of one year, Tapson is prohibited from acting as an agent or investment adviser representative in Arkansas, unless his employing firm provides on-site heightened supervision of Tapson's activities by a Series 24 Registrant. This heightened supervision must include daily review of Tapson's new accounts, trades, and correspondence by a registered principal to ensure that all correspondence and documents provided to customers have been approved and that trades are authorized, suitable, and comply with the supervisory and compliance policies and procedures set forth by his employing firm.

21. Nothing herein shall preclude Arkansas, its departments, agencies, boards, commissions, authorities, political subdivisions and corporations, other than the Arkansas Securities Department, from asserting any administrative, civil, or criminal claims and/or causes of action against Respondents in connection with the activities and conduct described in this Order.

22. For any person or entity not a party to the Order, this Order does not limit or create any private rights or remedies against Respondents or limit or create defenses of Respondents to any claims. For greater certainty, nothing herein shall preclude the right of Respondents to take a contrary legal or factual position in litigation or other legal proceeding in which the Department is not a party.

23. If after this Order is entered, any Respondent fails to comply with any of the terms set forth herein, the Staff may, at its discretion, upon 10 days written notice to the non-complying Respondent(s), commence a proceeding under the Act and Rules for: (a) violations of this Order; (b) all activities of Respondents referenced in this Order; and/or (c) any activities of Respondents discovered during the investigation underlying this Order.

24. This Order shall be governed, construed, and enforced in accordance the laws of the state of Arkansas, without regard to any choice of law principles.

25. Respondents enter into this Order voluntarily and each separately represent that no threats, offers, promises, or inducements of any kind have been made by the Department or any member, officer, employee, agent, or representative of the Department to induce Respondents to enter into this Order.

26. This Order shall be binding upon Apple Tree Investments, Inc. and its successors and assigns as well as to successors and assigns of relevant affiliates with respect to all conduct

subject to the provisions above and all future obligations, responsibilities, undertakings, commitments, limitations, restrictions, events, and conditions.

27. This Order shall be binding upon John Steven Kiefer and Mitchum Wilhite Tapson and their heirs, successors, and assigns as well as to heirs, successors, and assigns of their relevant affiliates with respect to all conduct subject to the provisions above and all future obligations, responsibilities, undertakings, commitments, limitations, restrictions, events, and conditions.

DATED this 8<sup>th</sup> day of December, 2009.

BY ORDER OF THE ARKANSAS  
SECURITIES COMMISSIONER

  
A. Heath Abshure, Commissioner

**CONSENT TO ENTRY OF ORDER  
BY APPLE TREE INVESTMENTS, INC.**

Apple Tree Investments, Inc. hereby acknowledges that it has been served with a copy of this Consent Order ("Order"), has read the foregoing Order, is aware of its right to a hearing and appeal in this matter, and has waived the same.

Apple Tree Investments, Inc. admits the jurisdiction of the Arkansas Securities Commissioner, neither admits nor denies the Statement of Facts and Conclusions of Law contained in this Order; and consents to entry of this Order by the Arkansas Securities Commissioner as settlement of the issues contained in this Order.

Apple Tree Investments, Inc. agrees that it shall not claim, assert, or apply for a tax deduction or tax credit with regard to any state, federal or local tax for any administrative monetary penalty that Apple Tree Investments, Inc. shall pay pursuant to this Order.

Apple Tree Investments, Inc. states that no promise of any kind or nature whatsoever was made to it to induce it to enter into this Order and that it has entered into this Order voluntarily.

John Steven Kiefer represents that he is President of Apple Tree Investments, Inc. and that, as such, has been authorized by Apple Tree Investments, Inc. to enter into this Order for and on behalf of Apple Tree Investments, Inc.

DATED this 3<sup>rd</sup> day of December, 2009.

APPLE TREE INVESTMENTS, INC.

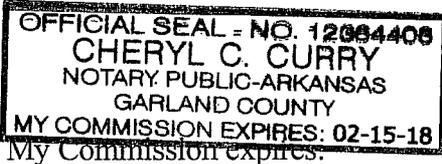
By: \_\_\_\_\_

John Steven Kiefer

Title: \_\_\_\_\_

CEO

SUBSCRIBED AND SWORN TO before me this 3<sup>rd</sup> day of December, 2009.



Cheryl C. Curry  
Notary Public

02-15-18

**CONSENT TO ENTRY OF ORDER  
BY JOHN STEVEN KIEFER**

John Steven Kiefer hereby acknowledges that he has been served with a copy of this Consent Order ("Order"), has read the foregoing Order, is aware of his right to a hearing and appeal in this matter, and has waived the same.

John Steven Kiefer admits the jurisdiction of the Arkansas Securities Commissioner; neither admits nor denies the Statement of Facts and Conclusions of Law contained in this Order; and consents to entry of this Order by the Arkansas Securities Commissioner as settlement of the issues contained in this Order.

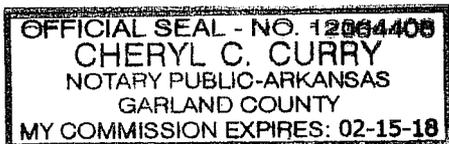
John Steven Kiefer agrees that he shall not claim, assert, or apply for a tax deduction or tax credit with regard to any state, federal or local tax for any administrative monetary penalty that he shall pay pursuant to this Order.

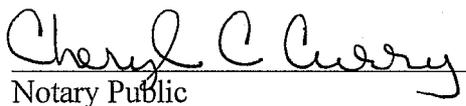
John Steven Kiefer states that no promise of any kind or nature whatsoever was made to him to induce it to enter into this Order and that he has entered into this Order voluntarily.

DATED this 3<sup>rd</sup> day of December, 2009.

  
\_\_\_\_\_  
John Steven Kiefer

SUBSCRIBED AND SWORN TO before me this 3<sup>rd</sup> day of December, 2009.



  
\_\_\_\_\_  
Notary Public

My Commission expires:

02-15-18

**CONSENT TO ENTRY OF ORDER  
BY MITCHUM WILHITE TAPSON**

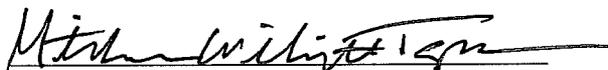
Mitchum Wilhite Tapson hereby acknowledges that he has been served with a copy of this Consent Order ("Order"), has read the foregoing Order, is aware of his right to a hearing and appeal in this matter, and has waived the same.

Mitchum Wilhite Tapson admits the jurisdiction of the Arkansas Securities Commissioner; neither admits nor denies the Statement of Facts and Conclusions of Law contained in this Order; and consents to entry of this Order by the Arkansas Securities Commissioner as settlement of the issues contained in this Order.

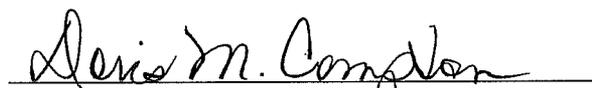
Mitchum Wilhite Tapson agrees that he shall not claim, assert, or apply for a tax deduction or tax credit with regard to any state, federal or local tax for any administrative monetary penalty that he shall pay pursuant to this Order.

Mitchum Wilhite Tapson states that no promise of any kind or nature whatsoever was made to him to induce it to enter into this Order and that he has entered into this Order voluntarily.

DATED this 24<sup>th</sup> day of December, 2009.

  
\_\_\_\_\_  
Mitchum Wilhite Tapson

SUBSCRIBED AND SWORN TO before me this 24<sup>th</sup> day of December, 2009.

  
\_\_\_\_\_  
Notary Public

