

April 23, 2007

Certified Financial Planner Board of Standards, Inc.
ATTN: Ethics Task Force
1670 Broadway, Suite 600
Denver, CO 80202-4809

On behalf of the NAPFA Board of Directors, we are submitting our comments to you and the CFP Board regarding the *Second Exposure Draft*. We appreciated the opportunity to present comments to the CFP Board at the Denver meeting on March 30, 2007. These remarks reinforce our overall support of the CFP Board's *Second Exposure Draft* which we expressed at that time.

In our September 2005 comments we addressed four primary areas of concern with our comments on the *First Exposure Draft* of the CFP Board's revised Code of Ethics. These were:

1. changes to the definition of "Fee-Only";
2. the optional fiduciary standard for a CFP certificant;
3. the aspirational nature of the Code; and
4. the terminology used in Section 6 reflecting a suitability standard rather than a fiduciary standard.

We are pleased that the CFP Board has effectively addressed these concerns in its *Second Exposure Draft*.

"Fee-Only" Definition. The revised definition of "fee-only" effectively reinstates the prior definition of "fee-only" set forth in the original Code of Ethics. At the March 30, 2007 conference the CFP Board Task Force members responded to a host of questions on this issue, and it became clear that "fee-only" compensation under the new definition excludes the receipt, *directly or indirectly*, of anything other than fees based upon an hourly fee, retainer fee, flat fee, or percentage of assets under management, either by the CFP® Certificant and/or by his or her firm and/or his or her business partner (if such receipt would in any way affect the compensation or profits of the CFP® Certificant).

While we have always expressed our view that fee-only compensation methods best avoid the conflicts of interest which financial planners may face, we do not suggest that "fee-only" compensation removes all conflicts of interest between a CFP® Certificant and his or her client. Full disclosure and proper management of compensation-related conflicts of interest is still required as a result of CFP® Certificant's fiduciary status. We thank the CFP Board for recognizing, however, that the definition of "fee-only" has achieved a certain meaning in the world of the financial consumer and in the profession, and we are pleased to see this meaning preserved by the *Second Exposure Draft*.

We do suggest that the CFP Board clarify, in its issuing release or through subsequent interpretations, that the receipt of certain soft-dollar compensation by CFP® Certificants does not negate "fee-only" status. For example, it is common for custodian firms (Schwab, TD Ameritrade, Fidelity, etc.) to provide a range of services to registered investment adviser firms (including those composed of CFP® Certificants), including access to electronic trading systems,

duplicate trade confirmations and materials, and research. In addition, some of these custodial firms host annual conferences at which education is provided at reduced fees, or for no fees, paid by CFP® Certificants who attend such conferences. These services and educational events have long occurred in the registered investment advisory community, and it is not possible under currently adopted systems for CFP® Certificants to pay for these services directly. Until such time as this system of soft dollar compensation is repealed (which would take action by the U.S. Congress), we suggest that the CFP Board require full disclosure of such indirect compensation to CFP® Certificants, but clarify that the receipt of such compensation does not impact the “fee-only” status of the CFP® Certificant. The definition of “Commission” in the *Second Exposure Draft* could be modified in order to exclude from such definition the receipt of indirect soft dollar compensation, provided that such compensation is fully disclosed to the CFP® Certificant’s clients.

The Best Interests Standard. In the *Second Exposure Draft*, the CFP Board proposes to adopt the best interests standard at all times for CFP® Certificants, stating in the first sentence of Rule 1.4, “A certificant shall at all times place the interest of the client ahead of his or her own.” NAPFA strongly supports this requirement as essential to aligning the interests of the client with the interests of the CFP® Certificant.

NAPFA notes that this reflects an evolution that has occurred since the last Code of Ethics for the CFP Board was adopted in 1993. It is now more clear under the common law that financial planners will likely be held by federal and state courts to the standard in which they must at all times act in the best interests of their clients. For example, in 2006 a U.S. Court of Appeals held that a licensed financial planner was a fiduciary, specifically noting that the elderly client relied upon the fiduciary as a financial advisor and estate planner. *U.S. v. Williams*, 441 F.3d 716, 724 (9th Cir. 2006). While additional cases arising under the common law might be expected, the vast majority of financial plans prepared for individual consumers are already governed by the Investment Advisers Act of 1940 and its imposition of the best interests of the client standard pursuant to the *Capital Gains* decision. Cases which involve registered representatives are nearly always handled through arbitration proceedings. However, it is significant that the few cases found which address the fiduciary status of financial planners (when advising retail clients) impose fiduciary status upon the financial planner. Furthermore, with the overturning of the broker-dealer fee-based accounts rule by the U.S. Court of Appeals on March 30, 2007, the broad application of the Advisers Act to nearly all financial planning activities, as expressed by SEC Release IA-1072, has been restored.

NAPFA notes that common law fiduciary status, which is likely to result for all financial planners, is not the function of the regulatory scheme under which the CFP® Certificant may be registered. The common law applies to all CFP® Certificants, regardless of how they are registered. The CFP Board’s actions are significant in that they establish for all Certified Financial Planners™ a single, uniform standard of conduct, in recognition that the best interests standard applies under the common law as well. The CFP Board’s proposal will greatly serve to minimize consumer confusion and enable consumers to rely upon the advice of all Certified Financial Planners.

NAPFA also notes the rise of 401k and other defined contribution plans over the last 30 years, as well as the demise of defined benefit plans and increasingly complex tax laws. As a result, more and more of our fellow citizens possess greater responsibility for their financial futures, a

responsibility that most find daunting. Given the very high degree of knowledge and understanding necessary to successfully navigate today's complex financial planning minefields, consumers need a trusted professional to turn to for advice. The CFP Board's *Second Exposure Draft* represents a significant advance in the service of consumers.

There may be some who argue that the CFP Board should not apply the best interests standard to activities which occur when a financial plan, prepared by a CFP® Certificant or his or her firm, is then implemented by that CFP® Certificant. Such argument does not reflect sound reasoning. As every Certificant knows, financial planning is a dynamic six-step process. The advisory function does not cease when implementation of the financial plan begins. Advice continues throughout the course of the relationship with the client, including the implementation and monitoring stages. During implementation new facts or circumstances arise, and these may necessitate revisions to the financial plan. As practice in the real world and logic dictate, the CFP Board should apply the best interests of the client standard to any material element of the financial planning process.

NAPFA also notes that there may be some who argue that certificants should be able to use the CFP mark as a mark of educational achievement only. However, for years Certificants have been required to adhere to high standards of ethical conduct. Professor Austin Scott, who for many years was the leading American scholar in the field of trust law, in 1949, defined the term fiduciary as “a person who undertakes to act in the interest of another person.” This is nearly identical to the language contained in CFP Board's current Rule 202. Accordingly, for many years CFP® Certificants have been on notice that they may be held to act in the best interests of the client.

NAPFA notes that some may argue against any changes to the CFP Board's Rules of Conduct. However, as already noted, the CFP Board is not imposing new duties upon its Certificants; it is merely reflecting in its professional codes of conduct the best interests of the client standard. The best interest standard is already imposed by numerous federal and state laws and also, as noted previously, judicial decisions applying the common law. Moreover, the CFP Board is a 501(c)(3) organization, and exists to benefit the public, not the securities industry. If the CFP Board were to not revise its Rules of Conduct to reflect changes in the common law, or were it to omit the best interests of the client standard in its *Rules of Conduct*, then the CFP Board may not be adhering to its mission to help people benefit from competent, professional and ethical financial planning.

Fiduciary Standard. The second sentence of Rule 1.4 of the *Rules of Conduct* contained in the *Second Exposure Draft* states: “When the certificant provides financial planning or material elements of the financial planning process, the certificant owes to the client the duty of care of a fiduciary as defined by CFP Board.”

We suggest that this second sentence be set forth as a separate Rule 1.5. Furthermore, we suggest that the sentence be modified to state: “When the certificant provides financial planning or any material elements of the financial planning process, the certificant owes to the client the duty of care of a fiduciary as defined by CFP Board.”

We accept the proposition, stated by the CFP Board in its Q&A, that the mere establishment of a brokerage account by a CFP® Certificant, nor the taking of an order for the purchase or sale of a

security by a CFP® Certificant, without more, does not constitute a material element of the financial planning process. But we believe it is incumbent upon the CFP® Board to note, in its issuing release for the final adopted rule, that the purchase or sale of a security following the presentation of any material element of the financial planning process, or the promulgation of any financial planning advice, either in writing or verbally, is subject to both the best interests standard and the fiduciary duty of due care.

In Conclusion. The National Association of Personal Financial Advisors believes that the Second Exposure Draft is a significant step in the raising of professional standards to the level the law should, and does, require. NAPFA urges the CFP Board to strictly enforce the best interest standard of conduct in order to continue to protect the interests of all consumers of the services of CFP® Certificants.

We would like to conclude by thanking the Certified Financial Planner Board of Standards, Inc. for the time devoted to reviewing and revising the CFP Code of Ethics. You have reached out to many groups within our industry, including NAPFA, to gather input. Through your courage and foresight you have significantly advanced the interests of your constituency – the consumers of financial planning services. We encourage the CFP Board to move forward and adopt the Code of Ethics requiring a fiduciary standard of conduct when any material element of the financial planning process is undertaken, and to adopt the best interests of the client standard for all CFP® Certificants at all times.

Sincerely,

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