CFP BOARD

GUIDE TO SATISFYING THE DUTY OF CARE

WHEN PROVIDING FINANCIAL ADVICE THAT DOES NOT REQUIRE FINANCIAL PLANNING

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GUIDE TO SATISFYING THE DUTY OF CARE

A cornerstone of the *Code of Ethics and Standards of Conduct* (*Code and Standards*) is the Fiduciary Duty that applies whenever a CFP® professional is providing Financial Advice to a Client. (Standard A.1.) To act as a fiduciary and, therefore, act in the best interests of the Client, a CFP® professional must fulfill the Duty of Loyalty, the Duty of Care, and the Duty to Follow Client Instructions. This guide describes the process by which a CFP® professional may satisfy the Duty of Care when providing Financial Advice that does not require Financial Planning.

To fulfill the Duty of Care, a CFP® professional must exercise the care, skill, prudence, and diligence that a prudent professional would exercise in light of the Client's goals, risk tolerance, objectives, and financial and personal circumstances. A CFP® professional may satisfy this requirement by implementing a process that enables the CFP® professional to act in the best interests of the Client when providing Financial Advice.

CFP® professionals are familiar with process requirements. When a CFP® professional provides or agrees to provide Financial Advice that requires Financial Planning, a CFP® professional must follow the *Practice Standards for the Financial Planning Process* (*Practice Standards*) set forth in Section C of the *Code and Standards*. The process that the *Practice Standards* provides for Financial Planning is a further articulation of the Duty of Care that applies to Financial Planning.

What Is the Difference between Financial Advice and Financial Planning?

Financial Advice

A A communication that, based on its content, context, and presentation, would reasonably be viewed as a recommendation that the Client take or refrain from taking a particular course of action with respect to:

1. The development or implementation of a financial plan;
2. The value of or the advisability of investing in, purchasing, holding, gifting, or selling Financial Assets;
3. Investment policies or strategies, portfolio composition, the management of Financial Assets, or other financial matters; or
4. The selection and retention of other persons to provide financial or Professional Services to the Client; or

B The exercise of discretionary authority over the Financial Assets of a Client.

Financial Planning

A collaborative process that helps maximize a Client's potential for meeting life goals through Financial Advice that integrates relevant elements of the Client's personal and financial circumstances.

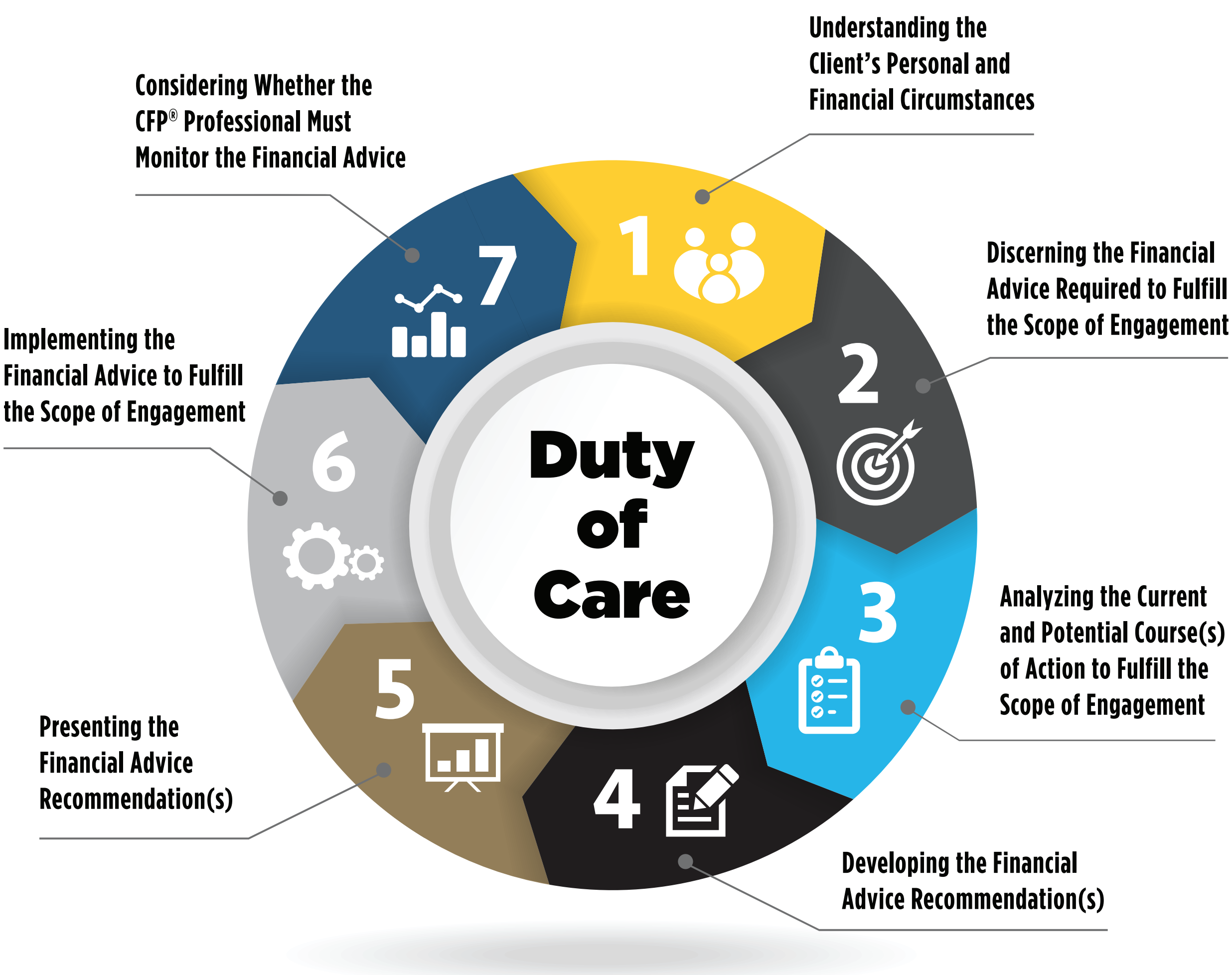
A reference in this guide to "Financial Advice" is to Financial Advice that <u>does not</u> require Financial Planning, and a reference to "Financial Planning" is to Financial Advice that <u>does</u> require Financial Planning.

The Duty of Care process that applies to Financial Advice that does not require Financial Planning is similar to the Duty of Care process set forth in the *Practice Standards*. However, there are significant differences in the depth and scope of what is required. More specifically, the information that a CFP® professional must obtain and analyze, and the breadth of that analysis, typically is greater for Financial Planning than it is for Financial Advice. Similarly, what the Duty of Care requires will depend upon the facts and circumstances and the Financial Advice being provided.

The process for satisfying the Duty of Care when providing Financial Advice that does not require Financial Planning is set forth below. To better enable CFP® professionals to understand how this process relates to the *Practice Standards*, CFP Board has set forth the process for satisfying the Duty of Care when providing Financial Advice in seven steps and compared this process to the Financial Planning process set forth in the *Practice Standards*.

If a CFP® professional does not follow this process, it will be difficult to comply with the Duty of Care that the *Code and Standards* requires. CFP Board will be designing case studies that apply this process to various factual circumstances.

7 Steps: Duty of Care Process for Financial Advice



UNDERSTANDING THE CLIENT'S PERSONAL AND FINANCIAL CIRCUMSTANCES

STEP 1

The CFP® professional must:

- Obtain quantitative and qualitative information
- Analyze information
- Address incomplete information

When providing Financial Advice, a CFP® professional must determine what information is necessary to fulfill the Scope of Engagement in the best interests of the Client. As with Financial Planning, a CFP® professional providing Financial Advice must collaborate with the Client to obtain that information. The information that a CFP® professional needs usually is more extensive for Financial Planning than it is for Financial Advice.

What Information to Gather

The *Practice Standards* in the *Code and Standards* provides examples of the qualitative and quantitative information that may be needed to fulfill a Scope of Engagement for Financial Planning. When the Scope of Engagement is for Financial Advice, the information that a CFP® professional needs to provide Financial Advice in the Client's best interests likely will be more limited. Nevertheless, the examples set forth in Standard C.1.a. of the *Code and Standards* are helpful to consider.

Examples of qualitative or subjective information may include:

☐ Client's health	☐ Attitudes	☐ Goals
☐ Life expectancy	☐ Expectations	☐ Needs
☐ Family circumstances	☐ Earnings potential	☐ Priorities
☐ Values	☐ Risk tolerance	☐ Current course of action

Examples of quantitative or objective information may include:

☐ Client's age	☐ Savings	☐ Government benefits
☐ Dependents	☐ Assets	☐ Insurance coverage
☐ Other professional advisors	☐ Liabilities	☐ Estate plans
☐ Values	☐ Available resources	☐ Capacity for risk
☐ Income	☐ Liquidity	☐ Education and retirement accounts and benefits
☐ Expenses	☐ Taxes	
☐ Cash flow	☐ Employee benefits	

A CFP® professional must then analyze the qualitative and quantitative information to assess the Client's personal and financial circumstances that are relevant to the Scope of Engagement.

The CFP® professional always should ask the Client for any information needed to fulfill the Scope of Engagement, including additional information the CFP® professional needs after reviewing the information the Client initially provided. If unable to obtain information necessary to fulfill the Scope of Engagement, then the CFP® professional may not be able to provide Financial Advice in the best interests of the Client. The CFP® professional may need to limit the Scope of Engagement or terminate the Engagement. The CFP® professional must inform the Client of any such limitations. For example, if a Client asks for Financial Advice regarding the tax implications of selling a particular investment but does not provide tax statements the CFP® professional needs to complete the analysis, then the CFP® professional should inform the Client that the CFP® professional needs the information to fulfill the Scope of Engagement, and if the Client does not provide the information, then limit the Scope of Engagement to Financial Advice the CFP® professional is able to provide or terminate the Engagement.

STEP 2 DISCERNING THE FINANCIAL ADVICE REQUIRED TO FULFILL THE SCOPE OF ENGAGEMENT

The CFP® professional must understand the Scope of Engagement and the Financial Advice required to fulfill the Scope of Engagement.

Depending upon the Scope of Engagement, the CFP® professional may need to:

- Identify potential goals
- Help Clients select and prioritize goals

When providing Financial Planning, the *Practice Standards* require a CFP® professional to help the Client identify, select, and prioritize goals. Financial Advice is narrower in scope than Financial Planning and may not require goal setting and prioritizing. However, a CFP® professional must understand the Scope of Engagement and the Financial Advice needed to fulfill the Scope of Engagement.

STEP 3

ANALYZING THE CURRENT AND POTENTIAL COURSE(S) OF ACTION TO FULFILL THE SCOPE OF ENGAGEMENT

The CFP® professional must:

- Analyze the Client's current course of action
- Analyze potential alternative courses of action

When providing Financial Planning, a CFP® professional is required to analyze the Client's current course of action and, where appropriate, potential alternative course(s) of action to help maximize the potential for meeting the Client's goals. When providing Financial Advice that does not require Financial Planning, a CFP® professional also must analyze the Client's current course of action to determine whether any action is required. If so, then the CFP® professional must consider and analyze the reasonably available alternative courses of action, including the material advantages and disadvantages of each alternative as they relate to the Client's needs and circumstances. The breadth and scope of this requirement generally is more limited when providing Financial Advice than when providing Financial Planning, because with Financial Planning, a CFP® professional also must consider how each alternative course of action integrates the relevant elements of the Client's personal and financial circumstances and helps to maximize the potential for the Client to meet the Client's Financial Planning goals. With Financial Advice, a CFP® professional may focus more narrowly on the goals of the specific Financial Advice that is the subject of the Scope of Engagement.

The potential course of action that emerges from this analysis may include specific actions, products, and/or services (including account types) that are reasonably available from which the CFP® professional will choose a proposed course of action to recommend to the Client.

When a CFP® Professional's Firm's Offers Proprietary or Other Limited Product Menus, or Limited Account Types

Reasonably available courses of action are those that are accessible to the CFP® professional through ordinary and usual means at a reasonable cost to the Client. A CFP® professional is not required to recommend a course of action that is not available to the CFP® professional because, for example, a CFP® Professional's Firm may only allow recommendations of proprietary or other limited ranges of products or accounts. However, a CFP® professional may limit a recommendation of a course of action to those available through the CFP® Professional's Firm only if the course of action is in the Client's best interests. What is in the Client's best interests will depend on the Financial Advice required to fulfill the Scope of Engagement.

A CFP® professional does not have to be familiar with or evaluate every possible course of action, either offered outside of the CFP® Professional's Firm or available on the firm's platform. Instead, a CFP® professional must review possible courses of action that a prudent professional would evaluate under the facts and circumstances at the time of the recommendation.

If the CFP® professional determines that none of the reasonably available courses of action would be in the Client's best interests, then the CFP® professional would not be able to recommend them to the Client. Importantly, a CFP® professional cannot use the CFP® Professional's Firm's limited product menu to justify recommending a course of action that is not in the Client's best interests. Under such circumstances, the CFP® professional must decline to offer the Financial Advice.

When assessing reasonably available alternatives to determine which is/are in the Client's best interests, a CFP® professional who does not anticipate assisting the Client with implementation or monitoring should consider the extent to which the Client is able to implement or monitor the Financial Advice without assistance from the CFP® professional or another competent professional. A CFP® professional must exercise the judgment that a reasonable CFP® professional would exercise in evaluating a Client's ability to implement and monitor the Financial Advice without professional assistance. In doing so, the CFP® professional must evaluate the Client's experience and financial knowledge and the complexity of the Financial Advice. The less experienced or financially knowledgeable a Client and the more complex the Financial Advice, the more likely it is that the Client will not be able to implement or monitor the Financial Advice without competent professional assistance.

The Importance of Competency. The *Code and Standards* sets forth 15 Duties to Clients, all of which apply when a CFP® professional is providing Financial Advice. One of these is the Duty of Competency, which is found in Standard A.3.:

> A CFP® professional must provide Professional Services with competence, which means with relevant knowledge and skill to apply that knowledge. When the CFP® professional is not sufficiently competent in a particular area to provide the Professional Services required under the Engagement, the CFP® professional must gain competence, obtain the assistance of a competent professional, limit or terminate the Engagement, and/or refer the Client to a competent professional. The CFP® professional shall describe to the Client any requested Professional Services that the CFP® professional will not be providing.

A CFP® professional must be knowledgeable about the available courses of action, and whether (and how) they meet the Client's needs. For example, when recommending an investment product, a CFP® professional must be knowledgeable about the product features, costs (including fees), risk, comparative rate of return, maturity, liquidity, payout events, and other factors. A CFP® professional also must have the skill to determine how the product fits the Client's circumstances, consistent with the Scope of the Engagement.

STEP 4

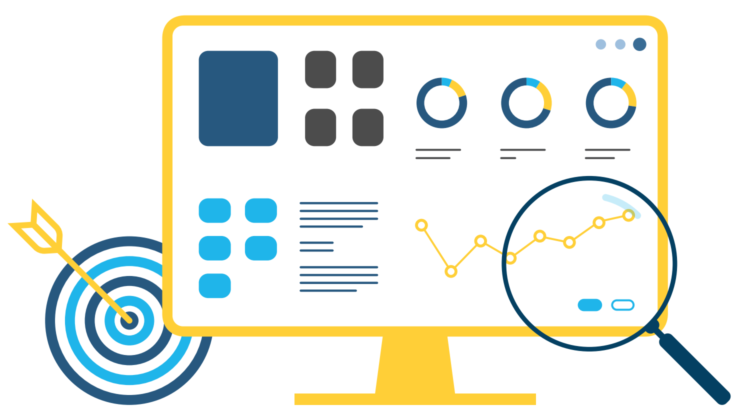
DEVELOPING THE FINANCIAL ADVICE RECOMMENDATION(S)

For each recommendation, the CFP® professional must:

- Determine which of the reasonably available alternative courses of action satisfy the Duty of Care and thus may be prudently recommended to the Client

When developing a Financial Advice recommendation, a CFP® professional must determine which of the reasonably available alternatives satisfy the Duty of Care and thus may be prudently recommended to the Client. A CFP® professional must consider how the course of action is designed to fulfill the Scope of Engagement, and the advantages and disadvantages of the course of action relative to reasonably available alternatives. There may be more than one option that will satisfy the CFP® professional's Fiduciary Duty to act in the best interests of the Client, including the Duty of Care. If so, then a CFP® professional may recommend from any of these options.

The factors that a CFP® professional must consider in making a Financial Advice recommendation are not as expansive as those for a Financial Planning recommendation. This is because the depth and breadth of Financial Advice is narrower than that of Financial Planning. Financial Advice is, by definition, advice that does not require an examination of all of the Client's goals or the integration of all of the Client's personal and financial circumstances. Other factors that a CFP® professional must consider when providing Financial Planning, such as the timing and scope of the recommendation, and whether the recommendation is independent or must be implemented with another recommendation, also may not be relevant to a Financial Advice Engagement. Nevertheless, a CFP® professional must consider the assumptions and estimates used to make the recommendation and how the recommendation is designed to maximize the Client's potential for meeting the goals of the Financial Advice.



STEP 5

PRESENTING THE FINANCIAL ADVICE RECOMMENDATION(S)

The CFP® professional must:

- Present to the Client the selected recommendation(s) and information that the CFP® professional was required to consider when developing the recommendation(s)

With Financial Advice, a CFP® professional's work developing the recommendation and implementing the recommendation may occur contemporaneously. However, in some instances, a CFP® professional providing Financial Advice may not be implementing that Financial Advice. In such instances, a CFP® professional presenting a Financial Advice recommendation, like a CFP® professional presenting a Financial Planning recommendation, must present to the Client the selected recommendations and the basis for the recommendations.

STEP 6

IMPLEMENTING THE FINANCIAL ADVICE TO FULFILL THE SCOPE OF ENGAGEMENT

If the CFP® professional has implementation responsibility, then the CFP® professional must:

- Identify, analyze, and select courses of action for implementation
- Recommend one or more courses of action for implementation
- Select and implement courses of action

Implementation of Financial Advice and Financial Planning is very similar. If the Scope of Engagement includes implementation responsibilities, then a CFP® professional must identify courses of action designed to implement the recommendations, and then determine which of the reasonably available alternatives satisfy the Duty of Care and thus may be prudently recommended to the Client. A CFP® professional must consider how the course of action that would implement the recommendations is designed to fulfill the Scope of Engagement, and the advantages and disadvantages of the course of action relative to reasonably available alternatives. A CFP® professional may not cause the Client to incur excessive cost or be exposed to excessive risk relative to comparable, reasonably available alternatives.

A CFP® professional with implementation responsibilities must recommend one or more course of action to the Client. If there is more than one reasonably available alternative that satisfies the Duty of Care and thus may be prudently recommended, then a CFP® professional could recommend any of those alternatives as being in the best interest of the Client. If the Client requests it, then the CFP® professional also must discuss with the Client the basis for selecting a course of action. A CFP® professional also must disclose and manage any Material Conflicts of Interest concerning the course of action.

If a CFP® professional is implementing a Financial Advice (or Financial Planning) recommendation made by another financial professional, then the CFP® professional must:

Help the Client select and implement the courses of action and discuss with the Client any recommendation that deviates from the Financial Advice (or Financial Planning) recommendation.

Document to Demonstrate Compliance. A CFP® professional should consider, as a best practice, maintaining documents or providing documents to Clients that demonstrate compliance with the *Code and Standards*, even when not explicitly required by law, regulation, or the *Code and Standards*. For example, when recommending alternatives that expose a Client to costs that are higher or risks that are greater than other reasonably available alternatives, a CFP® professional should consider documenting the basis for the recommendation, including why it was in the best interests of the Client. A CFP® professional must comply with any legal or regulatory requirements, including with respect to documenting recommendations. CFP® professionals also should be mindful of the Duty to Provide Information to a Client in writing, as set forth in Standard A.10.b. of the *Code and Standards*, when providing or required to provide Financial Planning.

STEP 7

CONSIDERING WHETHER THE CFP® PROFESSIONAL MUST MONITOR AND UPDATE THE FINANCIAL ADVICE

If the CFP® professional has monitoring and updating responsibilities, then the CFP® professional must:

- Monitor to see if circumstances warrant a change or update, and update as appropriate

The Duty of Care generally does not encompass a duty to monitor Financial Advice. Whether the CFP® professional is required to monitor the Financial Advice and update recommendations will depend on the Scope of Engagement and the legal standards that apply to the Financial Advice. For example, a CFP® professional who is engaged to provide a one-time recommendation of a life insurance policy or 529 Savings Plan generally would not have an obligation to monitor the Financial Advice (unless the Scope of Engagement provided otherwise), while a CFP® professional who is engaged to provide ongoing portfolio management on a discretionary basis would be required to monitor and update the Financial Advice (as required by applicable law).

When a CFP® professional has a duty to monitor and update (by virtue of a legal obligation or because of the Scope of Engagement), the Duty of Care requires the CFP® professional to skillfully and diligently monitor the Financial Advice provided to determine whether a change in circumstances warrants an update to the recommendations, and update as appropriate.

CFP BOARD

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