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BEFORE THE DEPARTMENT OF FINANCIAL PROTECTION AND INNOVATION  
OF THE STATE OF CALIFORNIA

In the Matter of:	)	CRD NO.: 107673
THE COMMISSIONER OF FINANCIAL PROTECTION AND INNOVATION,	)	STATEMENT OF ISSUES
Complainant,	)	
v.	)	
NEAL ALLEN PEPPER, PhD,	)	
Respondent.	)	

The Commissioner of Financial Protection and Innovation (Commissioner) is informed and believes, and based upon such information and belief, alleges and charges Respondent as follows:

**I.**

**Jurisdiction**

1. The Commissioner has jurisdiction over the licensing and regulation of persons and entities engaged in the business of investment advising under the Corporate Securities Law of 1968 (CSL) (Corp. Code, § 25000 et seq.). The Commissioner is authorized to administer and enforce the CSL and the rules and regulations promulgated under the CSL in title 10 of the California Code of Regulations (CCR).<sup>1</sup>

<sup>1</sup> Unless otherwise indicated, all further references to the California Code of Regulations are to title 10.



1           9.       On April 2 and 8, 2019, Pepper submitted incomplete responses to the report of  
2 examination. The responses provided virtually none of the requested corrective actions, which  
3 involved providing records, reports, and confirmations.

4           10.      On June 12, 2019, the Commissioner sent a letter to Pepper notifying him that his  
5 response was incomplete and requiring a written response no later than June 21, 2019, that  
6 addressed each section of the letter.

7           11.      On July 17, 2019, after not receiving a response from Pepper, the Commissioner sent  
8 a final 10-day demand letter requiring Pepper to submit a written response no later than July 27,  
9 2019.

10          12.      On July 25, 28, and 29 and August 7, 2019, Pepper submitted incomplete responses  
11 to the Commissioner’s July 17, 2019 final demand. The responses provided virtually none of the  
12 requested records, reports, or confirmations.

13          13.      On November 15, 2019, although Pepper had not yet submitted a complete response  
14 to the Commissioner’s July 17, 2019 final demand, the Commissioner sent another final 10-day  
15 demand letter requiring Pepper to submit a written response no later than November 25, 2019. The  
16 Commissioner informed Pepper that instead of submitting a complete response addressing all  
17 deficiencies, he could surrender his investment adviser certificate, cease business, and provide  
18 related written confirmations.

19          14.      On January 14, 2020, Pepper submitted an incomplete response in which he  
20 requested to be exempt from most of the CSL’s recordkeeping requirements, among other things.

21          15.      As a result of the examination, the Commissioner finds the following:

22                               **Failure to Maintain Books and Records and to File Reports**

23          16.      Pepper failed to prepare or maintain accurate or current accounting records,  
24 including a general ledger and income statements, in violation of Corporations Code section 25241,  
25 subdivision (a), and CCR section 260.241.3, subdivision (a)(1), (a)(2), and (a)(6).

26          17.      Pepper failed to prepare or maintain accurate or current bank statements and cash  
27 reconciliations in violation of Corporations Code section 25241, subdivision (a), and CCR section  
28 260.241.3, subdivision (a)(4).

1           18.     Pepper failed to prepare monthly and maintain records of the computations of the  
2 minimum financial requirements (MFR) of CCR section 260.237.2 in violation of Corporations  
3 Code section 25241, subdivision (a), and CCR section 260.241.3, subdivisions (a)(6) and (j). This  
4 failure prevented the Commissioner from determining whether Pepper’s net worth met or exceeded  
5 the MFR.

6           19.     Pepper failed to file annual financial reports within 90 days after his fiscal year end  
7 for fiscal years 2012, 2013, 2014, 2015, 2016, 2017, and 2018 in violation of Corporations Code  
8 section 25241, subdivision (a), and CCR section 260.241.2, subdivision (a)(2), (a)(3), and (a)(4).

9           20.     Pepper also failed to file accompanying verifications for each annual financial report  
10 in violation of Corporations Code section 25241, subdivision (a), and CCR section 260.241.2,  
11 subdivision (b).

12           21.     Pepper failed to file with the Investment Adviser Registration Depository (IARD)  
13 annual updating amendments to Part 2 of Form ADV (a brochure disclosing information about the  
14 investment adviser firm to clients and prospective clients) within 90 days after his fiscal year end  
15 for fiscal years 2012, 2013, 2014, 2015, and 2017 in violation of Corporations Code section 25241,  
16 subdivision (a), and CCR section 260.241.4, subdivision (e).

17           22.     Pepper failed to file a Form U4 (Uniform Application for Securities Industry  
18 Registration or Transfer) with the Central Registration Depository (CRD) and keep a copy in his  
19 records in violation of Corporations Code section 25241, subdivision (a), and CCR sections  
20 260.236.1, subdivision (a)(2), and 260.241.3, subdivision (a)(17).

21           **Investment Advisory Activities Not Promoting Fair, Equitable, and Ethical Principles**

22           23.     Pepper failed to keep written suitability information—namely, information  
23 concerning clients’ investment objectives, financial situations, or needs—regarding three clients in  
24 violation of Corporations Code section 25238 and CCR section 260.238, subdivision (a).

25           24.     Pepper entered into or renewed an investment advisory contract that did not disclose  
26 a flat advisory fee that was charged to the client in violation of Corporations Code section 25238  
27 and CCR section 260.238, subdivision (n).

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**Willful Violations**

25. Pepper willfully committed the violations described above. (See *ACCO Engineered Systems, Inc. v. Contractors’ State License Bd.* (2018) 30 Cal.App.5th 80, 87 [“willful” requires only showing of general intent to commit act, not specific intent to violate law]; *In re Stacy Ann Maspero* (Dept. of Corp., Jan. 13, 2003) No. L2002090534 [2003 WL 23634202 at p. \*6] [“willfully” implies purpose or willingness to act or omit to act and does not require intent to violate law].)

**III.**

**Commissioner’s Authority to Issue Order to Discontinue Violations and to Levy**

**Administrative Penalties**

26. Corporations Code section 25249 provides:

If, after examination or investigation, the commissioner has reasonable grounds to believe that any broker-dealer or investment adviser has violated any law or rule binding upon it, the commissioner shall, by written order addressed to the broker-dealer or investment adviser, direct the discontinuance of the violation. The order shall be effective immediately, but shall not become final except in accordance with the provisions of Section 25251.

27. Corporations Code section 25252 provides in relevant part:

The commissioner may, after appropriate notice and opportunity for hearing, by orders, levy administrative penalties as follows:

...

(b) Any broker-dealer or investment adviser that willfully violates any provision of this division to which it is subject, or that willfully violates any rule or order adopted or issued pursuant to this division and to which it is subject, is liable for administrative penalties of not more than five thousand dollars (\$5,000) for the first violation, not more than ten thousand dollars (\$10,000) for the second violation, and not more than fifteen thousand dollars (\$15,000) for each subsequent violation.

...

(d) The administrative penalties available to the commissioner pursuant to this section are not exclusive, and may be sought and employed in any combination with civil, criminal, and other administrative remedies deemed advisable by the commissioner to enforce the provisions of this division.

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IV.

Applicable Law

28. Corporations Code section 25238 provides:

No investment adviser licensed under this chapter and no natural person associated with the investment adviser shall engage in investment advisory activities, or attempt to engage in investment advisory activities, in this state in contradiction of such rules as the commissioner may prescribe designed to promote fair, equitable and ethical principles.

29. Corporations Code section 25241 provides in relevant part:

(a) Every broker-dealer and every investment adviser licensed under Section 25230 shall make and keep accounts, correspondence, memorandums, papers, books, and other records and shall file financial and other reports as the commissioner by rule requires, subject to the limitations of Section 15(h) of the Securities Exchange Act of 1934 with respect to broker-dealers and Section 222 of the Investment Advisers Act of 1940 with respect to investment advisers.

30. California Code of Regulations, title 10, section 260.236.1, provides in relevant part:

(a) The procedures set forth in this subsection are applicable to investment advisers licensed pursuant to Section 25230 of the Code. References to an investment adviser representative shall mean both an investment adviser representative and an associated person of an investment adviser, as those terms are defined in Section 25009.5(a) of the Code.

...

(2) Upon employment or engagement of an individual as an investment adviser representative, the investment adviser shall file Form U4 with CRD in accordance with its procedures, and pay the fee prescribed by Section 25608(p) for transmission to the Commissioner. Form U4, including any Disclosure Reporting Page(s), shall be completed in accordance with the form instructions. The filing of Form U4 with CRD does not constitute an automatic “approval” of the filing by the Commissioner. Investment advisers shall not consider an investment adviser representative “registration” with CRD approved until approved by the Commissioner and the approval has been received by CRD. If requested by the Commissioner, additional information, documentation or detail pertaining to Form U4 or the investment adviser representative’s compliance with the qualification requirements shall be filed directly with the Commissioner within 15 days from the date of the request. In accordance with Section 250.16, Form U4 may be abandoned if the Commissioner does not receive the requested information within the time prescribed. The Commissioner shall “reject” with CRD an abandoned Form U4.

31. California Code of Regulations, title 10, section 260.237.2, provides in relevant part:

(a) Every investment adviser who has custody of client funds or

1 securities shall maintain at all times a minimum net worth of \$35,000,  
2 and every investment adviser who has discretionary authority over  
3 client funds or securities but does not have custody of client funds or  
4 securities, shall maintain at all times a minimum net worth of \$10,000.

5 ...

6 (j) For purposes of subsection (c) of this rule, if the failure to discover  
7 that an investment adviser’s net worth is less than the minimum required  
8 is the result of the investment adviser’s failure to keep true, accurate and  
9 current the books and records required under Section 260.241.3, the  
10 investment adviser will be deemed to have discovered that the  
11 investment adviser’s net worth is less than the minimum required by this  
12 section.

13 32. California Code of Regulations, title 10, section 260.238, provides in relevant part:

14 The following activities do not promote “fair, equitable or ethical  
15 principles,” as that phrase is used in Section 25238 of the Code:

16 (a) Recommending to a client to whom investment supervisory,  
17 management or consulting services are provided the purchase, sale or  
18 exchange of any security without reasonable grounds to believe that the  
19 recommendation is suitable for the client on the basis of information  
20 furnished by the client after reasonable inquiry concerning the client’s  
21 investment objectives, financial situation and needs, and any other  
22 information known or acquired by the adviser after reasonable  
23 examination of such of the client’s records as may be provided to the  
24 adviser.

25 ...

26 (n) Entering into, extending or renewing any investment advisory  
27 contract, other than a contract for impersonal advisory services, unless  
28 such contract is in writing and discloses, in substance, the services to be  
provided, the term of the contract, the advisory fee or the formula for  
computing the fee the amount or the manner of calculation of the  
amount of the prepaid fee to be returned in the event of contract  
termination or nonperformance, whether the contract grants  
discretionary power to the adviser or its representatives.

33. California Code of Regulations, title 10, section 260.241.2, provides in relevant part:

(a) General Rule. Subject to the provisions of subsection (c) of this  
section, every licensed broker-dealer, and every licensed investment  
adviser subject to the provisions of Section 260.237.2 of these rules,  
shall file an annual financial report, as follows:

...

(2) The annual report for an investment adviser shall contain a balance  
sheet, income statement, and computations of the minimum financial  
requirements required under Section 260.237.2 of these rules.

(3) The financial statements included in the annual report shall be

1 prepared in accordance with generally accepted accounting principles  
2 and shall be audited by either an independent certified public accountant  
3 or independent public accountant; provided, however, the financial  
4 statements need not be audited if:

5 The broker-dealer or investment adviser has not held or accepted  
6 custody of funds and securities for or owed money or securities to  
7 customers or clients during the period covered by the report; and

8 (A) if the licensee is a broker-dealer, the securities business has been  
9 limited to soliciting subscriptions for securities of an issuer and the  
10 broker-dealer promptly forwarded the subscriptions to the issuer,  
11 underwriter, sponsor or other distributor of the securities and received  
12 checks, drafts, notes or other evidence of indebtedness payable solely to  
13 the issuer, underwriter, sponsor or distributor who delivered the  
14 securities purchased directly to the subscriber; and

15 (B) if the licensee is an investment adviser, the investment adviser only  
16 has discretionary authority over client funds or securities, the  
17 investment adviser has taken only limited powers of attorney to execute  
18 transactions on behalf of its clients, or the investment adviser does not  
19 accept prepayment of more than \$500 per client for more than six  
20 months in advance; or

21 (C) as otherwise permitted by the Commissioner.

22 (4) The report shall be filed not more than 90 days after the investment  
23 adviser or broker-dealer's fiscal year end.

24 . . .

25 (b) Verification of Reports. Attached to each financial report filed with  
26 the Commissioner shall be a verification that, to the best knowledge and  
27 belief of the person making the verification,

28 (1) the financial statements and supporting schedules are true and  
correct, and

(2) neither the broker-dealer nor any partner, officer, or director thereof  
has any proprietary interest in any account classified solely as that of a  
customer. If the broker-dealer or investment adviser is a sole  
proprietorship, the verification shall be made by the proprietor; if a  
partnership, by a general partner; or if a corporation, by a duly  
authorized officer.

34. California Code of Regulations, title 10, section 260.241.3, provides in relevant part:

(a) Every licensed investment adviser shall make and keep true, accurate  
and current the following books and records relating to such person's  
investment advisory business:

(1) A journal or journals, including cash receipts and disbursements  
records, and any other records of original entry forming the basis of  
entries in any ledger.



1 (2) General and auxiliary ledgers (or other comparable records)  
2 reflecting asset, liability, reserve, capital, income and expense accounts.

3 ...

4 (4) All check books, bank statements, cancelled checks and cash  
5 reconciliations of the investment adviser.

6 ...

7 (6) All trial balances, financial statements, worksheets that contain  
8 computations of minimum financial requirements required under  
9 Section 260.237.2, of these rules, and internal audit working papers  
10 relating to the business of such investment adviser.

11 ...

12 (17) For investment advisers filing through IARD, copies, with original  
13 signatures of the investment adviser’s appropriate signatory and the  
14 investment adviser representative, of each initial Form U4.

15 ...

16 (j) Any investment adviser who is subject to the minimum financial  
17 requirements of Section 260.237.2 shall, in addition to the records  
18 otherwise required under this section, maintain a record of the proof of  
19 money balances of all ledger accounts in the form of trial balances and  
20 a record of the computations of minimum net worth pursuant to Section  
21 230.237.2 of these rules (as of the trial balance date). The trial balances  
22 and computations shall be prepared currently at least once a month.

23 35. California Code of Regulations, title 10, section 260.241.4, provides in relevant part:

24 (e) A licensed investment adviser shall file an annual updating  
25 amendment, in accordance with the instruction in Form ADV, with  
26 IARD in accordance with its procedures for transmission to the  
27 Commissioner within ninety (90) days of the end of the investment  
28 adviser’s fiscal year.

**V.**

**Prayer**

For the foregoing reasons, the Commissioner finds that Pepper willfully engaged in investment advisory activities not promoting fair, equitable, and ethical principles in violation of Corporations Code section 25238 and related provisions of the California Code of Regulations.

The Commissioner also finds that Pepper willfully failed to keep or maintain books and records and to file reports in violation of Corporations Code section 25241, subdivision (a), and related provisions of the California Code of Regulations.

1           Accordingly, the Commissioner, having grounds to issue an order to discontinue violations  
2 under Corporations Code section 25249, has issued an Order to Discontinue Violations directing  
3 Neal Pepper, PhD, to discontinue violating Corporations Code sections 25238 and 25241,  
4 subdivision (a), and CCR sections 260.236.1, subdivision (a)(2); 260.238, subdivisions (a) and (n);  
5 260.241.2, subdivisions (a)(2), (a)(3), (a)(4), and (b); 260.241.3, subdivisions (a)(1), (a)(2), (a)(4),  
6 (a)(6), (a)(17), and (j); and 260.241.4, subdivision (e). Such an order is necessary and appropriate in  
7 the public interest and for the protection of investors.

8           Additionally, the Commissioner has grounds to issue an order levying administrative  
9 penalties under Corporations Code section 25252. Such an order is necessary and appropriate in the  
10 public interest and for the protection of investors.

11           WHEREFORE, IT IS PRAYED that the Order to Discontinue Violations be made final and  
12 that an order levying administrative penalties be issued against Neal Pepper, PhD, in the amount of  
13 \$15,000.00, consisting of \$5,000.00 for the violation of Corporations Code section 25238 and  
14 \$10,000.00 for the violation of section 25241, subdivision (a).

15 Dated: December 2, 2020  
16           Los Angeles, California

MANUEL P. ALVAREZ  
Commissioner of Financial Protection and Innovation

17  
18 By: \_\_\_\_\_  
19 SAMUEL J. PARK  
20 Counsel  
21 Enforcement Division  
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