Ethics

Standards of Practice Handbook

flashcard concepts

- FUNDAMENTAL RESPONSIBILITIES
  - Know the Laws and Rules
  - Don't Break or Help Others break the law
- RELATIONSHIPS AND RESPONSIBILITIES TO THE PROFESSION
  - Use of Professional Designation: Use the CFA mark in a dignified manner
  - Professional Misconduct: Don't do anything that reflects adversely on the profession
  - Plagiarism: Don't use other's work without reference and permission
- RELATIONSHIP WITH AND RESPONSIBILITY TO THE EMPLOYER
  - Inform your employer of the Code and Standards
  - Get your employer's written permission to consult
  - Disclose conflicts between you and your employer to your employer
  - Disclose additional compensation from outside your firm to your employer
  - Responsibility of Supervisors: They are responsible for supervising subordinates
- RELATIONSHIPS WITH AND RESPONSIBLITIES TO CLIENTS AND PROSPECTS
  - *The Investment Process*
    - Have a Reasonable Basis and Representation
      - Exercise Diligence and Thoroughness
      - Have a reasonable basis for your recommendation
      - Avoid misrepresentations
      - Keep Appropriate records
    - Research Reports
      - Use reasonable judgment
      - Distinguish between fact and opinion
    - Indicate the basic characteristics of the investment
    - Maintain Independence and Objectivity - Don't appear to have lost objectivity
  - *Interaction with Clients and Prospects*
    - *Fiduciary Duties* - Place your client's interest before your own
    - *Portfolio Investment Recommendations and Actions*
      - Know your client
      - Consider the appropriateness and suitability of the investment for your client
      - Distinguish between fact and opinion
      - Disclose the investment process
    - *Fair Dealing* - Disseminate investment recommendations fairly
    - *Priority of Transactions*- Client trades have priority over your or your firm's trades
    - *Preservation of Confidentiality*- Don't talk about your client's business
    - *Prohibition Against Misrepresentation* - Don't guarantee an investment return
      - Don't say you can do what you can't
      - Don't lie about your qualifications
      - Don't lie about your academic or professional credentials
    - *Disclosure of Conflicts to Clients*- Disclose things that may bias your recommendations
    - *Disclosure of Referral Fees* - Do it

- RELATIONSHIPS WITH AND RESPONSIBILITIES TO THE INVESTING PUBLIC
  - Prohibition against use of Material Non-public information
  - Performance presentation

Standards of Practice Casebook

Flashcard Concepts

- *Soft Dollars* is the use of client brokerage commissions to pay for research or other services that benefit the investment manager. Soft Dollars should only be used to benefit the portfolio beneficiaries
- The *Safe Harbor* provision of § 28(e) of the Securities and Exchange Act states that investment managers have not breached their fiduciary duty to the client if commission paid are reasonable relative to the research received
- There are TWO approaches to dealing with potential conflicts of interest:
  - Avoidance, and
  - Disclosure
- In a *Blind Trust*, control of the portfolio is turned over to a manager who has full discretion over portfolio assets within the guidelines that have been established. The beneficiary does not know the composition of the portfolio except at certain reporting periods
- There are Several Key Elements to Compliance Programs
  - Communication
  - Education
  - Effective Written Compliance Documents
- A Corporate Credo is a document that contains the guiding principles that members of a firm can follow. The purpose is to instill an ethical culture in the firm
- Supervisors should take an active role in monitoring the actions of employees. Supervisors cannot rely solely on compliance manuals and the firm's compliance department to monitor employees
- Client trades must take precedence over employee trades. AIMR suggests a 24-hour restriction on employee trades.
- Proprietary employer information must be kept confidential
- The allocation of block trades must be carefully considered so that a fiduciary duty is not violated. Clients with similar investment policies should be treated equally in the allocation of a block trade.
- Client trades must be suitable for the client given her stated investment policy.
- When dealing with trading errors in a client account, the following factors must be considered
  - *Fairness* - All clients with similar policies should be treated the same when correcting trading errors
  - *Financial Risk* - Client portfolios should not suffer losses from inappropriate trades. The firm cannot shift the financial risk of an inappropriate trade to clients by selling from one client account and simultaneously buying in another. The firm must take full responsibility for the trades.
- Suitable care and independent professional judgment should be used when developing a research report

Ethics

- The MOSAIC Theory states than an analyst can compile non-material, non-public information and use the implications of this data to form the basis of a research recommendation
- Researchers must have a reasonable basis for the recommendations and avoid material misrepresentations
- *Soft Dollars* are commission dollars paid to brokerage firms in excess of the cost of pure trading
- The Securities and Exchange Act of 1934, § 28(e), contains a *Safe Harbor* provision allowing investment managers to use soft dollars for research purposes only. Hence, soft dollars represent dollars paid for investment research
- In a pension context, soft dollars may only be used to the extent that they will benefit plan participants and beneficiaries. An investment management firm's fiduciary duty lies with plan participants, not with plan sponsor's
- Members should consider how appropriate and suitable the investment recommendations are for each portfolio. Only those trades that are consistent with a client's needs are permissible.
- The SEC defines having control over an account as "when a client relies upon the broker to such an extent that the broker is in a position to control the volume and frequency of the transactions in the account."
- Should a conflict arise between a company's recommendation to buy and a client's policy statement, managers are charged to work in the best interest of the client

