A. DUTIES OWED TO CLIENTS, 5. DISCLOSE AND MANAGE CONFLICTS OF INTEREST:

1: THE DUTY TO DISCLOSE MATERIAL CONFLICTS OF INTEREST WHEN MAKING A ROLLOVER RECOMMENDATION

Bruce, a CFP® professional, is a representative of XYZ Advisors, Inc., a registered investment adviser. XYZ does not permit its investment adviser representatives to charge a fee for managing assets in a 401(k) plan. Bruce is engaged by Heather, who is retiring, to provide Financial Planning. After obtaining information about and understanding Heather's personal and financial circumstances, Bruce helps Heather develop a goal of having adequate income during her retirement. Bruce analyzes Heather's existing account in the 401(k) plan and the plan's investment options, fees and expenses, services, and other features. Bruce concludes that the management fees Heather will pay if she rolls over the assets into an individual retirement account ("IRA") will be higher than if she leaves the assets in her account in the 401(k) plan. Nevertheless, based on his review of Heather's circumstances and analysis of the relevant factors, Bruce determines that such a rollover is in Heather's best interest. Bruce presents that recommendation to Heather and tells Heather that he would receive an ongoing fee for managing the assets in the IRA. Bruce does not tell Heather that she would not have to pay Bruce a fee if she continues to invest her assets in the account in the 401(k) plan, as he would not be advising on those assets.

QUESTION:

With respect to Bruce's Duty to Disclose Conflicts of Interest, which of the following is the best response?

RESPONSE OPTIONS:

A. **Bruce has no Material Conflict of Interest because Heather understands that Bruce will be paid for his services.**

B. **Bruce satisfied his disclosure obligation when he disclosed his fee for managing the IRA.**

C. **Bruce did not fully disclose to Heather the Material Conflict of Interest that his recommendation presented.**

D. **Since Bruce sincerely believed that his recommendation was in Heather's best interest, he was excused from making full disclosure to Heather.**

Best Response: Response C is the best response. This case involves the Duty to Disclose Conflicts of Interest (Standard A.5.a.) and the definitions of Conflict of Interest and Material (Glossary).

A CFP® professional must make full disclosure of all Material Conflicts of Interest with the CFP® professional's Client that could affect the professional relationship. A CFP® professional must provide the Client with sufficiently specific facts so that a reasonable Client would be able to understand the CFP® professional's Material Conflicts of Interest and the business practices that give rise to the conflicts, and give informed consent to such conflicts or reject them. One way that a Conflict of Interest occurs is when a CFP® professional's interests (including the interests of the CFP® Professional's Firm) are adverse to the CFP® professional's duties to a Client. Information is Material when a reasonable Client or prospective Client would consider the information important in making a decision. A CFP® professional must make full disclosure and obtain the informed consent of the Client before providing any Financial Advice regarding which the CFP® professional has a Material Conflict of Interest.

In this case, Bruce has a Material Conflict of Interest that could affect his professional relationship with Heather because of how he is compensated for his services. To provide sufficiently specific facts for Heather to understand this Material Conflict of Interest, Bruce must explain to Heather that he will receive an ongoing fee for managing Heather's assets only if she accepts the recommendation and the assets are invested in an IRA; Bruce will receive no compensation if Heather keeps the assets in the account in the 401(k) plan because he will not be providing Financial Advice on those assets. A reasonable Client, like Heather, would consider that information important in making a decision whether to follow or reject Bruce's Financial Advice. Because Bruce did not fully disclose that information to Heather, he did not satisfy his Duty to Disclose Material Conflicts of Interest.

Response A is not the best response because Bruce has a Material Conflict of Interest.

Response B is not the best response because the Duty to Disclose Conflicts of Interest requires Bruce to do more than disclose that he would receive a fee for managing the assets in the IRA. Bruce also is required to explain to Heather that he will receive a fee only if she accepts his recommendation.

Response D is not the best response because a sincere belief by a CFP® professional that he or she is acting in the Client's best interests is insufficient to excuse a failure to make full disclosure of a Material Conflict of Interest.

While the Duty to Disclose Conflicts of Interest does not require disclosure of Material Conflicts of Interest in writing, evidence of oral disclosure of a conflict will be given such weight as CFP Board in its judgment deems appropriate. As a best practice, CFP Board recommends that a CFP® professional disclose the Conflict of Interest in writing before or when providing the Financial Advice.

Relevant Standards and Definitions: Disclose and Manage Conflicts of Interest (Standard A.5); definitions of Conflict of Interest and Material (Glossary).