



CERTIFIED FINANCIAL PLANNER BOARD OF STANDARDS, INC.

CONFLICTS OF INTEREST BETWEEN CFP® PROFESSIONALS AND CLIENTS

I. Background

In their day-to-day business, it is not uncommon for CFP® professionals to face decisions about whether a particular action or circumstance constitutes a conflict of interest. In response to recent increases in the number of conflict of interest cases reviewed by CFP Board, CFP Board presents this Advisory Opinion to provide guidance to CFP® professionals concerning conflicts of interest in order to help CFP® professionals address conflicts of interest in compliance with CFP Board's *Standards of Professional Conduct* ("Standards").

II. Issue: Conflicts of Interests Between CFP® Professionals and Clients

- i. What constitutes a conflict of interest under CFP Board's definition of conflicts of interest?
- ii. How and when should a CFP® professional disclose a conflict of interest to a client or prospective client?

III. Rules

CFP Board defines "conflict of interest" in the Terminology section of the *Standards*, which states that a conflict of interest exists when a CFP® professional's financial, business, property and/or personal interests, relationships or circumstances reasonably may impair his/her ability to offer objective advice, recommendations or services. Several *Rules of Conduct* are related to this definition:

- Rule 1.4 requires that a CFP® professional shall at all times place the interest of the client ahead of his or her own. When the CFP® professional provides financial planning or material elements of financial planning, the CFP® professional owes to the client the duty of care of a fiduciary as defined by CFP Board.
- Rule 2.2(b) requires a CFP® professional to disclose to a prospective client or client a general summary of likely conflicts of interest between the client and the CFP® professional, the CFP® professional's employer or any affiliates or third parties, including, but not limited to, information about any familial, contractual or agency relationship of the CFP® professional or the CFP® professional's employer that has a potential to materially affect the relationship. Further, Rule 2.2 also imposes an ongoing obligation to disclose any conflicts of interest that arise during the course of the CFP® professional-client relationship.

- Rule 4.1 requires a CFP® professional to treat prospective clients and clients fairly and provide professional services with integrity and objectivity.

IV. Analysis

- i. What constitutes a conflict of interest under CFP Board's definition?

According to CFP Board's definition, a conflict of interest exists when a CFP® professional's financial, business, property and/or personal interests, relationships or circumstances reasonably may impair his/her ability to offer objective advice, recommendations or services. There are two key phrases in CFP Board's definition of a conflict of interest.

The first key phrase is "financial, business, property and/or personal interests, relationships or circumstances." These terms include not only pecuniary interests, but also familial interests and relationships, the motive to obtain professional or personal advancement or reputational benefits, such as the ability to develop or maintain a relationship with an individual or entity. For example, if the CFP® professional recommends that a client purchase a private placement not because he or she will earn money from the recommendation but because he or she seeks a relationship with the issuer or underwriter of the private placement, that is a conflict of interest.

The second key phrase is "reasonably may impair his/her ability to offer objective advice, recommendations or services." First, CFP® professionals should carefully consider whether their interests may impair their ability to offer objective advice, recommendations or services. Loyalty and independent judgment are essential elements of a CFP® professional's relationship with a client. CFP® professionals should clearly identify each client they are working with and determine whether the client may have any interests that conflict with the CFP® professional or the CFP® professional's other clients. For example, a CFP® professional who advises owners of a business personally and serves as the adviser for the business may have a conflict of interest as the interests of the business may diverge from the interests of an individual owner or the individual owners' relationship may become adversarial.

The second key phrase does not require that the conflict of interest actually manifest itself. Rather, this definition indicates that a conflict occurs anytime "financial, business, property and/or personal interests, relationships or circumstances reasonably may," or have the potential to, impair the CFP® professional's ability to offer objective advice, recommendations or services. For example, if a CFP® professional enters into a transaction to purchase a home from a client, there is a conflict that may impair the CFP® professional's ability to offer objective advice. The CFP® professional's ability to offer objective advice, recommendations or services may not actually be impaired, but there is the potential for the conflict of interest to impair the CFP® professional's ability to offer objective advice, recommendations or services.

- ii. When and how should a CFP® professional disclose a conflict of interest to a client?

Rule 2.2 requires a CFP® professional to disclose conflicts of interest to a client. If the conflict is apparent at the initiation of the relationship, the CFP® professional should disclose the conflict at that time. If the conflict arises later in the relationship, the disclosure should be made promptly. Generally, CFP Board will consider a disclosure to be prompt if made within 30 days of the date the CFP® professional knew or should have known about the conflict of interest, unless notification prior to 30 days was necessary to avoid an adverse consequence to a client.

CFP Board's rules require CFP® professionals providing financial planning services to disclose all conflicts in writing. While CFP® professionals who are not providing financial planning services may make conflict disclosures orally, CFP Board encourages CFP® professional to make all disclosures in writing.

After disclosing the conflict of interest to the client, the CFP® professional may want to consider obtaining written consent from the client in which the client acknowledges the conflict of interest and consents to move forward in the CFP® professional-client relationship despite the conflict of interest. CFP® professionals need to consider, however, that some conflicts of interest may be such that the client is not protected by the disclosure and the CFP® professional will not be able to offer objective advice, recommendations or services. In these instances, the CFP® professional should end the client relationship.

The examination of several case studies will be instructive to the CFP® professional in navigating conflict of interest situations.

Case Study 1: Conflicts of Interest When Dealing With Multiple Clients

Husband and Wife retained a CFP® professional to represent the couple's combined interests, although the majority of the assets in the couple's portfolio were brought to the marriage by Husband. The CFP® professional advised the couple to invest the majority of the assets (over a million dollars) in an IRA in Husband's name only, with the Wife as beneficiary. The CFP® professional also recommended that the residue of the couple's assets be placed in a joint checking account, to address short and medium term income needs and cash management. Because the couple was happily married at the time, this did not pose an immediate problem. Wife claimed she never knew there was a separation of ownership of the couple's assets into two separate accounts as the CFP® professional had always corresponded with Husband and Wife regarding both accounts.

Several years later, the couple began experiencing marital difficulties and started divorce proceedings. After divorce proceedings began, Wife wrote a check in an attempt to withdraw almost all of the funds from the joint account. CFP® professional immediately contacted Husband and informed him that Wife was attempting to remove all of the money from the joint account and asked him if was willing to sell securities to

cover the check. Husband indicated that he was not, and the CFP® professional directed the bank not to process the check. When Wife inquired as to whether the check had cleared, CFP® professional represented to Wife that the check had cleared. The CFP® professional did not inform Wife that he had contacted Husband and that Husband had refused to sell any securities to allow the check to clear.

The CFP® professional violated Rules 1.4, 4.1 and 4.4 by failing to: 1) communicate with both clients appropriately regarding conflicts in representing both of them after he became aware of a potential divorce; and 2) appropriately respond to Wife's inquiries and subsequent check processing by failing to inform her that Husband refused to consent to the sale of investments to cover the check. When the couple's interests diverged, a conflict of interest developed between Wife and the CFP® professional due to the CFP® professional's relationship with Husband, which caused the CFP® professional to favor Husband. The CFP® professional should have consulted his compliance department and disclosed the potential conflict with his clients.

Case Study 2: Referral Conflict of Interest

A CFP® professional owned a dually registered firm with investment advisory and broker-dealer divisions. The CFP® professional, in his capacity as a registered representative, referred clients to the investment advisory division of his firm. The CFP® professional did not disclose to clients that: 1) the divisions were related and that the clients could use investment advisory services from other firms; and 2) the CFP® professional had a conflict of interest in referring clients to the investment advisory division because he stood to obtain additional compensation through the firm's receipt of investment advisory fees.

The CFP® professional violated Rules 1.4 and 2.2(b). The CFP® professional should have disclosed the conflict of interest due to the related party status of his firm's investment advisory division and clearly advised clients that they had the opportunity to seek investment advisory services from an unrelated firm.

Case Study 3: Financial Conflict of Interest

A CFP® professional served as the president and owner of an investment advisory firm and had primary responsibility for the financial and investment services offered by the firm. The firm held a private offering to raise money for working capital, marketing, expansion of present facilities, and operating expenses. The CFP® professional recommended that clients purchase shares in the private offering. Four clients purchased \$2,550,000 worth of shares of the firm, which represented 12.5% of the company.

The CFP® professional violated Rules 1.4 and 2.2(b). The CFP® professional's sale of interests in his firm constituted a conflict of interest. The conflict arose due to the CFP® professional's status as the owner of the firm and an investment adviser to the clients who purchased an interest in the firm. The CFP® professional should have made clear disclosures regarding the potential conflict prior to making the sale and encouraged the clients to seek out another adviser with respect to that transaction.

V. Conclusion

CFP® professionals should carefully evaluate the potential for conflicts of interest in each client relationship. If a conflict of interest exists, the CFP® professional should evaluate whether he/she can continue to advise the client without impairing his/her ability to offer objective advice, recommendations or services. In all cases, the CFP® professional must disclose the conflict. If the CFP® professional believes he/she can offer objective advice despite the conflict, the CFP® professional should obtain the client's informed written consent to the conflict. If, on the other hand, the CFP® professional believes he/she cannot continue to offer objective advice because of the conflict, the CFP® professional should end the client relationship.