Question 1
L2R02TB-AC050-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Peter Jenkins is a Level II candidate. He was having particular difficulty remembering a formula from the curriculum. A colleague suggested a mnemonic (word association) that might help jog his memory. Knowing that formula sheets are not permitted in the exam center, he instead wrote the mnemonic on his hand and used it to recall the formula for a question. Did Jenkins violate the Standards of Professional Conduct?

- ○ No.
- ◉ Yes, because he failed to follow the spirit of the exam center rules.
- ○ Yes, because plagiarized his colleague's mnemonic.

Rationale
❌ **No.**
Candidates may not bring any study aids into the exam center. Writing a memory aid on his hand gave him an unfair advantage over other candidates who followed the exam center rules. Therefore, Jenkins is in violation of the Standard.

Rationale
✅ **Yes, because he failed to follow the spirit of the exam center rules.**
Candidates may not bring any study aids into the exam center. Writing a memory aid on his hand gave him an unfair advantage over other candidates who followed the exam center rules. Therefore, Jenkins is in violation of the Standard.

Rationale
❌ **Yes, because plagiarized his colleague's mnemonic.**
Candidates may not bring any study aids into the exam center. Writing a memory aid on his hand gave him an unfair advantage over other candidates who followed the exam center rules. Therefore, Jenkins is in violation of the Standard.

Question 2
L2ET-TB0010-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Michael Bourne manages a sector-focused equity investment fund that is mandated to remain at least 95% invested at all times. After a recent bull market, he believes that stocks are grossly overvalued and rotates half the portfolio away from equities and into cash. Shortly after this, the equity markets fall violently and the fund benefits greatly from its lower exposure levels. With respect to Bourne's duties under Standard III(C): Suitability, which of the following statements is *most likely* accurate?

- (selected) Bourne has violated the Standard.
- Bourne has not violated the Standard since his actions were in the best interests of investors.
- Bourne has not violated the standard since his actions generated profits for investors.

Rationale

This Answer is Correct

By breaching the mandate of the fund that he is charged with running, Bourne has violated Standard III(C). The fact that the decision made money is irrelevant. If his agreed mandate is to remain 95% invested, then he should follow the mandate of the fund.

Question 3
L2R02TB-AC031-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Jennifer Wagner is the director of sales for a boutique research firm. Her travel expenses are reimbursed by the company. Wagner has arrangements with her hairdresser, dry cleaner, and certain local restaurants to provide her with backdated receipts that she submits as part of her travel reimbursements. Upon discovering the padded expenses, her boss terminates her employment. He also considers reporting her to the CFA Institute Professional Conduct Program.

	Did Wagner Violate the Standards?	*Is Her Boss Required to Report Her to CFAI PCP?*
A.	Yes	Yes
B.	Yes	No
C.	No	Yes

- ROW A
- ROW B
- ROW C

Rationale
ROW A
Deceptively filing false or misleading expense reports for personal gain is an act of dishonesty, which is a violation of the Standards. While her boss is well justified in reporting her actions to the CFA Institute Professional Conduct Program and is encouraged to do so, the Standards do not require him to file a report.

Rationale
ROW B
Deceptively filing false or misleading expense reports for personal gain is an act of dishonesty, which is a violation of the Standards. While her boss is well justified in reporting her actions to the CFA Institute Professional Conduct Program and is encouraged to do so, the Standards do not require him to file a report.

Rationale
ROW C
Deceptively filing false or misleading expense reports for personal gain is an act of dishonesty, which is a violation of the Standards. While her boss is well justified in reporting her actions to the CFA Institute Professional Conduct Program and is encouraged to do so, the Standards do not require him to file a report.

Question 4
L2R02TB-AC006-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Paula Kester is the controller for a small manufacturing company, Gizmo Mfg., which trades on the pink sheets. One of the firm's competitors approached Gizmo's CEO with an offer to purchase the company at a substantial premium to its current market price. Kester mentioned in confidence to her sister, Marie, that she is concerned about losing her job after the takeover. Marie shared those concerns with Becker, her husband and a stockbroker, who began accumulating shares of Gizmo stock for himself and advising certain clients to do the same. Did Kester or Becker violate the Standards of Professional Conduct?

	Kester	*Becker*
A.	Yes	Yes
B.	Yes	No
C.	No	Yes

- ○ ROW A
- ○ ROW B
- ◉ ROW C

Rationale
✗ ROW A
The Standard prohibits members from trading or encouraging others to trade on material, nonpublic information. The information about the potential acquisition is both material and nonpublic. However, Kester did not share the information with her sister with the intent to encourage her to trade, only to express concern over her employment situation. Nor was it reasonable to foresee that it would be shared with anyone else. Becker knew or should have known that the offer was nonpublic, making his actions a violation of the Standard.

Rationale
✗ ROW B
The Standard prohibits members from trading or encouraging others to trade on material, nonpublic information. The information about the potential acquisition is both material and nonpublic. However, Kester did not share the information with her sister with the intent to encourage her to trade, only to express concern over her employment situation. Nor was it reasonable to foresee that it would be shared with anyone else. Becker knew or should have known that the offer was nonpublic, making his actions a violation of the Standard.

Rationale
✓ ROW C
The Standard prohibits members from trading or encouraging others to trade on material, nonpublic information. The information about the potential acquisition is both material and nonpublic. However, Kester did not share the information with her sister with the intent to encourage her to trade, only to express concern over her employment situation. Nor was it reasonable to foresee that it would be shared with anyone else. Becker knew or should have known that the offer was nonpublic, making his actions a violation of the Standard.

Question 5
L2R02TB-AC052-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Nicole Plott is a hedge fund manager specializing in biotechnology companies. She subscribes to a service that describes itself as an expert network. The service provides information about what biotech firms are working on, what pharmaceutical companies are looking for, and technical developments in the industry. Plott has taken a large position in Beta Miracle Cures (BMC) whose latest cancer drug is in final trials with the federal drug agency. Plott calls her contact at the expert network, Charles Tucker, to get his opinion and is told, "…the federal agency did not approve the drug, but BMC is appealing for more time. Get out now before they announce it. The new drug is dead." With respect to the Standards of Professional Conduct, Plott's best course of action is to:

- sell all her shares in BMC as advised by Tucker.
- hold all her shares until the federal agency announces its findings.
- make further inquiry into the source of the information provided by Tucker.

Rationale

sell all her shares in BMC as advised by Tucker.

Plott must be careful in utilizing the services of expert networks. If the information Tucker provided is an opinion based on expert conjecture, it does not likely violate Standard II(A). If, however, the source is someone directly involved in the drug trials, the regulatory agency, or management of the company, trading on the information is likely a violation.

Rationale

hold all her shares until the federal agency announces its findings.

Plott must be careful in utilizing the services of expert networks. If the information Tucker provided is an opinion based on expert conjecture, it does not likely violate Standard II(A). If, however, the source is someone directly involved in the drug trials, the regulatory agency, or management of the company, trading on the information is likely a violation.

Rationale

make further inquiry into the source of the information provided by Tucker.

Plott must be careful in utilizing the services of expert networks. If the information Tucker provided is an opinion based on expert conjecture, it does not likely violate Standard II(A). If, however, the source is someone directly involved in the drug trials, the regulatory agency, or management of the company, trading on the information is likely a violation.

Question 6
L2R02TB-AC019-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Rodney Webber is a technology analyst with DAT Research. After accepting a position with one of DAT's competitors, he realizes that he cannot take records of his past work to his new firm. While cleaning out his old office, Webber empties the file cabinet containing those records into a waste bin for shredding. Did Webber violate the Standards of Professional Conduct?

- (selected) Yes.
- No, because he did not take the records with him.
- No, because his past work is no longer relevant.

Rationale
✔ **Yes.**
The records of Webber's past work belong to DAT Research. While it is a violation of the Standard for him to take them, it is also a violation to destroy them without DAT's permission.

Rationale
✖ **No, because he did not take the records with him.**
The records of Webber's past work belong to DAT Research. While it is a violation of the Standard for him to take them, it is also a violation to destroy them without DAT's permission.

Rationale
✖ **No, because his past work is no longer relevant.**
The records of Webber's past work belong to DAT Research. While it is a violation of the Standard for him to take them, it is also a violation to destroy them without DAT's permission.

Question 7

L2ET-TB0021-1412

LOS: LOS-5660

Lesson Reference: Lesson 1: Standard I: Professionalism

Difficulty: medium

Which of the following is *least likely* a recommended procedure for compliance under Standard VI(B): Priority of Transactions?

- (selected) Disclose trade allocation procedures.
- Providing duplicate confirmations of transactions.
- Preclearance procedures for personal trades.

Rationale

This Answer is Correct

The disclosure of trade allocation procedures is a recommended procedure for compliance with Standard III(B): Fair Dealing. The first and second options are recommended procedures for compliance with Standard VI(B): Priority of Transactions.

Question 8
L2ET-TBB211-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Fred Bull, CFA, is a portfolio manager who works for Birchwood Investments LLC. In a recent heavily oversubscribed IPO, three clients, clients A, B, and C, subscribed to 1,000, 2,000, and 3,000 shares, respectively. Bull is informed by the lead broker on the IPO that he will receive only 1,000 shares for his accounts. The exchange on which the new shares are listed has a minimum lot size of 200 shares. Which of the following allocations best fulfills the requirements of Bull under Standard III(B): Fair Dealing?

- ○ 1,000 shares to client A.
- ○ 167 shares to client A, 333 shares to client B, 500 shares to client C.
- ◉ 200 shares to client A, 300 shares to client B, 500 shares to client C.

Rationale

This Answer is Correct

According to Standard III(B): Fair Dealing, Bull should allocate the shares pro rata to size of client while avoiding odd-lot allocations below the minimum lot size of the exchange. The first option is incorrect since this allocation will favor client A at the expense of other clients. The second option is incorrect since the allocation to client A is below the minimum lot size. The third option is the best answer that meets the requirements of approximate pro rata by size while avoiding an allocation smaller than that of the minimum lot size of the exchange.

Question 9

L2ET-PQ0210-1502

LOS: LOS-5660

Lesson Reference: Lesson 2: Standard II: Integrity of Capital Markets

Difficulty: hard

According to the recommended procedures for compliance with Standard II(A)—Material Nonpublic Information, on receipt of material nonpublic information on a company, a member or candidate should make reasonable efforts to achieve public dissemination of the information through:

- ○ Disclosing the information to a news provider.
- ◉ Encouraging the company to make a public announcement.
- ○ Issuing a public statement through their firm.

Rationale

✗ **Disclosing the information to a news provider.**

Incorrect. If a member or candidate determines that information is material, the member or candidate should make reasonable efforts to achieve public dissemination of the information. These efforts usually entail encouraging the issuing company to make the information public. If public dissemination is not possible, the member or candidate must communicate the information only to the designated supervisory and compliance personnel within the member's or candidate's firm and must not take investment action or alter current investment recommendations on the basis of the information.

Rationale

✓ **Encouraging the company to make a public announcement.**

Correct. If a member or candidate determines that information is material, the member or candidate should make reasonable efforts to achieve public dissemination of the information. These efforts usually entail encouraging the issuing company to make the information public. If public dissemination is not possible, the member or candidate must communicate the information only to the designated supervisory and compliance personnel within the member's or candidate's firm and must not take investment action or alter current investment recommendations on the basis of the information.

Rationale

✗ **Issuing a public statement through their firm.**

Incorrect. If a member or candidate determines that information is material, the member or candidate should make reasonable efforts to achieve public dissemination of the information. These efforts usually entail encouraging the issuing company to make the information public. If public dissemination is not possible, the member or candidate must communicate the information only to the designated supervisory and compliance personnel within the member's or candidate's firm and must not take investment action or alter current investment recommendations on the basis of the information.

Question 10
L2ET-PQ0206-1502
LOS: LOS-5660
Lesson Reference: Lesson 3: Standard III: Duties to Clients
Difficulty: hard
All of the following are recommended procedures for compliance with Standard I(C)—Misrepresentation, except:

- (selected) Refrain from using third party research.
- Provide a written list of services offered by a firm and the qualifications of the firm's employees.
- Encourage firms to verify outside information.

Rationale

✅ **Refrain from using third party research.**

Recommended procedures for compliance with Standard I(C)—Misrepresentation include using factual information to describe a firm's services and the qualifications and abilities of its employees. Covered persons should encourage their firm to develop procedures for verifying soundness of information obtained from outside sources.

Rationale

❌ **Provide a written list of services offered by a firm and the qualifications of the firm's employees.**

Recommended procedures for compliance with Standard I(C)—Misrepresentation include using factual information to describe a firm's services and the qualifications and abilities of its employees. Covered persons should encourage their firm to develop procedures for verifying soundness of information obtained from outside sources.

Rationale

❌ **Encourage firms to verify outside information.**

Recommended procedures for compliance with Standard I(C)—Misrepresentation include using factual information to describe a firm's services and the qualifications and abilities of its employees. Covered persons should encourage their firm to develop procedures for verifying soundness of information obtained from outside sources.

Question 11
L2R02TB-AC041-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Ricardo Plum is a portfolio manager at a money management firm. He also serves on the board of a private hospital where his wife is a physician. The position includes a small compensation package. In notifying his employer of his participation on the board, which of the following is Plum *least likely* to disclose?

- The duration of his service and the average monthly time required.
- The fact that his wife is also a physician at the same hospital.
- The amount of compensation he receives for his service.

Rationale
The duration of his service and the average monthly time required.
The fact that his wife is a physician at the hospital does not appear relevant to the facts and would not likely contribute to any conflict of interest with Plum's money management employment.

Rationale
The fact that his wife is also a physician at the same hospital.
The fact that his wife is a physician at the hospital does not appear relevant to the facts and would not likely contribute to any conflict of interest with Plum's money management employment.

Rationale
The amount of compensation he receives for his service.
The fact that his wife is a physician at the hospital does not appear relevant to the facts and would not likely contribute to any conflict of interest with Plum's money management employment.

Question 12
L2R02TB-AC021-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Sydney Wicks is a fixed-income analyst with Consistent Capital. A colleague introduced him to commodity-linked bonds as a means to enhance returns. Believing that his firm would not be interested in these securities, he buys several for his personal account. Some months later, Wicks writes a report recommending that his firm consider commodity-linked bonds for its clients and includes the issue he owns in a list of potential investments. According to the Standards of Professional Conduct, Wicks must:

- (selected) Disclose his beneficial ownership of the issue in the report.
- Liquidate his positions prior to making any recommendations.
- List his holdings in the next quarterly investment disclosure document.

Rationale
✅ **Disclose his beneficial ownership of the issue in the report.**
Wicks' ownership of bonds he includes in his recommendation creates the appearance of a conflict, at the very least. Therefore, he must disclose his ownership interest in the report.

Rationale
❌ **Liquidate his positions prior to making any recommendations.**
Wicks' ownership of bonds he includes in his recommendation creates the appearance of a conflict, at the very least. Therefore, he must disclose his ownership interest in the report.

Rationale
❌ **List his holdings in the next quarterly investment disclosure document.**
Wicks' ownership of bonds he includes in his recommendation creates the appearance of a conflict, at the very least. Therefore, he must disclose his ownership interest in the report.

Question 13
L2ET-TBB209-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Which of the following actions is *least likely* to be in violation of Standard II(B): Market Manipulation?

- (selected) The use of high-frequency trading strategies to take advantage of short-term perceived market inefficiencies.
- Manipulation of model inputs to reflect only negative market scenarios when valuing structured products.
- The crossing of a small amount of stock in a small-cap company at a price significantly different to the price of the most recent automatically matched trade shortly before the calculation of settlement prices used for option payoff calculations.

Rationale

✓ **The use of high-frequency trading strategies to take advantage of short-term perceived market inefficiencies.**

Correct. Standard II(B) is not intended to preclude transactions undertaken on legitimate trading strategies based on perceived market inefficiencies. The manipulation of model inputs to value securities in a biased way and the execution of trades in order to impact option settlement prices are both examples of types of behavior that are in breach of Standard II(B).

Rationale

✗ **Manipulation of model inputs to reflect only negative market scenarios when valuing structured products.**

Incorrect. Standard II(B) is not intended to preclude transactions undertaken on legitimate trading strategies based on perceived market inefficiencies. The manipulation of model inputs to value securities in a biased way and the execution of trades in order to impact option settlement prices are both examples of types of behavior that are in breach of Standard II(B).

Rationale

✗ **The crossing of a small amount of stock in a small-cap company at a price significantly different to the price of the most recent automatically matched trade shortly before the calculation of settlement prices used for option payoff calculations.**

Incorrect. Standard II(B) is not intended to preclude transactions undertaken on legitimate trading strategies based on perceived market inefficiencies. The manipulation of model inputs to value securities in a biased way and the execution of trades in order to impact option settlement prices are both examples of types of behavior that are in breach of Standard II(B).

Question 14
L2ET-PQ0228-1502
LOS: LOS-5650
Lesson Reference: Lesson 5: Standard V: Investment Analysis, Recommendations, and Actions
Difficulty: hard
Den Sawyer is an employee of Eve Partners, an investment firm that manages client investments both in-house and on an external outsourced basis. When selecting new hedge fund managers, Sawyer considers the two main factors for investing success to be experience and track record, hence he uses a simple process to select hedge fund managers. He gives each potential manager a score which is calculated as the average annual return of the fund multiplied by the number of years the fund has been in existence. He then allocates funds to the manager with the highest score. According to Standard V(A)—Diligence and Reasonable Basis, which of the following is *most likely* to be correct?

- Sawyer is in violation of the Standard since he should not outsource investment management of client funds.
- Sawyer is in violation of the Standard since he did not perform sufficient due diligence on external managers.
- Sawyer is in compliance with the Standard.

Rationale
Sawyer is in violation of the Standard since he should not outsource investment management of client funds.
Incorrect. According to Standard V(A), outsourcing to external managers is permitted; however, members and candidates should conduct proper due diligence when selecting external managers. By considering only performance and experience, Sawyer has not conducted sufficient review of potential funds to satisfy the requirements of Standard V(A). A thorough investigation of the funds and their operations should be conducted to ensure that they are suitable for the clients.

Rationale
Sawyer is in violation of the Standard since he did not perform sufficient due diligence on external managers.
Correct. According to Standard V(A), outsourcing to external managers is permitted; however, members and candidates should conduct proper due diligence when selecting external managers. By considering only performance and experience, Sawyer has not conducted sufficient review of potential funds to satisfy the requirements of Standard V(A). A thorough investigation of the funds and their operations should be conducted to ensure that they are suitable for the clients.

Rationale
Sawyer is in compliance with the Standard.
Incorrect. According to Standard V(A), outsourcing to external managers is permitted; however, members and candidates should conduct proper due diligence when selecting external managers. By considering only performance and experience, Sawyer has not conducted sufficient review of potential funds to satisfy the requirements of Standard V(A). A thorough investigation of the funds and their operations should be conducted to ensure that they are suitable for the clients.

Question 15
L2ET-TB0019-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Stuart Robinson is head economist at a leading UK investment bank. After years of low interest rates, it is now the market consensus opinion that central banks will start increasing interest rates due to a prolonged rise in asset prices and an increase in inflation. Robinson states in a television interview: "Given that interest rates will go up some time in the next year, the prudent trade is to shorten duration a little until this scenario begins to play out." Robinson has

- ○ Not violated the Standards.
- ○ Violated Standard II(A): Material Nonpublic Information.
- ◉ Violated Standard V(B): Communication with Clients

Rationale

This Answer is Correct

Robinson has stated as a fact that interest rates will rise in the next year when it is only current market consensus that this eventuality will happen. Under Standard V(B): Communication with Clients, analysts should differentiate between opinion and fact in all communications with clients and prospective clients in either written or verbal communication.

Question 16
L2R02TB-ITEMSET-AC056-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium

Use the following information to answer the next 3 questions:

Enrique Badillo, CFA, was a portfolio manager at Triunfo Asset Management (TAM). He has been managing index funds, but wants to shift his career to hedge funds. At a local CFA society luncheon, Badillo met Marta Guarin who runs a hedge fund and is looking for a backup manager to work under independent contract with her fund. The two hit it off, and Badillo agreed to speak to his supervisor, Gorge Padin, for approval. He sent an email listing the name of the hedge fund, the client profile, and the expected time commitment. Padin approved based on this information.

After working with Guarin for a few months, Badillo was offered and accepted a full-time position. He discussed his resignation with Padin, who wished him well on his new position. As the men shook hands, Badillo asks if he may take some files that he had worked on while at TAM. Padin replied, “That's fine with me, but let's not make a big deal about it. We'll just call it a “handshake” agreement.”

Once settled into his new job, Badillo is approached by Guarin about a charity event. She said, “We're desperate for corporate sponsors. Do you know any business leaders in the area?” Badillo says, “At TAM, I worked with Mutual Insurance. Jeff Johnson is the CEO who is also heavily involved in philanthropy. In fact, I handled the transfer of a large donation from his personal account to the Children's Foundation two years ago … you know, that $2 million anonymous gift reported in all the papers. That was Jeff. I'll get you his number.”

i.
According to the Standards of Professional Conduct required compliance and recommended procedures, in discussing the part-time position at the hedge fund, Badillo should provide Padin with which additional piece of information left out of his email?

- (selected) The compensation.
- The name of his supervisor.
- A copy of the agreement or contract.

Rationale
This Answer is Correct
Standard IV(A): Loyalty to Employers states that members must obtain consent from their employers prior to entering independent practice that might compete with them. The information provided should include a description of the services, clients, duration, and compensation. Standard IV(B): Additional Compensation Arrangement recommended procedures suggests members provide written notification that should include the form and amount of compensation and the duration of the arrangement.

Rationale
This Answer is Correct
Standard IV(A): Loyalty to Employers states that members must obtain consent from their employers prior to entering independent practice that might compete with them. The information provided should include a description of the services, clients, duration, and compensation. Standard IV(B): Additional Compensation Arrangement recommended procedures suggests members provide written notification that should include the form and amount of compensation and the duration of the arrangement.

Rationale
This Answer is Correct

Standard IV(A): Loyalty to Employers states that members must obtain consent from their employers prior to entering independent practice that might compete with them. The information provided should include a description of the services, clients, duration, and compensation. Standard IV(B): Additional Compensation Arrangement recommended procedures suggests members provide written notification that should include the form and amount of compensation and the duration of the arrangement.

ii.

In taking files from TAM, did Badillo follow the required compliance and recommended procedures of the Standards of Professional Conduct?

- (selected) No.
- Yes, because he first obtained permission from his supervisor.
- Yes, because he only took files that he had personally worked on.

Rationale

This Answer is Incorrect

Standard IV(A) Loyalty to Employers requires that departing employees should not take customer lists or records without the written permission of their supervisors. Padin agreed to Badillo's request but did not properly document the approval. Badillo should ask for it in writing.

Rationale

This Answer is Incorrect

Standard IV(A) Loyalty to Employers requires that departing employees should not take customer lists or records without the written permission of their supervisors. Padin agreed to Badillo's request but did not properly document the approval. Badillo should ask for it in writing.

Rationale

This Answer is Incorrect

Standard IV(A) Loyalty to Employers requires that departing employees should not take customer lists or records without the written permission of their supervisors. Padin agreed to Badillo's request but did not properly document the approval. Badillo should ask for it in writing.

iii.

With respect to the charity sponsorship, did either Badillo or Guarin violate the Standards of Professional Conduct?

- Guarin did, but Badillo did not.
- Both Guarin and Badillo did.
- (selected) Badillo did, but Guarin did not.

Rationale

This Answer is Incorrect

In revealing information about a past client, Badillo violated Standard III(E): Preservation of Confidentiality. This standard requires that members keep information about current, former, and prospective clients confidential. Badillo should have first asked Johnson's permission before divulging any information about his giving or account activity.

Rationale

This Answer is Incorrect

In revealing information about a past client, Badillo violated Standard III(E): Preservation of Confidentiality. This standard requires that members keep information about current, former, and prospective clients confidential. Badillo should have first asked Johnson's permission before divulging any information about his giving or account activity.

Rationale

This Answer is Incorrect

In revealing information about a past client, Badillo violated Standard III(E): Preservation of Confidentiality. This standard requires that members keep information about current, former, and prospective clients confidential. Badillo should have first asked Johnson's permission before divulging any information about his giving or account activity.

Question 17
L2R02TB-AC013-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Robert Duggan is a financial advisor with Atticus Investments. He has been recruited to join Benedict Advisors and provides notice of his resignation to Atticus, which will be effective in two weeks. Prior to leaving the firm, Duggan contacts several of his clients, informs them of his pending departure, and asks their permission to call on them once he moves to Benedict. Did Duggan violate the Standards of Professional Conduct?

- ○ No.
- ◉ Yes, by soliciting his employer's customers.
- ○ Yes, by informing clients of his pending departure.

Rationale
No.
Duggan must perform his duties on behalf of Atticus until his departure. Soliciting clients is not acting in his employer's interest and is a violation of the Standard. He may not solicit clients until after he leaves and without taking any records that belong to Atticus.

Rationale
Yes, by soliciting his employer's customers.
Duggan must perform his duties on behalf of Atticus until his departure. Soliciting clients is not acting in his employer's interest and is a violation of the Standard. He may not solicit clients until after he leaves and without taking any records that belong to Atticus.

Rationale
Yes, by informing clients of his pending departure.
Duggan must perform his duties on behalf of Atticus until his departure. Soliciting clients is not acting in his employer's interest and is a violation of the Standard. He may not solicit clients until after he leaves and without taking any records that belong to Atticus.

Question 18
L2ET-TBB213-1412
LOS: LOS-5650
Lesson Reference: Lesson 3: Standard III: Duties to Clients
Difficulty: medium
Which of the following performance analysts is *most likely* to be in violation of Standard III(D): Performance Presentation?

- ○ An analyst who prepares performance reports according to the GIPS standards except for some detailed issues regarding composite composition.
- ○ An analyst who reports simulated performance figures to prospective clients.
- ● An analyst who excludes terminated accounts as part of performance history.

Rationale

✗ **An analyst who prepares performance reports according to the GIPS standards except for some detailed issues regarding composite composition.**

Incorrect. Answer C is a clear violation of Standard III(D), which states that terminated accounts should be included as part of performance history in order to avoid survivorship bias biasing historical returns upwards. The analyst in answer A is not a violation unless the analyst claims compliance with GIPS. The analyst in answer B will not be in violation if they disclose and clearly identify which part of the performance is derived from simulation.

Rationale

✗ **An analyst who reports simulated performance figures to prospective clients.**

Incorrect. Answer C is a clear violation of Standard III(D), which states that terminated accounts should be included as part of performance history in order to avoid survivorship bias biasing historical returns upwards. The analyst in answer A is not a violation unless the analyst claims compliance with GIPS. The analyst in answer B will not be in violation if they disclose and clearly identify which part of the performance is derived from simulation.

Rationale

✓ **An analyst who excludes terminated accounts as part of performance history.**

Correct. Answer C is a clear violation of Standard III(D), which states that terminated accounts should be included as part of performance history in order to avoid survivorship bias biasing historical returns upwards. The analyst in answer A is not a violation unless the analyst claims compliance with GIPS. The analyst in answer B will not be in violation if they disclose and clearly identify which part of the performance is derived from simulation.

Question 19
L2ET-TB0018-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Sue West is an investment analyst who has set up a website in order to enable discussion of investment opportunities and try to attract new clients to her current employer. She posts some research on the website that looks at a specific event-driven earnings-based hedge fund strategy and points out how successful the strategy has been over the most recent earnings season over the past six weeks. West concludes that the strategy is an attractive one and makes several long-term buy recommendations of hedge funds that follow the strategy in question. West has *most likely:*

- ○ Not violated the Standards.
- ○ Violated Standard II(B): Market Manipulation.
- ● Violated Standard V(A): Diligence and Reasonable Basis.

Rationale

This Answer is Correct

By basing her long-term recommendation on such a short sample period of only six weeks, West has likely violated Standard V(A): Diligence and Reasonable Basis. West should consider the likely performance of the strategy over several different earnings seasons and at different points of the economic cycle in order to gain a long-term view on how the strategy will perform in different scenarios. Answer B is incorrect since West is not attempting to distort market prices or by her actions.

Question 20
L2ET-TB0013-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
According to Standard IV(A): Loyalty, members and candidates must:

- Abstain from independent practice that could conflict with the interests of their employer.
- Abstain from independent practice that could conflict with the interests of their employer without disclosing said practice to their employer.
- Abstain from independent practice that could conflict with the interests of their employer without obtaining prior consent for said practice from their employer.

Rationale

This Answer is Correct

Standard IV(A) does not preclude members or candidates from entering into an independent business while still employed, but members and candidates must obtain prior consent from their employer should they desire to engage in independent practice.

Question 21
L2R02TB-AC009-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Anna Bolsky is a well-known biotech analyst with Solid Analytics. As a speaker at a professional society luncheon, she was asked about her opinion of Protoplasm Bio. She responded by saying, “Its recent drug trials have disappointed and there's not much left in the pipeline. I'll be downgrading my rating on the stock in my report next week. You can check that out for details.” Several of the attendees are institutional clients of Solid Analytics. Did Bolsky violate the Standards of Professional Conduct announcing the downgrade or the impending report?

	Downgrade	*Report*
A.	Yes	Yes
B.	Yes	No
C.	No	Yes

- ROW A
- ROW B (selected)
- ROW C

Rationale
ROW A (incorrect)
Bolsky violated the Standard by disclosing the change in her recommendation to a select group of clients who may then act upon it before her other clients. Advising that the report itself is about to be released is not a violation because the content of the report will be available to all once it is released.

Rationale
ROW B (correct)
Bolsky violated the Standard by disclosing the change in her recommendation to a select group of clients who may then act upon it before her other clients. Advising that the report itself is about to be released is not a violation because the content of the report will be available to all once it is released.

Rationale
ROW C (incorrect)
Bolsky violated the Standard by disclosing the change in her recommendation to a select group of clients who may then act upon it before her other clients. Advising that the report itself is about to be released is not a violation because the content of the report will be available to all once it is released.

Question 22
L2ET-PQ0230-1502
LOS: LOS-5650
Lesson Reference: Lesson 6: Standard VI: Conflicts of Interest
Difficulty: hard
Matthew Segall is a broker working for Mostdirect Brokerage LLC. Segall has recently come under pressure at his employment since a major client has stopped trading and caused his commission levels to fall dramatically. In response to this, Segall calls an old school friend, Bob Angler, who works at LoyalT Investments, a major buy side investment company. Angler manages the pension plan assets of several large corporations. Segall asks Angler to consider adding Mostdirect to the approved broker list of LoyalT, something that Angler agrees to do internally at his firm. Have Angler's actions breached Standard VI(A): Conflicts of Interest?

- (selected) Yes, since he should disclose his relationship with Segall to his employer.
- Yes, since he should not do business with people with which he has a personal relationship.
- No.

Rationale

✔ **Yes, since he should disclose his relationship with Segall to his employer.**

Correct. Angler has violated Standard VI(A) by not disclosing to his employer his personal relationship with Segall. Disclosure of his past history with Segall would allow his firm to determine whether the conflict may have impaired Segall's independence in deciding to recommend Mostdirect be added to LoyalT's recommended broker list.

Rationale

✖ **Yes, since he should not do business with people with which he has a personal relationship.**

Incorrect. Angler has violated Standard VI(A) by not disclosing to his employer his personal relationship with Segall. Disclosure of his past history with Segall would allow his firm to determine whether the conflict may have impaired Segall's independence in deciding to recommend Mostdirect be added to LoyalT's recommended broker list.

Rationale

✖ **No.**

Incorrect. Angler has violated Standard VI(A) by not disclosing to his employer his personal relationship with Segall. Disclosure of his past history with Segall would allow his firm to determine whether the conflict may have impaired Segall's independence in deciding to recommend Mostdirect be added to LoyalT's recommended broker list.

Question 23

L2R02TB-AC034-1512

LOS: LOS-5650

Lesson Reference: Lesson 1: Standard I: Professionalism

Difficulty: medium

John Fields is a portfolio manager in charge of several mutual funds. In one fund, he had accumulated a position in several thinly traded stocks that were not performing well. Fields found that by trading the stocks between the funds he could increase the closing price and volume. Fields hopes that the apparent increased liquidity will make it easier to exit the positions and minimize his losses. Did Fields violate the Standards of Professional Conduct with respect to market manipulation?

- ○ No.
- ○ Yes, because trading the same stock between funds is always a violation.
- ◉ Yes, because the transactions were intended to alter the price and volume data.

Rationale

✗ **No.**

Market manipulation is defined as attempting to distort price or volume data. In this case, Fields executed trades between two funds that he controlled with the intent to impact the price and volume data for the stock.

Rationale

✗ **Yes, because trading the same stock between funds is always a violation.**

Market manipulation is defined as attempting to distort price or volume data. In this case, Fields executed trades between two funds that he controlled with the intent to impact the price and volume data for the stock.

Rationale

✓ **Yes, because the transactions were intended to alter the price and volume data.**

Market manipulation is defined as attempting to distort price or volume data. In this case, Fields executed trades between two funds that he controlled with the intent to impact the price and volume data for the stock.

Question 24
L2R02TB-AC002-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Arbor Timber Company invited a group of analysts to tour its new lumber mill and meet with firm executives. Because the location is fairly remote, Arbor will provide transportation to the site on a chartered flight and provide lodging at a local ski resort. After the meetings, the analysts are invited to stay for the weekend to enjoy skiing and other activities at the resort paid by Arbor. According to the Standards of Professional Conduct, which of the following may be accepted by the analysts?

	Chartered Flight	*Weekend Activities*
A.	Yes	No
B.	No	Yes
C.	Yes	Yes

- (●) ROW A
- ( ) ROW B
- ( ) ROW C

Rationale
ROW A
Whenever possible, members should pay for their own transportation and lodging. However, under certain circumstances, like accessing the remote locations described here, members may accept such hospitality. However, enjoying a weekend of recreation could give the appearance of infringing on one's objectivity at the very least. Therefore, any weekend activities, including lodging should be declined.

Rationale
ROW B
Whenever possible, members should pay for their own transportation and lodging. However, under certain circumstances, like accessing the remote locations described here, members may accept such hospitality. However, enjoying a weekend of recreation could give the appearance of infringing on one's objectivity at the very least. Therefore, any weekend activities, including lodging should be declined.

Rationale
ROW C
Whenever possible, members should pay for their own transportation and lodging. However, under certain circumstances, like accessing the remote locations described here, members may accept such hospitality. However, enjoying a weekend of recreation could give the appearance of infringing on one's objectivity at the very least. Therefore, any weekend activities, including lodging should be declined.

Question 25
L2ET-TBB202-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Paul Squires is an investment analyst who was a member of CFA Institute for 11 years before his membership was deactivated due to failure to pay applicable annual CFA Institute membership dues. In marketing communications with clients and prospective clients, Squires often states that he was a CFA Institute member in the past for 11 years. Squires has:

- (selected) Not violated Standard VII(B) reference to CFA Institute, the CFA Designation, and the CFA Program.
- Violated Standard VII(B) reference to CFA Institute, the CFA Designation, and the CFA Program, since he should not associate himself with CFA Institute when not an active member.
- Violated Standard VII(B) reference to CFA Institute, the CFA Designation, and the CFA Program, since he should seek permission from CFA Institute to reference his prior membership status when communicating with clients.

Rationale

This Answer is Correct

Individuals who are not active members of CFA Institute must not present themselves to others as active members; however, they are permitted to state that they were CFA Institute members in the past or refer to the years when their membership was active.

Question 26
L2R02TB-AC043-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Robert Lucia is an analyst preparing a report on FranCo Industries. He uses forecasted earnings per share as a key input to his valuation model. After listening to a management conference call with other analysts, Lucia uses the projected earnings suggested by the FranCo's CEO to value the firm without further analysis. In his report, he cites several of the reasons mentioned on the call to support his valuation. Did Lucia have a reasonable and adequate basis for his valuation?

- No.
- Yes, because the CEO is best equipped to estimate earnings.
- Yes, because he supported his valuation with several reasons.

Rationale
No.
Relying solely on the company's management estimates lacks the diligence necessary to perform a valuation analysis. While management's opinions might have analytical merit, they must be judged in light of other sources or analysis.

Rationale
Yes, because the CEO is best equipped to estimate earnings.
Relying solely on the company's management estimates lacks the diligence necessary to perform a valuation analysis. While management's opinions might have analytical merit, they must be judged in light of other sources or analysis.

Rationale
Yes, because he supported his valuation with several reasons.
Relying solely on the company's management estimates lacks the diligence necessary to perform a valuation analysis. While management's opinions might have analytical merit, they must be judged in light of other sources or analysis.

Question 27
L2R02TB-AC049-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Lyle Kent is a broker at Jackson & Phax (J&P), a discount brokerage firm that is expanding into research and asset management services. In an effort to generate business for the new units, J&P is offering an employee incentive of $500 for each new client referral from the brokerage unit that signs on with the asset management group. Kent has made several successful referrals in the first month without disclosing the incentive program. Did Kent violate the Standards of Professional Conduct?

- (selected) Yes.
- No, because the referral was directed toward his own firm.
- No, because the bonus is part of his employment compensation.

Rationale

✔ **Yes.**

The Standard does not prohibit referral fees or arrangements but requires that they be disclosed before entering into a service agreement so that the client can make an informed judgment as to the motivations of the providers.

Rationale

✖ **No, because the referral was directed toward his own firm.**

The Standard does not prohibit referral fees or arrangements but requires that they be disclosed before entering into a service agreement so that the client can make an informed judgment as to the motivations of the providers.

Rationale

✖ **No, because the bonus is part of his employment compensation.**

The Standard does not prohibit referral fees or arrangements but requires that they be disclosed before entering into a service agreement so that the client can make an informed judgment as to the motivations of the providers.

Question 28
L2ET-TB0007-1412
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Which of the following tools is *least likely* to be useful in ensuring members and candidates adhere to Standard II(A): Material Nonpublic Information?

- ◉ Restricted lists.
- ○ Firewalls.
- ○ Watch lists.

Rationale

This Answer is Correct

Restricted lists are used by investment banks writing research on issuers for which they also have an investment banking relationship. In order to avoid the investment banking conflict, firms should place these issuers on a restricted list and issue only factual information about the companies. Firewalls, which are barriers to information, and watch lists, which are lists of securities in which employees have sensitive information, are both used as recommended procedures for compliance with Standard II(A).

Question 29
L2R02TB-AC014-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Oscar Vansant is a portfolio manager with Starstruck Asset Managers (SAM). After being recruited by a competing firm, he resigns without a non-competition agreement. Upon beginning work at his new firm, Vansant solicits business from his former employer's clients using the telephone numbers he can recall and online business directories. Did Vansant violate the Standards of Professional Conduct?

- (selected) No.
- Yes, because all client contact information belongs to SAM.
- Yes, because recollection stems from his employment at SAM.

Rationale
No.
Upon exiting an employment relationship, members must adhere to any non-competition agreements. In the absence of one, members must refrain from taking any data, materials, contact lists, or proprietary methods from their former employer without first getting permission. However, the member's skills and memory are his own. Therefore, rebuilding, reconstructing, or seeking information through other means are not violations of the Standard.

Rationale
Yes, because all client contact information belongs to SAM.
Upon exiting an employment relationship, members must adhere to any non-competition agreements. In the absence of one, members must refrain from taking any data, materials, contact lists, or proprietary methods from their former employer without first getting permission. However, the member's skills and memory are his own. Therefore, rebuilding, reconstructing, or seeking information through other means are not violations of the Standard.

Rationale
Yes, because recollection stems from his employment at SAM.
Upon exiting an employment relationship, members must adhere to any non-competition agreements. In the absence of one, members must refrain from taking any data, materials, contact lists, or proprietary methods from their former employer without first getting permission. However, the member's skills and memory are his own. Therefore, rebuilding, reconstructing, or seeking information through other means are not violations of the Standard.

Question 30

L2ET-PQ0202-1502

LOS: LOS-5660

Lesson Reference: Lesson 1: Standard I: Professionalism

Difficulty: hard

Which of the following policies and procedures is *likely* to be appropriate for an individual to encourage their firms to consider in order to attempt to prevent violations of Standard I(A): Knowledge of the Law?

- ○ Training programs to give employees expert knowledge of relevant laws and regulations
- ◉ Adopting a code of ethics
- ○ Forced secondment to the compliance department for all employees within their first three years of employment

Rationale

✗ Training programs to give employees expert knowledge of relevant laws and regulations

Incorrect. Standard I(A) recommends that members and candidates encourage their firms to adopt a code of ethics. There is no recommendation under the Standard for employees to become experts in compliance, or spend time working in compliance.

Rationale

✓ Adopting a code of ethics

Correct. Standard I(A) recommends that members and candidates encourage their firms to adopt a code of ethics. There is no recommendation under the Standard for employees to become experts in compliance, or spend time working in compliance.

Rationale

✗ Forced secondment to the compliance department for all employees within their first three years of employment

Incorrect. Standard I(A) recommends that members and candidates encourage their firms to adopt a code of ethics. There is no recommendation under the Standard for employees to become experts in compliance, or spend time working in compliance.

Question 31
L2R02TB-AC022-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Richard Pulaski is an equity research analyst who wants to purchase shares in Technical Enterprises for his personal account. His supervisor has also asked him to write a recommendation for the stock, but Pulaski is concerned that the firm's reaction to his recommendation will drive up the share price. According to the Standards of Professional Conduct, Pulaski must:

- purchase shares for his personal account before making the recommendation.
- purchase shares for his personal account after making the recommendation.
- refrain from ever purchasing any shares for his personal account.

Rationale
purchase shares for his personal account before making the recommendation.
The Standard requires that members place the interests of their clients first, their employers second, and then their own last. Pulaski, while not prohibited from investing alongside his clients or employer, must first satisfy their entire orders before purchasing shares for himself.

Rationale
purchase shares for his personal account after making the recommendation.
The Standard requires that members place the interests of their clients first, their employers second, and then their own last. Pulaski, while not prohibited from investing alongside his clients or employer, must first satisfy their entire orders before purchasing shares for himself.

Rationale
refrain from ever purchasing any shares for his personal account.
The Standard requires that members place the interests of their clients first, their employers second, and then their own last. Pulaski, while not prohibited from investing alongside his clients or employer, must first satisfy their entire orders before purchasing shares for himself.

Question 32
L2ET-PQ0223-1502
LOS: LOS-5660
Lesson Reference: Lesson 4: Standard IV: Duties to Employers
Difficulty: hard
The chief compliance officer of an investment advisor is considering implementing a competition policy, a termination policy, and a whistle-blowing policy at their firm. How many of these policies are recommended procedures for compliance under Standard IV(A): Loyalty?

- ○ One
- ○ Two
- ◉ Three

Rationale
This Answer is Correct
All three policies are recommended procedures for compliance under Standard IV(A).

Question 33
L2R02TB-AC029-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium

Sarah Write, CFA, is an independent equity research analyst operating an investment advisory website that provides stock recommendations and reports. In addition to unsolicited research reports, Write also writes issuer- paid reports for a flat fee. Although the issuer-paid reports do not disclose the contractual relationship between Write and the subject company, her website user agreement includes the following statement. “Certain research may be performed at the request of the issuer.” Did Write violate the Standards of Professional Conduct?

- (selected) Yes.
- No, because she disclosed issuer-paid research in the user agreement.
- No, because the Standards do not apply to Internet websites.

Rationale

✅ **Yes.**

The Standards do not prohibit issuer-paid reporting. However, providing such services creates a potential conflict of interest. Analysts must take steps to preserve their independence and objectivity by only accepting a flat fee. The relationship between the analyst and the issuer must be fully disclosed in the report so that the reader may make an informed judgment as to its objectivity.

Rationale

❌ **No, because she disclosed issuer-paid research in the user agreement.**

The Standards do not prohibit issuer-paid reporting. However, providing such services creates a potential conflict of interest. Analysts must take steps to preserve their independence and objectivity by only accepting a flat fee. The relationship between the analyst and the issuer must be fully disclosed in the report so that the reader may make an informed judgment as to its objectivity.

Rationale

❌ **No, because the Standards do not apply to Internet websites.**

The Standards do not prohibit issuer-paid reporting. However, providing such services creates a potential conflict of interest. Analysts must take steps to preserve their independence and objectivity by only accepting a flat fee. The relationship between the analyst and the issuer must be fully disclosed in the report so that the reader may make an informed judgment as to its objectivity.

Question 34
L2R02TB-AC025-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Maria Gomez, CFA, is the marketing director for Regal Asset Managers (RAM). She is reviewing a promotional brochure for an upcoming conference and exhibition. The brochure highlights the fact that all four of the firm's portfolio managers are charterholders who passed the three exams in succession on their first attempts. It goes on to imply that this achievement will ensure RAM's funds will perform in the top of their peer groups. Is the brochure compliant with the Standards of Professional Conduct?

- ○ Yes.
- ○ No, it may not make reference to the fact that RAM's managers passed on the first attempt.
- ◉ No, because it implies that its CFA charterholders will achieve superior investment returns.

Rationale
✗ **Yes.**
Standard VII(B) allows members to make statements of fact as to their participation in the CFA Program but prohibits implying that investors can expect superior investment performance by virtue of the CFA designation. The implication that passing the exams on the first attempt somehow makes one charter more valuable than another is also a violation of this Standard.

Rationale
✗ **No, it may not make reference to the fact that RAM's managers passed on the first attempt.**
Standard VII(B) allows members to make statements of fact as to their participation in the CFA Program but prohibits implying that investors can expect superior investment performance by virtue of the CFA designation. The implication that passing the exams on the first attempt somehow makes one charter more valuable than another is also a violation of this Standard.

Rationale
✓ **No, because it implies that its CFA charterholders will achieve superior investment returns.**
Standard VII(B) allows members to make statements of fact as to their participation in the CFA Program but prohibits implying that investors can expect superior investment performance by virtue of the CFA designation. The implication that passing the exams on the first attempt somehow makes one charter more valuable than another is also a violation of this Standard.

Question 35
L2R02TB-AC055-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Jan Watson is a retired portfolio manager. As a retiree, he stopped paying dues to CFA Institute and has not filed his Professional Conduct Statement. He recently accepted a volunteer position as treasurer of his condominium association. The directory of association officers lists him as, “Jan Watson, CFA (retired).” Does Watson's use of the CFA designation violate the Standards of Professional Conduct?

- (selected) Yes.
- No, because retired members are not required to pay dues or file conduct statements.
- No, because he is not using the designation within the context of the investment industry.

Rationale
Yes.
Standard VII(B) does not make special provisions for retired members. CFA Institute does offer reduced dues for members who classify themselves as retired. Only after following the appropriate procedures and receiving notice from CFA Institute that their status has changed may Watson resume using the designation. Furthermore, altering the designation with “(retired)” is a violation of this standard.

Rationale
No, because retired members are not required to pay dues or file conduct statements.
Standard VII(B) does not make special provisions for retired members. CFA Institute does offer reduced dues for members who classify themselves as retired. Only after following the appropriate procedures and receiving notice from CFA Institute that their status has changed may Watson resume using the designation. Furthermore, altering the designation with “(retired)” is a violation of this standard.

Rationale
No, because he is not using the designation within the context of the investment industry.
Standard VII(B) does not make special provisions for retired members. CFA Institute does offer reduced dues for members who classify themselves as retired. Only after following the appropriate procedures and receiving notice from CFA Institute that their status has changed may Watson resume using the designation. Furthermore, altering the designation with “(retired)” is a violation of this standard.

Question 36
L2ET-TB0004-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium

Tom Steel is a director of a large investment bank. He is reviewing recent gifts declared by members of the research and investment departments. He notices three gifts declared in the current month listed below:

> Gift 1: An analyst declared the use of a corporate jet provided by an issuer to attend their premises when commercial transportation was available.
> Gift 2: A fund manager declared tickets to the rugby world cup final provided by a broker.
> Gift 3: A fund manager declared a breakfast paid for by a sell-side analyst at a meeting about current issues in their sector of coverage.

How many of the gifts listed above are likely to violate Standard I(B): Independence and Objectivity?

- ○ One.
- ◉ Two.
- ○ Three.

Rationale
✖ **One.**
Incorrect. Gift 1 is in violation of the Standard since members and candidates should pay for travel expenses in order to avoid the appearance of a conflict of interest. Gift 2 is in violation of the Standard since the gift is significant and could be seen to influence the fund manager's selection of broker when transacting. Gift 3 seems to be in the ordinary line of business and hence is not in breach of the Standard.

Rationale
✔ **Two.**
Correct. Gift 1 is in violation of the Standard since members and candidates should pay for travel expenses in order to avoid the appearance of a conflict of interest. Gift 2 is in violation of the Standard since the gift is significant and could be seen to influence the fund manager's selection of broker when transacting. Gift 3 seems to be in the ordinary line of business and hence is not in breach of the Standard.

Rationale
✖ **Three.**
Incorrect. Gift 1 is in violation of the Standard since members and candidates should pay for travel expenses in order to avoid the appearance of a conflict of interest. Gift 2 is in violation of the Standard since the gift is significant and could be seen to influence the fund manager's selection of broker when transacting. Gift 3 seems to be in the ordinary line of business and hence is not in breach of the Standard.

Question 37
L2R02TB-AC030-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Rafi Binder is an oil industry analyst at a brokerage firm. He recently read an article in the *Wall Street Journal* describing a research study that analyzed global oil reserves. Binder thinks this study would provide insight into the long-term movement of oil prices and wants to quote the study in a research report he is preparing. Using the Journal article to identify the author as Dr. Rangoon of State University, Binder obtained a copy of the original research study and used several excerpts in his oil industry report. In citing the source of the excerpts, Binder must credit:

	Wall Street Journal	*The Original Study*
A.	Yes	No
B.	No	Yes
C.	Yes	Yes

- ROW A
- ROW B
- ROW C

Rationale
ROW A
Binder must give credit to the original author of the study. Simply because he first learned of the study in the *Wall Street Journal* does not require him to cite it as a source.

Rationale
ROW B
Binder must give credit to the original author of the study. Simply because he first learned of the study in the *Wall Street Journal* does not require him to cite it as a source.

Rationale
ROW C
Binder must give credit to the original author of the study. Simply because he first learned of the study in the *Wall Street Journal* does not require him to cite it as a source.

Question 38
L2R02TB-AC040-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Allison Kinley is an analyst with Insight Research Associations (IRA). Kinley wants to start her own research firm and is planning to leave IRA. She meets with her supervisor to discuss her resignation, but no documentation of the meeting is produced. In anticipation of her departure, she copies several of the reports that she authored for IRA and downloads a forecasting spreadsheet that she and a colleague at IRA had developed. Did Kinley violate the Standards of Professional Conduct by:

	Copying Reports?	*Downloading Spreadsheets?*
A.	Yes	Yes
B.	Yes	No
C.	No	Yes

- ROW A
- ROW B
- ROW C

Rationale
ROW A
The reports and spreadsheets that Kinley produced as an employee at IRA belong to the firm. If she wishes to take them, she must first get her supervisor's consent. Kinley may recreate the reports and spreadsheets from memory after departing the firm.

Rationale
ROW B
The reports and spreadsheets that Kinley produced as an employee at IRA belong to the firm. If she wishes to take them, she must first get her supervisor's consent. Kinley may recreate the reports and spreadsheets from memory after departing the firm.

Rationale
ROW C
The reports and spreadsheets that Kinley produced as an employee at IRA belong to the firm. If she wishes to take them, she must first get her supervisor's consent. Kinley may recreate the reports and spreadsheets from memory after departing the firm.

Question 39

L2R02TB-AC003-1512

LOS: LOS-5650

Lesson Reference: Lesson 1: Standard I: Professionalism

Difficulty: medium

Eric Dickens, CFA, is a salesman with Jeta Investments. Jeta provides asset allocation and attribution analysis using an internally developed proprietary model. Jeta has one equity analyst on staff that primarily reviews third-party research reports for certain inputs used in the allocation model. During a presentation to a group of portfolio managers, Dickens is asked about his firm's stock selection methodologies. Dickens refers to the firm's team of analysts researching fundamental factors to identify stocks with above average return prospects. Did Dickens violate the Standards of Professional Conduct?

- No.
- Yes, by using third-party research reports.
- Yes, by overstating his firm's capabilities.

Rationale

No.

By stating or implying that the firm has a team of researchers on staff performing fundamental analysis, Dickens is misrepresenting his firm's capabilities. While the lone analyst evaluating third-party research might be adequate to perform the required tasks, Dickens must not overstate the firm's capabilities or resources.

Rationale

Yes, by using third-party research reports.

By stating or implying that the firm has a team of researchers on staff performing fundamental analysis, Dickens is misrepresenting his firm's capabilities. While the lone analyst evaluating third-party research might be adequate to perform the required tasks, Dickens must not overstate the firm's capabilities or resources.

Rationale

Yes, by overstating his firm's capabilities.

By stating or implying that the firm has a team of researchers on staff performing fundamental analysis, Dickens is misrepresenting his firm's capabilities. While the lone analyst evaluating third-party research might be adequate to perform the required tasks, Dickens must not overstate the firm's capabilities or resources.

Question 40
L2ET-PQ0225-1502
LOS: LOS-5660
Lesson Reference: Lesson 4: Standard IV: Duties to Employers
Difficulty: hard
Which of the following situations is *least likely* to lead to a violation of Standard IV(B): Additional Compensation Arrangements?

- ○ Full written disclosure is given to the employer prior to receiving any additional compensation.
- ○ Verbal disclosure is given to the employer prior to entering into the agreement.
- ◉ Full written consent is given by the employer prior to entering into the agreement.

Rationale

❌ **Full written disclosure is given to the employer prior to receiving any additional compensation.**
Incorrect. Standard IV(B) requires members and candidates to obtain written permission from their employer before accepting compensation or other benefits from third parties for the services rendered to the employer or for any services that might create a conflict with their employer's interest.

Rationale

❌ **Verbal disclosure is given to the employer prior to entering into the agreement.**
Incorrect. Standard IV(B) requires members and candidates to obtain written permission from their employer before accepting compensation or other benefits from third parties for the services rendered to the employer or for any services that might create a conflict with their employer's interest.

Rationale

✅ **Full written consent is given by the employer prior to entering into the agreement.**
Correct. Standard IV(B) requires members and candidates to obtain written permission from their employer before accepting compensation or other benefits from third parties for the services rendered to the employer or for any services that might create a conflict with their employer's interest.

Question 41
L2R02TB-AC011-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Leslie Prist is the marketing director for Xion Investments. Xion manages a variety of open- and closed-end mutual funds. A brochure Prist sent to prospective investors stated, “Our funds have beaten their benchmark indices by an average of 5 percentage points over the last 10 years.” Which of the following practices would violate the Standards of Professional Conduct?

- ○ Failing to list the funds' benchmarks in the brochure.
- ○ Using a geometric mean instead of an arithmetic mean.
- ◉ Changing fund benchmarks on an ex post basis.

Rationale
✖ **Failing to list the funds' benchmarks in the brochure.**
The Standards do not require compliance with the Global Investment Performance Standards (GIPS). However, performance presentation must be clear, accurate, and complete. Changing the fund's benchmark after the fact would be a misrepresentation of its performance. Benchmarks must be stated in advance of the performance period and should only be changed if the fund's investment mandate or strategy changes in a way that renders the old benchmark obsolete.

Rationale
✖ **Using a geometric mean instead of an arithmetic mean.**
The Standards do not require compliance with the Global Investment Performance Standards (GIPS). However, performance presentation must be clear, accurate, and complete. Changing the fund's benchmark after the fact would be a misrepresentation of its performance. Benchmarks must be stated in advance of the performance period and should only be changed if the fund's investment mandate or strategy changes in a way that renders the old benchmark obsolete.

Rationale
✔ **Changing fund benchmarks on an ex post basis.**
The Standards do not require compliance with the Global Investment Performance Standards (GIPS). However, performance presentation must be clear, accurate, and complete. Changing the fund's benchmark after the fact would be a misrepresentation of its performance. Benchmarks must be stated in advance of the performance period and should only be changed if the fund's investment mandate or strategy changes in a way that renders the old benchmark obsolete.

Question 42
L2R02TB-AC005-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Bryan Haver, CFA, is a salesman at Asset Allocation Services. He frequently takes clients and prospects to lunch where he often consumes several drinks, becoming intoxicated. His assistant handles his calls and most other duties on days when Haver has one of these lunch meetings with clients, while Haver naps on the couch in his office. Is Haver in violation of the Standards of Professional Conduct?

- (selected) Yes.
- No, because entertaining clients is part of his job as a salesman.
- No, because his assistant handles his duties while he naps.

Rationale
✔ **Yes.**
The Standards require that members exhibit professionalism and competence in all their activities. Frequent intoxication, particularly with clients, reflects poorly on the member, the industry, and the CFA charter.

Rationale
✖ **No, because entertaining clients is part of his job as a salesman.**
The Standards require that members exhibit professionalism and competence in all their activities. Frequent intoxication, particularly with clients, reflects poorly on the member, the industry, and the CFA charter.

Rationale
✖ **No, because his assistant handles his duties while he naps.**
The Standards require that members exhibit professionalism and competence in all their activities. Frequent intoxication, particularly with clients, reflects poorly on the member, the industry, and the CFA charter.

Question 43
L2ET-PQ0229-1502
LOS: LOS-5650
Lesson Reference: Lesson 5: Standard V: Investment Analysis, Recommendations, and Actions
Difficulty: hard
Bella Burton is a successful fund manager focusing on special situations such as distressed equity. Many of the investments that Burton makes are in stocks with market capitalization of less than US$100 million. After a recent market downturn, the number of distressed equity opportunities has risen significantly due to business conditions becoming tough and companies losing access to traditional bank funding. Burton has been very successful running a small fund of US$50 million following the distressed equity strategy and her firm wishes to capitalize on this track record to increase funds under management. Her firm embarks upon a fund raising aiming to increase funds under management by US$1 billion by marketing the performance of the distressed equity strategy to pension funds and endowments. According to Standard V(B)—Communication with Clients and Prospective Clients, Burton should decline to be part of the fund raising unless:

- (selected) Liquidity and capacity issues are made clear to prospective investors.
- Current investors are given first refusal on investment in the new fund.
- At least 10 years of performance presentation is included in the marketing presentation.

Rationale

✓ Liquidity and capacity issues are made clear to prospective investors.

Correct. Standard V(B) Communications with Clients and Prospective Clients states that members and candidates must report the existence of limitations significant to the decision-making process. Examples of such factors and attributes include, but are not limited to, investment liquidity and capacity. Liquidity is the ability to liquidate an investment on a timely basis at a reasonable cost. Capacity is the investment amount beyond which returns will be negatively affected by new investments. In this case, it is clear that the strategy has only been tested for relatively small amounts of capital. Given also the small market capitalizations of the target investments, the liquidity and capacity issues of investing a higher amount of capital into the strategy should be clearly raised with prospective investors.

Rationale

✗ Current investors are given first refusal on investment in the new fund.

Incorrect. Standard V(B) Communications with Clients and Prospective Clients states that members and candidates must report the existence of limitations significant to the decision-making process. Examples of such factors and attributes include, but are not limited to, investment liquidity and capacity. Liquidity is the ability to liquidate an investment on a timely basis at a reasonable cost. Capacity is the investment amount beyond which returns will be negatively affected by new investments. In this case, it is clear that the strategy has only been tested for relatively small amounts of capital. Given also the small market capitalizations of the target investments, the liquidity and capacity issues of investing a higher amount of capital into the strategy should be clearly raised with prospective investors.

Rationale

✗ At least 10 years of performance presentation is included in the marketing presentation.

Incorrect. Standard V(B) Communications with Clients and Prospective Clients states that members and candidates must report the existence of limitations significant to the decision-making process. Examples of such factors and attributes include, but are not limited to, investment liquidity and capacity. Liquidity is the ability to liquidate an investment on a timely basis at a reasonable cost. Capacity is the investment amount beyond which returns will be negatively affected by new investments. In this case, it is clear that the strategy has only been tested for relatively small amounts of capital. Given also the small market capitalizations of the target investments, the liquidity and capacity issues of investing a higher amount of capital into the strategy should be clearly raised with prospective investors.

Question 44
L2R02TB-AC036-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Bravo Asset Managers handles a variety of institutional, private accounts, and hedge funds. The firm has a policy of allocating block trades and oversubscribed issues by order of priority. The best priced transactions are first allocated to the appropriate hedge fund, then institutional accounts, and lastly private accounts. As a result, the hedge funds usually outperform other accounts, even when they invest in the same assets at the same time. Bravo's new account documentation spells out this policy and requires the signatory to accept the terms in writing. Does this policy violate the Standards of Professional Conduct with respect to fair dealing?

- (selected) Yes.
- No, because the policy is disclosed and accepted by account holders.
- No, because the policy is applied consistently to all trades.

Rationale

✔ **Yes.**

The Standard does not allow managers to favor certain clients over others with respect to allocating trades. All shares should be allocated among client accounts at the average price. The Standards do not allow managers to subject clients to patently unfair policies even if the clients consent.

Rationale

✘ **No, because the policy is disclosed and accepted by account holders.**

The Standard does not allow managers to favor certain clients over others with respect to allocating trades. All shares should be allocated among client accounts at the average price. The Standards do not allow managers to subject clients to patently unfair policies even if the clients consent.

Rationale

✘ **No, because the policy is applied consistently to all trades.**

The Standard does not allow managers to favor certain clients over others with respect to allocating trades. All shares should be allocated among client accounts at the average price. The Standards do not allow managers to subject clients to patently unfair policies even if the clients consent.

Question 45
L2ET-TBB208-1412
LOS: LOS-5650
Lesson Reference: Lesson 5: Standard V: Investment Analysis, Recommendations, and Actions
Difficulty: medium

Xavier Stephens, CFA, is a research analyst who is preparing a research report concerning a new biotechnology company involved in the development of drugs used to treat diseases of the immune system. In the course of his research, he consults medical experts on the likely success of the drugs being trialed by the company. The experts are very confident that the trials will likely be successful and that the company will go on to sign major contracts with pharmaceutical companies. Stephens includes this information in his research and concludes the following:

“Based on the fact that the trials are going to be successful, we initiate coverage on the company with a strong buy rating.”

Which of the following Standards is *most likely* to have been violated by Stephens?

- ○ Standard II(A): Material Nonpublic Information.
- ○ Standard V(A): Diligence and Reasonable Basis.
- ◉ Standard V(B): Communication with Clients and Prospective Clients.

Rationale
✗ **Standard II(A): Material Nonpublic Information.**
Incorrect. Answer A is incorrect since the opinion of experts is unlikely to be material information. Answer B is incorrect since relying on expert opinion is a reasonable basis for research conclusions. Answer C is correct, since Stephens has stated the experts' opinions as fact rather than opinion, which is a breach of the requirement of Standard V(B).

Rationale
✗ **Standard V(A): Diligence and Reasonable Basis.**
Incorrect. Answer A is incorrect since the opinion of experts is unlikely to be material information. Answer B is incorrect since relying on expert opinion is a reasonable basis for research conclusions. Answer C is correct, since Stephens has stated the experts' opinions as fact rather than opinion, which is a breach of the requirement of Standard V(B).

Rationale
✓ **Standard V(B): Communication with Clients and Prospective Clients.**
Correct. Answer A is incorrect since the opinion of experts is unlikely to be material information. Answer B is incorrect since relying on expert opinion is a reasonable basis for research conclusions. Answer C is correct, since Stephens has stated the experts' opinions as fact rather than opinion, which is a breach of the requirement of Standard V(B).

Question 46
L2R02TB-AC004-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Karl Lender, CFA, is a money manager for high-net-worth individuals. In addition to portfolio management services, Lender also distributes an investment newsletter to all his clients. The newsletter is based on several proprietary research services that Lender purchases from brokerage firms. Lender summarizes the proprietary reports, adds his own commentary, and distributes the newsletter as solely his own work. Has Lender violated the Standards of Professional Conduct?

- ○ No.
- ○ Yes, by distributing third-party research to his clients.
- ◉ Yes, by presenting the newsletter as his own work.

Rationale
✖ **No.**
Lender is effectively taking credit for the work of others. Summarizing third-party research does not necessarily violate the Standards, but the sources of those summaries must be cited and never presented as his own work.

Rationale
✖ **Yes, by distributing third-party research to his clients.**
Lender is effectively taking credit for the work of others. Summarizing third-party research does not necessarily violate the Standards, but the sources of those summaries must be cited and never presented as his own work.

Rationale
✔ **Yes, by presenting the newsletter as his own work.**
Lender is effectively taking credit for the work of others. Summarizing third-party research does not necessarily violate the Standards, but the sources of those summaries must be cited and never presented as his own work.

Question 47
L2ET-PQ0205-1502
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: hard
Graham Munten is preparing a performance presentation for a prospective investor. Currently Munten's firm runs two hedge funds with very similar mandates, however, Munten instructs his team to produce a presentation based only on the best performing fund, and only show data for a period of strong performance. Which of the following statements regarding Munten's actions is most accurate?

- ( ) Munten has violated Standard I(C): Misrepresentation.
- ( ) Munten has not violated Standard I(C) but has violated other Standards of Professional Conduct.
- (•) Munten has violated Standard I(C) alongside other Standards of Professional Conduct.

Rationale

Munten has violated Standard I(C): Misrepresentation.
Incorrect. Munten is clearly being unethical in his choice of data to display in the presentation. His “cherry picking” of fund and time period is a violation of Standard I(C): Misrepresentation plus Standard III(D): Performance Presentation.

Rationale

Munten has not violated Standard I(C) but has violated other Standards of Professional Conduct.
Incorrect. Munten is clearly being unethical in his choice of data to display in the presentation. His “cherry picking” of fund and time period is a violation of Standard I(C): Misrepresentation plus Standard III(D): Performance Presentation.

Rationale

Munten has violated Standard I(C) alongside other Standards of Professional Conduct.
Correct. Munten is clearly being unethical in his choice of data to display in the presentation. His “cherry picking” of fund and time period is a violation of Standard I(C): Misrepresentation plus Standard III(D): Performance Presentation.

Question 48
L2ET-PQ0209-1502
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: hard
Jimmy Webb is a stock broker for a mid-tier sell-side investment firm. Webb receives a text message from one of his colleagues one evening indicating that he believes it is likely a certain company is likely to issue a profits warning in the next couple of days. Webb is aware that he has a large sell order open and resolves to complete the order that day. The next day the company does indeed issue a profit warning and the stock falls heavily. Which of the following statements is *most likely* to be accurate?

- Webb is in violation of Standard II(A): Material Nonpublic Information.
- Both Webb and his colleague are in violation of Standard II(A): Material Nonpublic Information.
- Neither Webb nor his broker is in violation of Standard II(A): Material Nonpublic Information.

Rationale

Webb is in violation of Standard II(A): Material Nonpublic Information.

Incorrect. It is unlikely that this information would be deemed material, since it is based on opinion and therefore would most likely be considered market noise. There are often rumors and whisper numbers before a release of any kind. Unless Webb knew that the colleague had an ongoing business relationship with the company, he had no reason to suspect he was receiving material nonpublic information that would prevent him from completing the order of the client.

Rationale

Both Webb and his colleague are in violation of Standard II(A): Material Nonpublic Information.

Incorrect. It is unlikely that this information would be deemed material, since it is based on opinion and therefore would most likely be considered market noise. There are often rumors and whisper numbers before a release of any kind. Unless Webb knew that the colleague had an ongoing business relationship with the company, he had no reason to suspect he was receiving material nonpublic information that would prevent him from completing the order of the client.

Rationale

Neither Webb nor his broker is in violation of Standard II(A): Material Nonpublic Information.

Correct. It is unlikely that this information would be deemed material, since it is based on opinion and therefore would most likely be considered market noise. There are often rumors and whisper numbers before a release of any kind. Unless Webb knew that the colleague had an ongoing business relationship with the company, he had no reason to suspect he was receiving material nonpublic information that would prevent him from completing the order of the client.

Question 49
L2ET-TBX107-1502
LOS: LOS-5650
Lesson Reference: Lesson 7: Standard VII: Responsibilities as a CFA Institute Member or CFA Candidate
Difficulty: easy
Juan Smitero has recently earned the right to use the CFA designation and wishes to update his profile name on a social networking platform. Which of the following names is *least likely* to be in violation of Standard VII(B): Reference to CFA Institute, the CFA Designation, and the CFA Program?

- Swiss Banker, CFA.
- Smitero, C.F.A.
- Juan Smitero, Chartered Financial Analyst.

Rationale

This Answer is Correct

The first option is incorrect since online account names that obscure true identity should not be tagged with the CFA designation. The second option is incorrect since the CFA logo does not have periods between the letters.

Question 50
L2R02TB-AC037-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Shelly Swain is a money manager dealing with private wealth clients. Her client, Thomas Wells, is averse to investing in international securities, which he considers too risky. Swain is aware of the diversification benefits of adding international equities to domestic-only portfolios. Wells is scheduled to meet with Swain to review his investment policy statement (IPS). Swain's *best* course of action is to:

- add international equities to the portfolio prior to the meeting.
- insist that Wells remove the constraint on her asset management.
- educate Wells about the diversification benefits and alter the IPS.

Rationale

add international equities to the portfolio prior to the meeting.
While managers should make investment decisions from a portfolio perspective, they must also follow the directives and mandates imposed by the client. However, part of the manager's duty is to educate the client about diversification and the benefits of adding low-correlation assets to his portfolio. Swain may only add the international exposure after convincing Wells to adjust the IPS.

Rationale

insist that Wells remove the constraint on her asset management.
While managers should make investment decisions from a portfolio perspective, they must also follow the directives and mandates imposed by the client. However, part of the manager's duty is to educate the client about diversification and the benefits of adding low-correlation assets to his portfolio. Swain may only add the international exposure after convincing Wells to adjust the IPS.

Rationale

educate Wells about the diversification benefits and alter the IPS.
While managers should make investment decisions from a portfolio perspective, they must also follow the directives and mandates imposed by the client. However, part of the manager's duty is to educate the client about diversification and the benefits of adding low-correlation assets to his portfolio. Swain may only add the international exposure after convincing Wells to adjust the IPS.

Question 51
L2R02TB-AC033-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Sandy Dixon is a portfolio manager for a major manufacturer's pension fund. Two years ago, she began accumulating shares in AccuTech based on favorable recommendations from several analysts. After completing the fund's large position, she advised several friends and family members to also buy shares. Based on more recent reports provided by third-party analysts, Dixon decides to sell the fund's entire holding in AccuTech very quickly. Realizing that the large block sale would likely have a detrimental effect on the stock price and because the smaller holdings are unlikely to impact the price, she advises her friends and family to liquidate their positions ahead of the fund's imminent sale. Did Dixon's recommendations violate the Standards of Professional Conduct with respect to the:

	Buy	*Sell*
A.	Yes	Yes
B.	Yes	No
C.	No	Yes

- ROW A
- ROW B
- ROW C (selected)

Rationale
ROW A (incorrect)
In the first instance, Dixon purchased the entire allotment of shares for the fund and then recommended it to others. Any impact from her fund's trading into the position would have already been reflected in the price of the shares. In the second instance, Dixon advises others to exit the stock ahead of the fund's trades. This is tantamount to front-running where her friends and family will benefit from exiting their positions before the price impact of the fund's trades are reflected. However, the fund will likely receive a lower average price for its shares because of the price impact from the other trades.

Rationale
ROW B (incorrect)
In the first instance, Dixon purchased the entire allotment of shares for the fund and then recommended it to others. Any impact from her fund's trading into the position would have already been reflected in the price of the shares. In the second instance, Dixon advises others to exit the stock ahead of the fund's trades. This is tantamount to front-running where her friends and family will benefit from exiting their positions before the price impact of the fund's trades are reflected. However, the fund will likely receive a lower average price for its shares because of the price impact from the other trades.

Rationale
ROW C (correct)
In the first instance, Dixon purchased the entire allotment of shares for the fund and then recommended it to others. Any impact from her fund's trading into the position would have already been reflected in the price of the shares. In the second instance, Dixon advises others to exit the stock ahead of the fund's trades. This is tantamount to front-running where her friends and family will benefit from exiting their positions before the price impact of the fund's trades are reflected. However, the fund will likely receive a lower average price for its shares because of the price impact from the other trades.

Question 52
L2ET-TB0008-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
An investment manager has received a directed brokerage order from their client. According to the Code and Standards, the manager should:

- ○ Refuse to execute the order.
- ○ Execute the order immediately.
- ◉ Execute the order but disclose to the client that they might not be getting best execution.

Rationale

This Answer is Correct

Directed brokerage arrangements do not breach any duty of loyalty between the manager and the client since the brokerage is the property of the client. However, the manager should still seek best execution and seek assurance from the client that the goods or services purchased from the brokerage will benefit account beneficiaries. The member or candidate should also disclose to the client that they may not be getting best execution.

Question 53
L2ET-TB0014-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Michael Lapin sits on the board of his local soccer team and regularly attends their matches as an avid supporter. In return for his services on the board, Lapin receives unlimited membership privileges for his family at all of the soccer club facilities, including use of vehicles owned by the club and use of the gymnasium facilities of the club. Lapin and his family also get to attend all matches free of charge. Lapin does not disclose this arrangement to his employer because he does not receive monetary compensation for his services and the soccer club is not in direct competition with his employer. Lapin owns a small holding in the soccer club in one of his client accounts. Lapin has *most likely*:

- (selected) Violated Standard IV(B): Additional Compensation Arrangements by failing to disclose the arrangement.
- Not violated Standard IV(B): Additional Compensation Arrangements since the compensation is nonmonetary.
- Not violated Standard IV(B): Additional Compensation Arrangements since the soccer club is not in direct competition with his employer.

Rationale
✔ **Violated Standard IV(B): Additional Compensation Arrangements by failing to disclose the arrangement.**
Correct. Standard IV(B): Additional Compensation Arrangements applies to all gifts, benefits, compensation, or consideration that competes with or might reasonably be expected to create a conflict of interest with their employer's interests unless they obtain written consent from all parties involved.

Rationale
✘ **Not violated Standard IV(B): Additional Compensation Arrangements since the compensation is nonmonetary.**
Incorrect. Standard IV(B): Additional Compensation Arrangements applies to all gifts, benefits, compensation, or consideration that competes with or might reasonably be expected to create a conflict of interest with their employer's interests unless they obtain written consent from all parties involved.

Rationale
✘ **Not violated Standard IV(B): Additional Compensation Arrangements since the soccer club is not in direct competition with his employer.**
Incorrect. Standard IV(B): Additional Compensation Arrangements applies to all gifts, benefits, compensation, or consideration that competes with or might reasonably be expected to create a conflict of interest with their employer's interests unless they obtain written consent from all parties involved.

Question 54
L2R02TB-AC045-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Kevin Wang is a portfolio manager at A-Plus Advisors. He makes asset allocation decisions based on third-party economic reports and the investment policy statements of each client. A-Plus maintains client records by scanning documents into an electronic database and has a policy to purge records after five years. Wang is diligent in ensuring that client investment policy statements are scanned but relies on third-party vendors to archive economic reports. Did Wang violate the Standards of Professional Conduct with respect to:

	Client Records?	*Economic Reports?*
A.	Yes	Yes
B.	Yes	No
C.	No	Yes

- ROW A
- ROW B
- ROW C (selected)

Rationale
ROW A
The Standard requires that Wang maintain his own records in support of his investment decisions. By relying on the vendors to retain the economic reports, he has failed to meet his obligations under the Standard. Storing client records in electronic forms is acceptable under the Standard. Only in the absence of explicit company policies, does the Standard recommend that records be retained for seven years.

Rationale
ROW B
The Standard requires that Wang maintain his own records in support of his investment decisions. By relying on the vendors to retain the economic reports, he has failed to meet his obligations under the Standard. Storing client records in electronic forms is acceptable under the Standard. Only in the absence of explicit company policies, does the Standard recommend that records be retained for seven years.

Rationale
ROW C
The Standard requires that Wang maintain his own records in support of his investment decisions. By relying on the vendors to retain the economic reports, he has failed to meet his obligations under the Standard. Storing client records in electronic forms is acceptable under the Standard. Only in the absence of explicit company policies, does the Standard recommend that records be retained for seven years.

Question 55

L2ET-TBX105-1502

LOS: LOS-5650

Lesson Reference: Lesson 6: Standard VI: Conflicts of Interest

Difficulty: easy

Jessie Cyrus is an investment manager; her brother William is a financial lawyer. When Jessie has a client in need of legal advice, she introduces them to her brother at a reduced rate. William also introduces his customers in need of investment management services to his sister at a reduced rate. Neither Jessie nor William has disclosed this arrangement to their employer. Specifically with respect to Standard VI(C): Referral Fees, which of the following statements is *most* accurate?

- (selected) Both Jessie and William are in breach of the Standard.
- The Standard has not been breached since the clients are being introduced at a reduced rate, and hence Jessie and William are not profiting from the arrangement.
- The Standard has not been breached since there is no benefit being paid for referral of potential customers.

Rationale

This Answer is Correct

Standard VI(C) states the responsibility of members and candidates to inform their employer, clients, and prospective clients of any benefit received for referrals of customers and clients. The benefit can be either monetary or nonmonetary. In this arrangement, the benefit to each Cyrus sibling from referring their clients to the other sibling is reciprocation of the act. As such, this referral fee arrangement should be disclosed.

Question 56
L2R02TB-AC024-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium

Rita Ross serves as a member of the CFA Institute Council of Examiners and participates in a preview of the CFA exam to be administered the following month. She is also a university professor with several students planning to sit for the upcoming exam. One of her students is having difficulty memorizing a complex formula, which unbeknownst to the student, will not appear on the exam. Ross advises the candidate that a perfect score is not required to pass and that her time would be better spent on other areas of the curriculum. Did Ross violate the Standards of Professional Conduct with her advice?

- (selected) No.
- Yes, because she gave an unfair advantage to her student.
- Yes, because she is privy to the contents of the upcoming exam.

Rationale

No. (correct)

The advice that Ross gave to her student was not particular to the content of the exam and, therefore, did not endanger its integrity.

Rationale

Yes, because she gave an unfair advantage to her student. (incorrect)

The advice that Ross gave to her student was not particular to the content of the exam and, therefore, did not endanger its integrity.

Rationale

Yes, because she is privy to the contents of the upcoming exam. (incorrect)

The advice that Ross gave to her student was not particular to the content of the exam and, therefore, did not endanger its integrity.

Question 57
L2ET-TB0017-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Standard V(A): Diligence and Reasonable Basis states that members and candidates:

- Cannot employ external advisers and subadvisers.
- Can use external advisers and subadvisers to absolve responsibility for diligence and reasonable basis.
- Can use external advisers and subadvisers provided they review external managers as diligently as they review individual funds and securities.

Rationale

This Answer is Correct

Under Standard V(A), members and candidates may appoint external advisers and subadvisers; however, the standard applies to the level of review necessary in selecting such adviser. Members and candidates must review managers as diligently as they review individual funds and securities.

Question 58
L2ET-TBB210-1412
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
According to Standard III(A): Loyalty, Prudence and Care, members and candidates in control of client assets should submit an itemized statement:

- ○ As often as necessary.
- ◉ At least quarterly.
- ○ At least annually.

Rationale

This Answer is Correct

The recommended procedures for compliance for Standard III(A): Loyalty, Prudence, and Care state that members and candidates with control of client assets should submit to each client an itemized statement at least quarterly.

Question 59
L2R02TB-AC038-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Jason Kessler is responsible for performance reporting for GenZ Investments. The firm's largest portfolios' performance records are compiled using the Global Investment Performance Standards (GIPS), but Kessler's supervisor feels that smaller portfolio's do not justify the added cost of GIPS compliance. GIPS require that the standards be applied on a firmwide basis to qualify for a valid claim of GIPS-compliant reporting. Kessler adds a GIPS compliance statement to each of the large portfolios' performance records, but not the small portfolios'. Did Kessler violate GIPS or the Standards of Professional Conduct?

	GIPS	*Standards of Professional Conduct*
A.	Yes	Yes
B.	Yes	No
C.	No	Yes

- ROW A (selected)
- ROW B
- ROW C

Rationale
✅ **ROW A**
GIPS must be applied on a firmwide basis. Therefore, if the Standards are only applied to some portfolios, a valid claim of compliance cannot be made for any of the portfolios. Making a claim of compliance with GIPS when the performance presentation does not conform to GIPS is itself a misrepresentation and a violation of the Standard.

Rationale
❌ **ROW B**
GIPS must be applied on a firmwide basis. Therefore, if the Standards are only applied to some portfolios, a valid claim of compliance cannot be made for any of the portfolios. Making a claim of compliance with GIPS when the performance presentation does not conform to GIPS is itself a misrepresentation and a violation of the Standard.

Rationale
❌ **ROW C**
GIPS must be applied on a firmwide basis. Therefore, if the Standards are only applied to some portfolios, a valid claim of compliance cannot be made for any of the portfolios. Making a claim of compliance with GIPS when the performance presentation does not conform to GIPS is itself a misrepresentation and a violation of the Standard.

Question 60
L2ET-TB0012-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Pat Levett has been accused of violating Standard III(E): Client Confidentiality since he has disclosed information relating to his clients recently on two separate occasions. On the first occasion, Levett disclosed information about his current clients in a marketing presentation to prospective clients, having first received the permission of his current clients. On the second occasion, Levett disclosed information regarding the activity of a former client through an electronic communication on a social networking website. Levett has *most likely:*

- ○ Not violated the standard on either occasion.
- ◉ Violated the standard on one occasion.
- ○ Violated the standard on both occasions.

Rationale

This Answer is Correct

Standard III(E): Preservation of Confidentiality states that members and candidates must keep information about current, former, and prospective clients confidential unless the information concerns illegal activities on the part of the client, disclosure is required by law, or the client permits disclosure of the information. In this case, Levett violated the Standard in the second instance but not the first instance since he obtained client permission to disclose the information.

Question 61
L2ET-PQ0216-1502
LOS: LOS-5650
Lesson Reference: Lesson 3: Standard III: Duties to Clients
Difficulty: hard
According to Standard III(C)—Suitability, an investment manager is

- ○ Prevented from using outsourced sub-managers to manage funds.
- ○ Relieved of the duty to ensure suitability when management is outsourced to a sub-manager.
- ● Responsible for ensuring that the new manager's services are appropriate for clients.

Rationale

This Answer is Correct

In order to adhere to the requirements of Standard III(C)—Suitability, a manager needs to ensure that any external manager or sub-manager is offering services that are appropriate to their clients.

Question 62
L2ET-TB0015-1412
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Which of the following incentive structures is *most likely* to be appropriate under Standard IV(C): Responsibilities of Supervisors? An incentive structure that aligns employee compensation with:

- Sales figures.
- Number of new clients.
- Long-term profitability.

Rationale
This Answer is Correct
Under Standard IV(C): Responsibilities of Supervisors, supervisors should consider that the incentive schemes that are used by the firm are not driven by short-term targets and that the schemes should focus on how outcomes are achieved rather than what is achieved. Focusing on sales figures and number of new clients is likely turning a blind eye to ethically inappropriate conduct in order to hit short-term targets. It is more likely that outcomes are achieved ethically when compensation is aligned with long-term profitability.

Question 63
L2ET-TB0005-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Which of the following analysts is *least likely* to be in violation of Standard I(C): Misrepresentation?

- (selected) An analyst who uses research and models created by prior employees of the firm with attribution.
- An analyst who reissues research previously released by an analyst that has since left the firm under his own name without attribution.
- An analyst who presents statistical estimates of forecasts prepared by others and identifies the sources but omits qualifying statements to the research.

Rationale

This Answer is Correct

Research and models developed while employed by the firm are the property of a firm, and the firm retains the right to continue using the work after the member or candidate has left the organization; hence, the first option is not a violation of the Standard. The second option is a violation due to plagiarism of the previous analysts' work, and the third option is a violation since omitting the qualifying statements to the research is engaging in misrepresentation of the research, even if the original source is cited.

Question 64

L2R02TB-AC023-1512

LOS: LOS-5660

Lesson Reference: Lesson 1: Standard I: Professionalism

Difficulty: medium

Sandy Lane is an investment advisor specializing in individual retirement accounts. Mark Pico is the general partner at a regional brokerage firm. In exchange for client referrals, Lane agrees to place all her trades through Pico's firm. When a prospective client calls Lane based on Pico's recommendation, Lane must disclose the terms of the referral arrangement:

- upon request.
- before executing any trades.
- before signing the client to a service agreement.

Rationale

upon request.

The Standard does not prohibit referral fees or arrangements but requires that they be disclosed before entering into a service agreement so that the client can make an informed judgment as to the motivations of the providers.

Rationale

before executing any trades.

The Standard does not prohibit referral fees or arrangements but requires that they be disclosed before entering into a service agreement so that the client can make an informed judgment as to the motivations of the providers.

Rationale

before signing the client to a service agreement.

The Standard does not prohibit referral fees or arrangements but requires that they be disclosed before entering into a service agreement so that the client can make an informed judgment as to the motivations of the providers.

Question 65
L2ET-TBX106-1502
LOS: LOS-5650
Lesson Reference: Lesson 7: Standard VII: Responsibilities as a CFA Institute Member or CFA Candidate
Difficulty: easy
Which of the following statements made by a recent CFA Level III candidate is most likely to be in violation of Standard VII(A): Conduct as Participants in CFA Institute Programs?

- "The exam seemed to be very easy compared to recent papers."
- "The content is completely irrelevant to my day-to-day activities at work."
- "I was delighted to see there was not a large number of questions on swaps—thankful since that was one of my weakest areas."

Rationale

This Answer is Correct

Revealing portions of the curriculum covered in the exam and areas not covered is a breach of Standard VII(A). Expressing an opinion on the difficulty of the exam or an adverse opinion on the CFA Program curriculum is not a violation of the Standard.

Question 66

L2ET-PQ0213-1502

LOS: LOS-5660

Lesson Reference: Lesson 2: Standard II: Integrity of Capital Markets

Difficulty: hard

All of the following procedures are recommended for compliance with Standard III(A): Loyalty, Prudence, and Care, except:

- ○ Establish the investment objectives of the client prior to engaging in business.
- ○ Diversify.
- ◉ Avoid conflicts of interest.

Rationale

This Answer is Correct

Standard II(A): Loyalty, Prudence, and Care recommends that members and candidates should address and encourage their firms to include policies on disclosing conflicts of interest, not avoiding them. Answers A and B are recommended procedures for compliance with the Standard.

Question 67
L2R02TB-AC039-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Lyndon Price is a financial planner advising private wealth clients. One of his clients, Shaun Mulligan, is a retired technology entrepreneur with an interest in social causes supporting education. Price sits on the board of a charitable foundation dedicated to providing computers to underprivileged high school students. As part of the foundation's fund raising efforts, Price compiles a list of names of potential donors, including Mulligan's, to the outreach chairperson. Did Price violate the Standards of Professional Conduct?

- No.
- Yes, unless he first obtains permission from Mulligan.
- Yes, even if he first obtains permission from Mulligan.

Rationale
No.
Price may not disclose any client information to an outside party without first getting his consent. By disseminating lists of potential donors from his clients' records without their consent, he is violating the Confidentiality Standard.

Rationale
Yes, unless he first obtains permission from Mulligan.
Price may not disclose any client information to an outside party without first getting his consent. By disseminating lists of potential donors from his clients' records without their consent, he is violating the Confidentiality Standard.

Rationale
Yes, even if he first obtains permission from Mulligan.
Price may not disclose any client information to an outside party without first getting his consent. By disseminating lists of potential donors from his clients' records without their consent, he is violating the Confidentiality Standard.

Question 68
L2ET-PQ0217-1502
LOS: LOS-5660
Lesson Reference: Lesson 3: Standard III: Duties to Clients
Difficulty: hard
According to Standard III(C)—Suitability, the recommended frequency for reviewing the investor's objectives and constraints should be at least:

- (selected) Annually.
- Quarterly.
- At the discretion of the manager and dependent upon business conditions.

Rationale

This Answer is Correct

Annual review is reasonable unless business or other reasons, such as a major change in market conditions, dictate more frequent review.

Question 69
L2R02TB-AC020-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Hoffman Neffer is a large brokerage firm that offers investment banking services. The firm has participated in the IPO and secondary offerings of Ryper Industries. Liz Clayton works in Hoffman's research department and is preparing a report on Ryper. Her spouse owns shares in Ryper in a retirement account. In the research report, Clayton must disclose:

	Banking Deals	*Her Beneficial Stock Ownership*
A.	Yes	Yes
B.	Yes	No
C.	No	Yes

- ROW A
- ROW B
- ROW C

Rationale
ROW A
Clayton has two conflicts of interest. First is the investment banking relationship between her firm and Ryper. Second is the beneficial ownership of stock, which is defined as shares owned by her, her spouse, a family member living with her, or a trust in which she has a beneficial interest. Both conflicts must be disclosed in the report.

Rationale
ROW B
Clayton has two conflicts of interest. First is the investment banking relationship between her firm and Ryper. Second is the beneficial ownership of stock, which is defined as shares owned by her, her spouse, a family member living with her, or a trust in which she has a beneficial interest. Both conflicts must be disclosed in the report.

Rationale
ROW C
Clayton has two conflicts of interest. First is the investment banking relationship between her firm and Ryper. Second is the beneficial ownership of stock, which is defined as shares owned by her, her spouse, a family member living with her, or a trust in which she has a beneficial interest. Both conflicts must be disclosed in the report.

Question 70
L2R02TB-AC016-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Peter Griffin is a supervisory analyst in the research department at a brokerage firm. He is responsible for reviewing subordinate analysts' reports prior to distribution to clients. Griffin maintains a weekly list of companies with pending reports along with each analyst's proposed recommendation, which he posts on a bulletin board outside his office. Unbeknownst to Griffin, employees from other departments became aware of this list and have been trading both personal and client accounts based on the information contained on the list. Did Griffin violate the Standards of Professional Conduct?

- (selected) Yes.
- No, because he is not responsible for employees he does not supervise.
- No, because he is unaware of the trading activities of the employees.

Rationale
✔ **Yes.**
The Standard requires managers to take reasonable efforts to prevent and detect violations of company policies, governing laws, and the Standards of Professional Conduct. Posting pending recommendations outside his office is an obviously unsecured way to manage sensitive information. Griffin should have anticipated that the information could be used by unauthorized persons.

Rationale
✖ **No, because he is not responsible for employees he does not supervise.**
The Standard requires managers to take reasonable efforts to prevent and detect violations of company policies, governing laws, and the Standards of Professional Conduct. Posting pending recommendations outside his office is an obviously unsecured way to manage sensitive information. Griffin should have anticipated that the information could be used by unauthorized persons.

Rationale
✖ **No, because he is unaware of the trading activities of the employees.**
The Standard requires managers to take reasonable efforts to prevent and detect violations of company policies, governing laws, and the Standards of Professional Conduct. Posting pending recommendations outside his office is an obviously unsecured way to manage sensitive information. Griffin should have anticipated that the information could be used by unauthorized persons.

Question 71
L2ET-TBB205-1412
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Which of the following practices is *least likely* to be in accordance with the recommended procedures for compliance with Standard I(B): Independence and Objectivity?

- ○ Firms should establish policies stating that every research report concerning the securities of a corporate client should reflect the unbiased opinion of the analyst.
- ● Members and candidates must not accept any gratuities and/or gifts of either a monetary or nonmonetary nature.
- ○ Firms should require prior approval for employee participation in IPOs.

Rationale

This Answer is Correct

The first and third options are explicit recommendations for compliance. Answer B is not in accordance with the recommended procedures for compliance with Standard I(B): Independence and Objectivity, since the standard does not preclude customary, ordinary business-related entertainment as long as its purpose is not to impact opinion or behavior.

Question 72
L2R02TB-AC001-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Jim Soltis, a CFA candidate, is an investment banker working on an initial stock offering for ChemCo. After filing a prospectus with the governing regulatory agency, ChemCo's CFO informs him that the income statement in the filed report slightly overstated the last two quarters' earnings. Soltis consults with his firm's legal department. The general counsel advises that the error is minor and the result of a relatively obscure accounting rule that will likely go unnoticed. Furthermore, even if detected, it will only require a restatement of the last two quarters. Therefore, the attorney instructs Soltis to let it go, which he does. Did Soltis violate the Standards of Professional Conduct?

- ○ No, because he is following legal advice of competent counsel.
- ○ No, because he was unaware of the error at the time he filed the report.
- ◉ Yes, because seeking legal counsel does not remove his duty to correct the error.

Rationale

❌ **No, because he is following legal advice of competent counsel.**

While the Standards do advise seeking the advice of legal counsel, doing so does not remove the responsibility for ensuring that all communications are true and accurate. Soltis should file a revised prospectus and inform any prospective investors of the corrected report.

Rationale

❌ **No, because he was unaware of the error at the time he filed the report.**

While the Standards do advise seeking the advice of legal counsel, doing so does not remove the responsibility for ensuring that all communications are true and accurate. Soltis should file a revised prospectus and inform any prospective investors of the corrected report.

Rationale

✅ **Yes, because seeking legal counsel does not remove his duty to correct the error.**

While the Standards do advise seeking the advice of legal counsel, doing so does not remove the responsibility for ensuring that all communications are true and accurate. Soltis should file a revised prospectus and inform any prospective investors of the corrected report.

Question 73
L2R02TB-AC026-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Rogelio Pocasangre is a broker and has been assigned to sell a bond issue for Americon Corp. The issue was underwritten by Tex Investments, which assumed all legal liability for the issue. After speaking with one of the investment bankers at Tex, Pocasangre is told that Americon utilizes special purpose entities to move much of its debt off its balance sheet. The prospectus makes no mention of its use of this off-sheet financing technique. Pocasangre meets with his supervisor to express his discomfort with promoting the debt issue without disclosing the practice, which he suspects may violate securities laws. The supervisor tries to ease his concerns by pointing out that any liability rests with Tex and not Pocasangre. According to the Standards of Professional Conduct, Pocasangre's *most* immediate course of action is to:

- ○ continue to sell the issue after confirming liability rests with Tex.
- ○ report the potential breach of law to the governing regulatory agency.
- ◉ refuse to participate and ask to be reassigned to another issue.

Rationale

✖ **continue to sell the issue after confirming liability rests with Tex.**

Pocasangre has an ethical duty not to misrepresent and to fully disclose relevant information to clients and prospects. If he feels that the firm's actions are contrary to the spirit of the Standards, his first course of action is to disassociate from the activity by requesting reassignment. The reaction of his supervisor might require further action on Pocasangre's part up to and including resigning from the firm.

Rationale

✖ **report the potential breach of law to the governing regulatory agency.**

Pocasangre has an ethical duty not to misrepresent and to fully disclose relevant information to clients and prospects. If he feels that the firm's actions are contrary to the spirit of the Standards, his first course of action is to disassociate from the activity by requesting reassignment. The reaction of his supervisor might require further action on Pocasangre's part up to and including resigning from the firm.

Rationale

✔ **refuse to participate and ask to be reassigned to another issue.**

Pocasangre has an ethical duty not to misrepresent and to fully disclose relevant information to clients and prospects. If he feels that the firm's actions are contrary to the spirit of the Standards, his first course of action is to disassociate from the activity by requesting reassignment. The reaction of his supervisor might require further action on Pocasangre's part up to and including resigning from the firm.

Question 74
L2R02TB-AC027-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Paula Nye, CFA, is an investment banker in the corporate finance division of a larger brokerage firm. As part of her sales presentation to Omega Consolidated seeking to underwrite their next securities issue, she provides assurance that her firm's research department will provide full coverage of the company. Has Nye violated the Standards of Professional Conduct by making such a pledge?

- ○ Yes, provided that the research reflects favorably on the company.
- ◉ No, provided that the research is unbiased and reflects the analyst's true opinion.
- ○ No, provided that the research presents only factual information.

Rationale
❌ **Yes, provided that the research reflects favorably on the company.**
Nye may assure a company that it will provide coverage for the new issue, but she cannot guarantee that the research will reflect positively on the company.

Rationale
✅ **No, provided that the research is unbiased and reflects the analyst's true opinion.**
Nye may assure a company that it will provide coverage for the new issue, but she cannot guarantee that the research will reflect positively on the company.

Rationale
❌ **No, provided that the research presents only factual information.**
Nye may assure a company that it will provide coverage for the new issue, but she cannot guarantee that the research will reflect positively on the company.

Question 75

L2R02TB-AC028-1512

LOS: LOS-5660

Lesson Reference: Lesson 1: Standard I: Professionalism

Difficulty: medium

Leo Tang, CFA, is an independent research analyst who has been hired by Delta DotCom to produce a report that the firm hopes will generate interest in its upcoming IPO. The firm offers Tang a flat fee to be paid when he begins the project, plus an opportunity to participate in the IPO, and a small allotment of stock options. According to the Standards of Professional Conduct, Tang should:

- (selected) accept the fee, but decline the stock options and participation in the IPO.
- accept the fee and the stock options, but decline participation in the IPO.
- accept the stock options, but decline the fee and participation in the IPO.

Rationale

✓ accept the fee, but decline the stock options and participation in the IPO.

Conducting research paid by the subject firm is not a violation of the Standards. However, steps must be taken to ensure the independence and objectivity of the report. The best practice is to accept flat-fee compensation without any conditions on the recommendations or analysis.

Rationale

✗ accept the fee and the stock options, but decline participation in the IPO.

Conducting research paid by the subject firm is not a violation of the Standards. However, steps must be taken to ensure the independence and objectivity of the report. The best practice is to accept flat-fee compensation without any conditions on the recommendations or analysis.

Rationale

✗ accept the stock options, but decline the fee and participation in the IPO.

Conducting research paid by the subject firm is not a violation of the Standards. However, steps must be taken to ensure the independence and objectivity of the report. The best practice is to accept flat-fee compensation without any conditions on the recommendations or analysis.

Question 76
L2R02TB-AC051-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Kevin Ruhl is a technology savvy broker who has embraced social media as a means of communicating with clients and prospects. What started out as updates on personnel changes, special events, and articles of interest has drifted toward solicitations for business and promotion of specific investments. The designated regulatory agency for brokerage firms issued a new rule effective before Ruhl shifted his usage patterns that strictly limit sales and marketing to investors via social media. The new rules were not well publicized in the major media and financial press. Ruhl's recent activities:

- ○ do not violate the Standards because the rule change has not been well publicized.
- ○ violate the Standards because he is expected to be an expert in compliance.
- ◉ violate the Standards because he is expected to inquire about those regulations prior to use.

Rationale
✗ **do not violate the Standards because the rule change has not been well publicized.**
If Ruhl is going to use new technology in his business, there is an expectation that he will seek out advice as to what the rules governing that technology might be and to stay abreast of changes to those rules as the technology evolves. When technology is new, the rules governing it can change rapidly. Standard I(A) implies that it is the member's responsibility to be particularly sensitive to staying informed about them.

Rationale
✗ **violate the Standards because he is expected to be an expert in compliance.**
If Ruhl is going to use new technology in his business, there is an expectation that he will seek out advice as to what the rules governing that technology might be and to stay abreast of changes to those rules as the technology evolves. When technology is new, the rules governing it can change rapidly. Standard I(A) implies that it is the member's responsibility to be particularly sensitive to staying informed about them.

Rationale
✓ **violate the Standards because he is expected to inquire about those regulations prior to use.**
If Ruhl is going to use new technology in his business, there is an expectation that he will seek out advice as to what the rules governing that technology might be and to stay abreast of changes to those rules as the technology evolves. When technology is new, the rules governing it can change rapidly. Standard I(A) implies that it is the member's responsibility to be particularly sensitive to staying informed about them.

Question 77
L2R02TB-AC015-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Pepper Tibbs is a portfolio manager with Albacor Asset Management. One of her wealthy clients, Walter Parks, offers to pay Tibbs a bonus if his portfolio outperforms the S&P 500 index return by more than five percent in any given year. According to the Standards of Professional Conduct, Tibbs may accept the offer if she obtains written consent from:

	Albacor	*All Her Clients*
A.	Yes	Yes
B.	Yes	No
C.	No	Yes

- ROW A
- ROW B
- ROW C

Rationale
ROW A
Receiving a bonus payment from a client can create a conflict of interest by encouraging preferential treatment. Members are not prohibited from accepting bonus incentives from clients but must first obtain written consent from their supervisors.

Rationale
ROW B
Receiving a bonus payment from a client can create a conflict of interest by encouraging preferential treatment. Members are not prohibited from accepting bonus incentives from clients but must first obtain written consent from their supervisors.

Rationale
ROW C
Receiving a bonus payment from a client can create a conflict of interest by encouraging preferential treatment. Members are not prohibited from accepting bonus incentives from clients but must first obtain written consent from their supervisors.

Question 78
L2R02TB-AC044-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium

Mary Kline is a technology analyst appearing on an investing television show. During an interview with the show's host, Kline makes the following statements.

> **Statement 1:** "Online advertising revenue will grow at 30 percent for the foreseeable future, which means the earnings multiples of this sector are way too low."
> **Statement 2:** "Traditional players, like Microsoft, are likely to continue to acquire Internet companies. If that plays out, the entire sector could get an additional boost in prices."

Taken in isolation, does either of these statements violate the Standards of Professional Conduct?

	Statement 1	*Statement 2*
A.	Yes	Yes
B.	Yes	No
C.	No	Yes

- ROW A
- ROW B (selected)
- ROW C

Rationale
ROW A (incorrect)
The Standard requires members to clearly distinguish fact from opinion. Statement 1 claims that advertising will grow and multiples are too low, which are opinions. However, they are stated as unqualified facts. Statement 2 proposes that traditional players are *likely* to continue acquisitions and this activity *might* cause prices to rise. The use of contingent statements implies that these are opinions.

Rationale
ROW B (correct)
The Standard requires members to clearly distinguish fact from opinion. Statement 1 claims that advertising will grow and multiples are too low, which are opinions. However, they are stated as unqualified facts. Statement 2 proposes that traditional players are *likely* to continue acquisitions and this activity *might* cause prices to rise. The use of contingent statements implies that these are opinions.

Rationale
ROW C (incorrect)
The Standard requires members to clearly distinguish fact from opinion. Statement 1 claims that advertising will grow and multiples are too low, which are opinions. However, they are stated as unqualified facts. Statement 2 proposes that traditional players are *likely* to continue acquisitions and this activity *might* cause prices to rise. The use of contingent statements implies that these are opinions.

Question 79
L2R02TB-AC042-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium

Lisa Thyme is vice president of research at Global Equity Insights. One of her staff analysts, Chad King, has been following Magic Tracks, a bicycle manufacturer involved in a major product liability lawsuit. King prepares a flash memo stating that a “confidential source” informed him that the plaintiff has irrefutable evidence that Magic's product was dangerously defective. With the trial scheduled to begin the next day, Thyme immediately approves the memo for distribution to clients without further inquiry. Did Thyme violate the Standards of Professional Conduct?

- ○ No.
- ○ Yes, by not waiting for the evidence to be presented at trial.
- ◉ Yes, by not evaluating the source of the information.

Rationale

✗ **No.**

Without confirming the source of the information, Thyme is effectively authorizing a rumor to be spread that might or might not prove to be accurate. She must identify the source in order to ascertain credibility of the information and to determine whether the information qualifies as material and nonpublic, in which case it may not be disseminated.

Rationale

✗ **Yes, by not waiting for the evidence to be presented at trial.**

Without confirming the source of the information, Thyme is effectively authorizing a rumor to be spread that might or might not prove to be accurate. She must identify the source in order to ascertain credibility of the information and to determine whether the information qualifies as material and nonpublic, in which case it may not be disseminated.

Rationale

✓ **Yes, by not evaluating the source of the information.**

Without confirming the source of the information, Thyme is effectively authorizing a rumor to be spread that might or might not prove to be accurate. She must identify the source in order to ascertain credibility of the information and to determine whether the information qualifies as material and nonpublic, in which case it may not be disseminated.

Question 80
L2ET-PQ0234-1502
LOS: LOS-5650
Lesson Reference: Lesson 7: Standard VII: Responsibilities as a CFA Institute Member or CFA Candidate
Difficulty: hard

Gary Loussier has recently registered for the CFA Level I examination and makes the following two statements in his resume:

Statement 1: “I am a level I candidate in the CFA Program”

Statement 2: “I expect to take no longer than 3 years to be awarded the charter”

How many of the statements above are in compliance with Standard VII(B): Reference to the CFA Institute, the CFA Designation, and the CFA Program?

- ○ Neither statement is in compliance with the Standards.
- ◉ Statement 1 is in compliance with the Standards, but statement 2 is not.
- ○ Statement 2 is in compliance with the Standards, but statement 1 is not.

Rationale
✗ **Neither statement is in compliance with the Standards.**
Incorrect. According to Standard VII(B), candidates can factually reference their participation in the CFA program; however, they are not permitted to state an expected completion or charter award date.

Rationale
✓ **Statement 1 is in compliance with the Standards, but statement 2 is not.**
Correct. According to Standard VII(B), candidates can factually reference their participation in the CFA program; however, they are not permitted to state an expected completion or charter award date.

Rationale
✗ **Statement 2 is in compliance with the Standards, but statement 1 is not.**
Incorrect. According to Standard VII(B), candidates can factually reference their participation in the CFA program; however, they are not permitted to state an expected completion or charter award date.

Question 81
L2ET-TB0011-1412
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
According to the recommended procedures for compliance with Standard III(D): Performance Presentation, members and candidates:

- ○ Must adhere to GIPS.
- ◉ Should encourage their firms to adhere to GIPS.
- ○ Should dissociate with performance presentations of non-GIPs employers.

Rationale

This Answer is Correct

Members and candidates are not required by the standards to use GIPS in their performance presentation; however, they should encourage their firms to become GIPS compliant.

Question 82
L2ET-PQ0224-1502
LOS: LOS-5650
Lesson Reference: Lesson 4: Standard IV: Duties to Employers
Difficulty: hard
Andres Williams manages the account of Caroline Cresher, a client. Williams is paid a salary by his employer, and Cresher pays the firm a standard fee based on the assets under management. Cresher proposes to Williams that “any year you beat the MSCI Global Equity Index, I will fly you to Malibu for a Christmas party in my personal villa.” Williams does not inform his employer of the arrangement, but never earns a return that allows him to take advantage of it.
Williams is:

- (●) In violation of Standard IV(B): Additional Compensation Arrangements.
- ( ) Not in violation of Standard IV(B) since he never took advantage of the offer from Cresher.
- ( ) Not in violation of Standard IV(B) since interests of Williams and Cresher remain aligned.

Rationale

✓ **In violation of Standard IV(B): Additional Compensation Arrangements.**
Correct. Williams should gain the permission of his employer before entering into any such arrangements of extra compensation from a client, since it may affect the attention that he pays to the client and cause a conflict of interest with other clients. Answer B is incorrect since the arrangement needs to be approved prior to it being entered into. Answer C is incorrect since Williams still needs to seek approval for extra compensation even if it originates from a client.

Rationale

✗ **Not in violation of Standard IV(B) since he never took advantage of the offer from Cresher.**
Incorrect. Williams should gain the permission of his employer before entering into any such arrangements of extra compensation from a client, since it may affect the attention that he pays to the client and cause a conflict of interest with other clients. Answer B is incorrect since the arrangement needs to be approved prior to it being entered into. Answer C is incorrect since Williams still needs to seek approval for extra compensation even if it originates from a client.

Rationale

✗ **Not in violation of Standard IV(B) since interests of Williams and Cresher remain aligned.**
Incorrect. Williams should gain the permission of his employer before entering into any such arrangements of extra compensation from a client, since it may affect the attention that he pays to the client and cause a conflict of interest with other clients. Answer B is incorrect since the arrangement needs to be approved prior to it being entered into. Answer C is incorrect since Williams still needs to seek approval for extra compensation even if it originates from a client.

Question 83
L2ET-TB0006-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Neil Grover has recently been cautioned by the police for possession of a prohibited substance. A colleague, Paul Jester, who has a strained relationship with Grover at work, has reported Grover to the CFA Institute and accused him of behavior that is in violation of Standard I(IV): Misconduct. Which of the following is *most likely* to be accurate?

- ○ Grover is in violation of the Standards.
- ◉ Jester is in violation of the Standards.
- ○ Both Grover and Jester are in violation of the Standards.

Rationale

This Answer is Correct

There is no evidence that Grover's indiscretion involves dishonesty, fraud, or deceit relating to his professional life. The Code and Standards are primarily aimed at conduct and actions related to a member's or candidate's professional life. Jester is more likely to be in violation of the standards for attempting to use the enforcement of the Code and Standards to settle a personal dispute, something that the CFA Institute has appropriate disciplinary policies for.

Question 84
L2ET-TBB203-1412
LOS: LOS-5650
Lesson Reference: Lesson 7: Standard VII: Responsibilities as a CFA Institute Member or CFA Candidate
Difficulty: medium

Rachel Adams is a performance attribution analyst who is enrolled in the CFA program. She passed the Level I exam in 2013 and the Level II in 2014. She makes the following two statements referencing her participation in the program during a job interview:

Statement 1: "I have successfully acquired the CFA Level II qualification."

Statement 2: "Completion of the CFA program and awarding of the designation is expected in 2015."

How many of the statements are in violation of Standard VII(B): Reference to the CFA Institute, the CFA Designation, and the CFA Program?

- ○ Neither.
- ○ One.
- ◉ Both.

Rationale
✖ **Neither.**
Incorrect. CFA candidates must never state or imply that they have a partial designation as a result of passing one or more levels, or cite an expected completion date of any level of the CFA program.

Rationale
✖ **One.**
Incorrect. CFA candidates must never state or imply that they have a partial designation as a result of passing one or more levels, or cite an expected completion date of any level of the CFA program.

Rationale
✔ **Both.**
Correct. CFA candidates must never state or imply that they have a partial designation as a result of passing one or more levels, or cite an expected completion date of any level of the CFA program.

Question 85
L2R02TB-AC010-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Patrick Hind manages individual retirement accounts for a number of clients. One of his clients, James Soltis, is a high-net-worth individual with over $1 million in his account. Another client, Stephanie Wagner, is of much more modest means with only $100,000 in her account. Both clients are very conservative and have over 10 years until retirement. An analysis of their risk tolerance at the beginning of the relationship with Hind showed that neither would feel comfortable with more than a five percent loss of principal in any given year. Hind invests Wagner in short- and intermediate-term high-grade corporate bonds and Treasuries. Since Soltis' high net worth enables him to assume more risk, Hind invests his account in more aggressive domestic growth stocks and emerging markets. Did Hind violate the Standards of Professional Conduct with respect to the suitability of the investments chosen for:

	Soltis' Account?	*Wagner's Account?*
A.	Yes	Yes
B.	Yes	No
C.	No	Yes

- ROW A
- ROW B
- ROW C

Rationale
ROW A
Risk tolerance is related to both the client's willingness and ability to take risk. Although Soltis has a greater ability to take risk, his willingness is similar to Wagner. Wagner's risk tolerance would imply that low-volatility assets such as investment grade corporates and Treasury securities would be appropriate.

Rationale
ROW B
Risk tolerance is related to both the client's willingness and ability to take risk. Although Soltis has a greater ability to take risk, his willingness is similar to Wagner. Wagner's risk tolerance would imply that low-volatility assets such as investment grade corporates and Treasury securities would be appropriate.

Rationale
ROW C
Risk tolerance is related to both the client's willingness and ability to take risk. Although Soltis has a greater ability to take risk, his willingness is similar to Wagner. Wagner's risk tolerance would imply that low-volatility assets such as investment grade corporates and Treasury securities would be appropriate.

Question 86
L2R02TB-AC053-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium

Raj Gupta works for a clearing firm, executing trades for online brokers. His direct supervisor is Rhonda Perkins. Each has made the following statements with respect to fiduciary duties and the Standards of Professional Conduct.

> Gupta: “The Standards create a fiduciary duty between me and our clients.”
> Perkins: “The Standards require that you act in the clients' best interests by seeking best execution and adhering to the trade parameters they set.”

Which of the statements are accurate?

	Gupta	*Perkins*
A.	No	Yes
B.	Yes	No
C.	Yes	Yes

- (selected) ROW A
- ROW B
- ROW C

Rationale
ROW A (correct)
The Standards do not impose a fiduciary duty on members to all their clients. They do require that members place their clients' interests ahead of their own within the scope of the services provided. For Gupta, Standard III(A) requires him only to perform his function to execute trades as instructed by clients without extending it to a broader fiduciary duty.

Rationale
ROW B (incorrect)
The Standards do not impose a fiduciary duty on members to all their clients. They do require that members place their clients' interests ahead of their own within the scope of the services provided. For Gupta, Standard III(A) requires him only to perform his function to execute trades as instructed by clients without extending it to a broader fiduciary duty.

Rationale
ROW C (incorrect)
The Standards do not impose a fiduciary duty on members to all their clients. They do require that members place their clients' interests ahead of their own within the scope of the services provided. For Gupta, Standard III(A) requires him only to perform his function to execute trades as instructed by clients without extending it to a broader fiduciary duty.

Question 87
L2R02TB-AC012-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Patrick Shallet is an advisor to university endowments in assessing capital expenditures. One of the universities he advises is considering a construction project to build a new biology lab. Part of Shallet's analysis includes detailed plans for the land development and construction costs. At a dinner party, a wealthy friend, Nancy Wang, mentions that she would like to make a donation to a university if she could receive naming rights on a campus structure. Shallet shows Wang the cost estimates for the new biology lab and suggests that she contact the university's board of directors regarding a donation. Did Shallet violate the Standard of Professional Conduct?

- (•) Yes.
- ( ) No, because he acted in his client's best interest.
- ( ) No, because endowments are nonprofit entities.

Rationale
Yes.
Shallet may not disclose financial details of the project to prospects without the consent of the university. Although his intentions are good, his actions violate the Standard.

Rationale
No, because he acted in his client's best interest.
Shallet may not disclose financial details of the project to prospects without the consent of the university. Although his intentions are good, his actions violate the Standard.

Rationale
No, because endowments are nonprofit entities.
Shallet may not disclose financial details of the project to prospects without the consent of the university. Although his intentions are good, his actions violate the Standard.

Question 88
L2ET-PQ0222-1502
LOS: LOS-5650
Lesson Reference: Lesson 4: Standard IV: Duties to Employers
Difficulty: hard
Tony Smith has been offered a role with a new employer which does not have an operational code of ethics. According to Standard IV(A): Loyalty, Smith should:

- Not accept the role until the new employer implements a code of ethics.
- Not accept the role until the new employer implements CFA Institute Code and Standards.
- Provide their employer with a copy of the Code and Standards should they decide to take the new position.

Rationale

Not accept the role until the new employer implements a code of ethics.

Incorrect. According to Standard IV(A): Loyalty, members and candidates are encouraged to provide their employer with a copy of the Code and Standards. These materials will inform the employer of the responsibilities of a CFA Institute member or a candidate in the CFA Program. Employers are not obligated to adhere to the Code and Standards, or indeed have a code of ethics in place; however, a member or candidate is still bound to comply with the Code and Standards.

Rationale

Not accept the role until the new employer implements CFA Institute Code and Standards.

Incorrect. According to Standard IV(A): Loyalty, members and candidates are encouraged to provide their employer with a copy of the Code and Standards. These materials will inform the employer of the responsibilities of a CFA Institute member or a candidate in the CFA Program. Employers are not obligated to adhere to the Code and Standards, or indeed have a code of ethics in place; however, a member or candidate is still bound to comply with the Code and Standards.

Rationale

Provide their employer with a copy of the Code and Standards should they decide to take the new position.

Correct. According to Standard IV(A): Loyalty, members and candidates are encouraged to provide their employer with a copy of the Code and Standards. These materials will inform the employer of the responsibilities of a CFA Institute member or a candidate in the CFA Program. Employers are not obligated to adhere to the Code and Standards, or indeed have a code of ethics in place; however, a member or candidate is still bound to comply with the Code and Standards.

Question 89

L2ET-PQ0233-1502

LOS: LOS-5650

Lesson Reference: Lesson 7: Standard VII: Responsibilities as a CFA Institute Member or CFA Candidate

Difficulty: hard

Roger Danal has recently registered for the CFA level III examination, and is aware that CFA Institute published the last three years of level III morning papers on the institute website. Danal conducts a review of recent morning papers and goes on to an internet forum to discuss specific questions, broad topic areas and formulas that are regularly tested. According to Standard VII(A): Responsibilities as a CFA Institute Member or CFA Candidate, which of the following statements is most accurate?

- ○ Danal has violated the Standards by discussing confidential exam information.
- ○ Danal has violated the Standards by discussing past exam questions.
- ◉ Danal has not violated the Standards.

Rationale

✖ **Danal has violated the Standards by discussing confidential exam information.**

Incorrect. According to Standard VII(A), all aspects of the exam, including questions, broad topical areas, and formulas, tested or not tested, are considered confidential until such time as CFA Institute elects to release them publicly. Since the past papers have been published by CFA Institute on their website, the information is no longer considered confidential and can be discussed.

Rationale

✖ **Danal has violated the Standards by discussing past exam questions.**

Incorrect. According to Standard VII(A), all aspects of the exam, including questions, broad topical areas, and formulas, tested or not tested, are considered confidential until such time as CFA Institute elects to release them publicly. Since the past papers have been published by CFA Institute on their website, the information is no longer considered confidential and can be discussed.

Rationale

✔ **Danal has not violated the Standards.**

Correct. According to Standard VII(A), all aspects of the exam, including questions, broad topical areas, and formulas, tested or not tested, are considered confidential until such time as CFA Institute elects to release them publicly. Since the past papers have been published by CFA Institute on their website, the information is no longer considered confidential and can be discussed.

Question 90
L2ET-TB0022-1412
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Standard VI(C): Referral Fees states that members and candidates should encourage their employers to:

- ○ Ban referral fee arrangements.
- ○ Adopt procedures to indicate the appropriate steps for requesting approval for referral arrangements.
- ● Adopt procedures to indicate the appropriate steps for requesting approval for referral arrangements and require that investment professionals provide the employer of updates on the amounts and nature of compensation received at least quarterly.

Rationale

This Answer is Correct

Under the recommended procedures for compliance for Standard VI(C): Referral Fees, members and candidates should encourage their employers to adopt procedures to indicate the appropriate steps for requesting approval for referral arrangements and require that investment professionals provide the employer with updates on the amounts and nature of compensation received at least quarterly.

Question 91
L2R02TB-AC048-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Ricardo Vaughn is a portfolio manager for Brilliant Asset Management (BAM). One of his accounts is owned by his parents. Vaughn's sister is named as a beneficiary on the account, but Vaughn is not. BAM has an opportunity to participate in an oversubscribed IPO that is appropriate for his parent's portfolio. According to the Standards of Professional Conduct, Vaughn's *best* course of action is to:

- ○ allocate shares to his parent's account only after other client accounts.
- ● allocate shares to his parent's account concurrently with other client accounts.
- ○ allocate no shares to his parent's account to make them available to other clients.

Rationale

✖ **allocate shares to his parent's account only after other client accounts.**

The Standard defines beneficial interest as accounts owned by the member, his or her spouse, children, and immediate family members residing with him or her. Family client accounts are any that are owned by family relatives that do not meet the preceding characteristics. Family client accounts should be neither advantaged nor disadvantaged because of the familial relationship. Therefore, Vaughn's parent's account should be allocated concurrently with the rest of his clients.

Rationale

✔ **allocate shares to his parent's account concurrently with other client accounts.**

The Standard defines beneficial interest as accounts owned by the member, his or her spouse, children, and immediate family members residing with him or her. Family client accounts are any that are owned by family relatives that do not meet the preceding characteristics. Family client accounts should be neither advantaged nor disadvantaged because of the familial relationship. Therefore, Vaughn's parent's account should be allocated concurrently with the rest of his clients.

Rationale

✖ **allocate no shares to his parent's account to make them available to other clients.**

The Standard defines beneficial interest as accounts owned by the member, his or her spouse, children, and immediate family members residing with him or her. Family client accounts are any that are owned by family relatives that do not meet the preceding characteristics. Family client accounts should be neither advantaged nor disadvantaged because of the familial relationship. Therefore, Vaughn's parent's account should be allocated concurrently with the rest of his clients.

Question 92
L2ET-PQ0231-1502
LOS: LOS-5660
Lesson Reference: Lesson 6: Standard VI: Conflicts of Interest
Difficulty: hard
According to the recommended procedure for compliance with Standard VI(B): Priority of Transactions, firms should:

- ○ Ban personal investing by investment personnel.
- ◉ Restrict investment in IPOs and private placements by investment personnel.
- ○ Ban client accounts where the client is a family member of an employee.

Rationale
✗ Ban personal investing by investment personnel.
Incorrect. Firms should restrict investment in IPOs and private placements by investment personnel in order to reduce the possibility of employees personally benefiting from such deals instead of clients. Answer A is incorrect because the Standard acknowledges that banning personal investing is *likely* to be too restrictive, while answer C is incorrect because families are permitted to be clients of the firm as long as they are treated the same as other similar clients of the firm.

Rationale
✓ Restrict investment in IPOs and private placements by investment personnel.
Correct. Firms should restrict investment in IPOs and private placements by investment personnel in order to reduce the possibility of employees personally benefiting from such deals instead of clients. Answer A is incorrect because the Standard acknowledges that banning personal investing is *likely* to be too restrictive, while answer C is incorrect because families are permitted to be clients of the firm as long as they are treated the same as other similar clients of the firm.

Rationale
✗ Ban client accounts where the client is a family member of an employee.
Incorrect. Firms should restrict investment in IPOs and private placements by investment personnel in order to reduce the possibility of employees personally benefiting from such deals instead of clients. Answer A is incorrect because the Standard acknowledges that banning personal investing is *likely* to be too restrictive, while answer C is incorrect because families are permitted to be clients of the firm as long as they are treated the same as other similar clients of the firm.

Question 93

L2ET-PQ0204-1502

LOS: LOS-5650

Lesson Reference: Lesson 1: Standard I: Professionalism

Difficulty: hard

Didier Sands is head of a research unit at a major investment bank. He is aware that his analysts frequently enquire as to what level of travel expenses they should be able to accept from corporate issuers that they cover. According to Standard I(B)—Independence and Objectivity, Sands should tell his analysts that best practice is to:

- ○ Never accept any travel expenses from companies that they cover.
- ◉ Only accept modestly arranged travel when commercial transportation is unavailable.
- ○ Accept modest travel expenses but must not accept hotel expenses.

Rationale

✖ **Never accept any travel expenses from companies that they cover.**

Incorrect. Standard I(B) states that to avoid the appearance of compromising their independence and objectivity, best practice dictates that members and candidates always use commercial transportation at their expense or at the expense of their firm rather than accept paid travel arrangements from an outside company. Should commercial transportation be unavailable, members and candidates may accept modestly arranged travel.

Rationale

✔ **Only accept modestly arranged travel when commercial transportation is unavailable.**

Correct. Standard I(B) states that to avoid the appearance of compromising their independence and objectivity, best practice dictates that members and candidates always use commercial transportation at their expense or at the expense of their firm rather than accept paid travel arrangements from an outside company. Should commercial transportation be unavailable, members and candidates may accept modestly arranged travel.

Rationale

✖ **Accept modest travel expenses but must not accept hotel expenses.**

Incorrect. Standard I(B) states that to avoid the appearance of compromising their independence and objectivity, best practice dictates that members and candidates always use commercial transportation at their expense or at the expense of their firm rather than accept paid travel arrangements from an outside company. Should commercial transportation be unavailable, members and candidates may accept modestly arranged travel.

Question 94
L2ET-TBX102-1502
LOS: LOS-5650
Lesson Reference: Lesson 5: Standard V: Investment Analysis, Recommendations, and Actions
Difficulty: easy
Nigel Oldman is a research analyst who covers domestic companies in the superstore retail sector. His most recent report draws on a variety of sources including face-to-face interviews with company management, comments made by management on Internet-based social media, and customer surveys carried out over the Internet by third-party market research agencies. In order to comply with Standard V(C): Record Retention, Oldman must document information gained from:

- ○ The interview with company management only.
- ○ The interview with company management and the third-party research only.
- ◉ The interview with company management, the comments made on social media, and the third-party research.

Rationale
This Answer is Correct
Oldman must document all the information that goes into his reports. This includes any information gained over social media and third-party research.

Question 95
L2ET-TBX109-1502
LOS: LOS-5650
Lesson Reference: Lesson 7: Standard VII: Responsibilities as a CFA Institute Member or CFA Candidate
Difficulty: easy
Which of the following statements clearly conflicts with the recommended procedures for compliance presented in the CFA Institute Standards of Practice Handbook?

- (selected) Employees should be prohibited from partaking in equity IPOs.
- Members and candidates must archive research notes and other documents either electronically or in hard copy that support their investment-related communications.
- Members' and candidates' firms are encouraged to include information on compensation packages in firms' promotional literature.

Rationale

This Answer is Correct

Standard VI(B): Priority of Transactions recommends only that reliable and systematic review procedures are established to ensure that conflicts relating to IPOs are identified and appropriately dealt with—it does not require a ban on participation in IPOs. The second option is a recommendation of Standard V(C): Record Retention, and the third option is a recommendation of Standard VI(A): Disclosure of Conflicts.

Question 96
L2ET-TB0020-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Analyst recommendations made via Twitter are:

- ○ Not allowed under the requirements of Standard V(C): Record Retention.
- ○ Not covered under the requirements of Standard V(C): Record Retention.
- ◉ Covered under the requirements of Standard V(C): Record Retention.

Rationale

This Answer is Correct

Members and candidates should understand that although employers and local regulators are developing digital media retention policies, these policies may lag behind the advent of new communication channels like Twitter. Such lag places greater responsibility on the individual for ensuring that all relevant information is retained under Standard V(C): Record Retention.

Question 97
L2R02TB-AC008-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium

Susan Jackson manages the pension fund for Elgin Manufacturing. Elgin's management is concerned about the rising pension expense of the underfunded plan. The company's CFO suggests that Jackson add riskier assets to the portfolio in the hopes of increasing the return and reducing the firm's pension expense. Based solely on this request, should Jackson increase the risk profile of the plan assets?

- ○ Yes.
- ○ No, because short-term volatility is bad for pension plans.
- ● No, because her fiduciary duty is owed to the plan beneficiaries.

Rationale

✗ **Yes.**

Members must know their fiduciary duties and to whom they are owed. As plan manager, Jackson owes a fiduciary duty to the plan beneficiaries (employees) and not the plan sponsor (Elgin). Increasing the plan's risk profile might benefit Elgin in the short-term through lower pension expense, but it might also risk the plan's long-term soundness to the detriment of the beneficiaries by exacerbating the underfunded status.

Rationale

✗ **No, because short-term volatility is bad for pension plans.**

Members must know their fiduciary duties and to whom they are owed. As plan manager, Jackson owes a fiduciary duty to the plan beneficiaries (employees) and not the plan sponsor (Elgin). Increasing the plan's risk profile might benefit Elgin in the short-term through lower pension expense, but it might also risk the plan's long-term soundness to the detriment of the beneficiaries by exacerbating the underfunded status.

Rationale

✓ **No, because her fiduciary duty is owed to the plan beneficiaries.**

Members must know their fiduciary duties and to whom they are owed. As plan manager, Jackson owes a fiduciary duty to the plan beneficiaries (employees) and not the plan sponsor (Elgin). Increasing the plan's risk profile might benefit Elgin in the short-term through lower pension expense, but it might also risk the plan's long-term soundness to the detriment of the beneficiaries by exacerbating the underfunded status.

Question 98
L2ET-TBB206-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium

An analyst uses the following sources of information:

> Source 1: A verbal quote that the analyst attributes to a "leading analyst."
> Source 2: A well-known research report from a reputable research company without verifying the information.
> Source 3: Statistics from a recognized financial reporting service without attribution.

By using these sources in the manner described above, the analyst likely violated Standard I(C): Misrepresentation:

- ○ Once.
- ◉ Twice.
- ○ Three times.

Rationale

This Answer is Correct

Using Sources 1 and 2 are in direct breach of the requirements of Standard I(C): Misrepresentation. Using information from recognized financial and statistical reporting services without attribution is not in violation of the standard.

Question 99
L2R02TB-AC007-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Peter Olson operates a stock market recommendation website called Independent-Researchers.com. Olson has contracts with several companies that trade on the pink sheets to provide research coverage for their stocks. He is compensated with a flat fee and stock options on the covered companies. Olson bases all his recommendations on projections provided by the companies' managements, none of which is verified. He lists no "sell" recommendations on his site. Most of his recommendations show a significant, if short-lived, increase in price following initiation of coverage. Has Olson violated the Standards of Professional Conduct with respect to market manipulation?

- ○ No.
- ○ Yes, by making recommendations over the Internet.
- ◉ Yes, by promoting stocks based on questionable information.

Rationale
❌ **No.**
The Standard prohibits manipulating security prices. Using questionable research to temporarily pump up the price of stocks would qualify as a market manipulation.

Rationale
❌ **Yes, by making recommendations over the Internet.**
The Standard prohibits manipulating security prices. Using questionable research to temporarily pump up the price of stocks would qualify as a market manipulation.

Rationale
✅ **Yes, by promoting stocks based on questionable information.**
The Standard prohibits manipulating security prices. Using questionable research to temporarily pump up the price of stocks would qualify as a market manipulation.

Question 100
L2ET-PQ0203-1502
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: hard
Julian Segovia is a portfolio manager who has been approached by an industry consultant on behalf of a large endowment that is looking to hire a new portfolio manager. Segovia is very keen to be recommended to the short list of candidates from the opportunity, and arranges to meet with the industry consultant. For several weeks, Segovia entertains the consultant, often taking them to the best restaurants in town and paying for them to play at the best golf courses in the country. The consultant even stays for free in Segovia's ski chalet in the French Alps. Segovia is delighted when he hears his firm has indeed made the short list for managing the endowment. Which of the following statements is *most accurate* regarding Segovia's behavior according to CFA Institute Standards?

- (selected) Segovia has violated Standard I(B): Independence and Objectivity.
- Segovia has not violated Standard I(B) since the entertainment can be viewed as a cost incurred in establishing a business relationship.
- Segovia has not violated Standard I(B) since the Standard only applies to analysts issuing recommendations.

Rationale

✔ **Segovia has violated Standard I(B): Independence and Objectivity.**

Correct. Segovia lavished gifts and expensive entertainment that could reasonably be expected to influence the consultant to recommend the hiring of his firm. Therefore, Segovia was in violation of Standard I(B). Answer B is incorrect since the gifts and entertainment are not modest expenses incurred in the course of doing business. Answer C is incorrect since the Standard applies to all members and candidates.

Rationale

✘ **Segovia has not violated Standard I(B) since the entertainment can be viewed as a cost incurred in establishing a business relationship.**

Incorrect. Segovia lavished gifts and expensive entertainment that could reasonably be expected to influence the consultant to recommend the hiring of his firm. Therefore, Segovia was in violation of Standard I(B). Answer B is incorrect since the gifts and entertainment are not modest expenses incurred in the course of doing business. Answer C is incorrect since the Standard applies to all members and candidates.

Rationale

✘ **Segovia has not violated Standard I(B) since the Standard only applies to analysts issuing recommendations.**

Incorrect. Segovia lavished gifts and expensive entertainment that could reasonably be expected to influence the consultant to recommend the hiring of his firm. Therefore, Segovia was in violation of Standard I(B). Answer B is incorrect since the gifts and entertainment are not modest expenses incurred in the course of doing business. Answer C is incorrect since the Standard applies to all members and candidates.

Question 101
L2ET-TB0016-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Standard V(A): Diligence and Reasonable Basis states that members and candidates:

- ○ Cannot rely on either secondary or third-party research.
- ○ Can rely on second-party research only provided they make reasonable and diligent efforts to determine whether such research is sound.
- ◉ Can rely on second-party or third-party research provided they make reasonable and diligent efforts to determine whether such research is sound.

Rationale

This Answer is Correct

Under Standard V(A), members and candidates may rely on second-party research, which is research conducted by other members of their firm, and third-party research, which is research conducted by those outside their firm. In both cases, the member or candidate should make reasonable and diligent efforts to determine whether such research is sound.

Question 102

L2ET-TBX108-1502

LOS: LOS-5650

Lesson Reference: Lesson 7: Standard VII: Responsibilities as a CFA Institute Member or CFA Candidate

Difficulty: easy

The mosaic theory is a defense against the violation of which of the CFA Standards of Professional Conduct?

- (selected) Standard II(A): Material Nonpublic Information.
- Standard V(A): Diligence and Reasonable Basis.
- Standard VI(A): Disclosure of Conflicts.

Rationale

This Answer is Correct

The mosaic theory states that an analyst may use material public information and nonmaterial nonpublic information in creating a larger picture that becomes material nonpublic information.

Question 103
L2R02TB-AC035-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Phillip Wilson is a portfolio manager with Safe Investments. Wilson places a portion of his fund's trades with Better Brokers. Better's commissions are higher than the average broker, but Wilson receives macroeconomic and industry reports each quarter from their research department that he uses in managing his portfolios. One of his clients requested that Wilson place his account's trades with Delta Brokers so that he can get their market commentary newsletter. Delta is not one of Safe Investments' recommended brokers. Did Wilson violate the Standards of Professional Conduct by placing trades with Better or Delta?

	Better	*Delta*
A.	Yes	Yes
B.	Yes	No
C.	No	No

- ROW A
- ROW B
- ROW C

Rationale
ROW A
If the research that Wilson gets from Better helps him to make investment decisions on behalf of his clients, then he is justified in paying the higher commissions. These types of “soft dollar” arrangements are permissible under the Standards as long as they benefit the clients. The Standards also permit client-directed brokerage as a means to obtain research, as well.

Rationale
ROW B
If the research that Wilson gets from Better helps him to make investment decisions on behalf of his clients, then he is justified in paying the higher commissions. These types of “soft dollar” arrangements are permissible under the Standards as long as they benefit the clients. The Standards also permit client-directed brokerage as a means to obtain research, as well.

Rationale
ROW C
If the research that Wilson gets from Better helps him to make investment decisions on behalf of his clients, then he is justified in paying the higher commissions. These types of “soft dollar” arrangements are permissible under the Standards as long as they benefit the clients. The Standards also permit client-directed brokerage as a means to obtain research, as well.

Question 104
L2ET-TBB212-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Jamie Sturgeon, CFA, is a portfolio manager who manages a high-risk fund with a mandate to aggressively lever positions in order to magnify exposure to stock market returns. Bill Kelly is a retail investor who is planning to retire within the next couple of years and has a large exposure to the fund run by Sturgeon in his personal pension fund. With regards to Standard III(C): Suitability, Sturgeon is *most likely:*

- ○ In violation of the Standards since Sturgeon has failed to assess the suitability of the fund as an investment for Kelly.
- ○ In violation of the Standards if stock markets fall and Kelly sustains losses in his pension portfolio that jeopardize the ability of his pension fund to meet its objectives.
- ◉ Not in violation of the Standards.

Rationale

This Answer is Correct

Sturgeon's responsibility is to invest in a manner consistent with the stated mandate of the fund. Members and candidates who manage pooled assets to a specific mandate are not responsible for determining the suitability of the fund as an investment for investors who may be purchasing shares in the fund. The responsibility for determining the suitability of an investment for clients can be conferred only on members and candidates who have an advisory relationship with clients.

Question 105
L2ET-TBX103-1502
LOS: LOS-5660
Lesson Reference: Lesson 6: Standard VI: Conflicts of Interest
Difficulty: easy
Which of the following procedures is most closely aligned with the requirements of Standard VI(A): Conflicts of Interest?

- ○ Sell side members and candidates should be prohibited from owning any equity securities.
- ○ Sell side members and candidates should be prohibited from owning equity securities that the member or candidate is recommending.
- ◉ Buy side members and candidates should disclose their procedures for reporting requirements for personal transactions.

Rationale

This Answer is Correct

The first and second options are incorrect because Standard VI(A) states that prohibiting members and candidates from owning the securities that they recommend to clients is too burdensome and discriminates against members and candidates.

Question 106
L2R02TB-AC017-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Pam Jenell is a research analyst specializing in the highly fragmented business services industry. She promised her supervisor that a comprehensive report would be completed in two weeks. Her firm uses a complex statistical model to forecast sales. Because her department is understaffed and the forecast model is labor-intensive, she models the three largest firms and forecasts the remaining firms' sales based on their market caps relative to the largest firms. Later, she models all of the firms and sends out revised recommendations. Did Jenell violate the Standards of Professional Conduct in preparing her report?

- No.
- B. Yes, she should have used the subject firms' management estimates.
- C. Yes, she should have only included those firms that she could model.

Rationale
No.
The release of incomplete analysis would constitute a violation of the Standard, particularly if the report did not explain the preliminary nature of the results.

Rationale
B. Yes, she should have used the subject firms' management estimates.
The release of incomplete analysis would constitute a violation of the Standard, particularly if the report did not explain the preliminary nature of the results.

Rationale
C. Yes, she should have only included those firms that she could model.
The release of incomplete analysis would constitute a violation of the Standard, particularly if the report did not explain the preliminary nature of the results.

Question 107
L2R02TB-ITEMSET-AC059-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium

Use the following information to answer the next 3 questions:

Wendy Chan, CFA, is the senior analyst with Schrader Hong Kong, an investment management firm. She supervises three other analysts in her department. One of the three is a CFA charterholder, and another is a candidate. The third is a junior analyst who has not yet entered the CFA program.

The firm's compliance manual calls for quarterly reviews of employee trading to ensure that frontrunning is not occurring. Chan's group is small and checking trades is tedious, so she delegated the task to Wayne Butler, her chartered subordinate. Several months later, it was discovered that the junior analyst on Chan's team was engaging in front-running trades. When she confronted Butler about the trading records, he admitted that he had not been checking them as she had asked.

After the front-running incident, Chan decided to implement more stringent compliance procedures. She met with her team and announced that they would implement three new policies.

1. All reports must be critiqued and approved by her prior to release.
2. A standards manual outlining reasonableness and adequacy of research will be drafted.
3. All third-party research providers must be thoroughly vetted and approved by her.

i.
Of the three analysts under Chan's supervision, how many must she subject to the CFA Code of Ethics and Standards of Professional Conduct?

- One.
- Two.
- Three.

Rationale
This Answer is Correct
Standard IV(C) Responsibilities of Supervisors states that members must make reasonable efforts to detect and prevent violations of applicable laws, rules, regulations and the Code and Standards. Because Chan is a covered person, she must enforce the Code and Standards on all her subordinates regardless of whether or not they are covered persons.

Rationale
This Answer is Correct
Standard IV(C) Responsibilities of Supervisors states that members must make reasonable efforts to detect and prevent violations of applicable laws, rules, regulations and the Code and Standards. Because Chan is a covered person, she must enforce the Code and Standards on all her subordinates regardless of whether or not they are covered persons.

Rationale
This Answer is Correct
Standard IV(C) Responsibilities of Supervisors states that members must make reasonable efforts to detect and prevent violations of applicable laws, rules, regulations and the Code and Standards. Because Chan is a covered person, she must enforce the Code and Standards on all her subordinates regardless of whether or not they are covered persons.

ii.

Did Chan violate the Standards of Professional Conduct with respect to the incident involving frontrunning?

- (selected) Yes.
- No, because she delegated the task to another charterholder.
- No, because she was unaware that Butler was not checking trades.

Rationale

This Answer is Incorrect

While delegation of supervisory responsibilities is permissible under Standard IV(C), it does not completely relieve Chan of her duty to ensure that the person to whom she delegated is performing the task. This responsibility includes reviews and training.

Rationale

This Answer is Incorrect

While delegation of supervisory responsibilities is permissible under Standard IV(C), it does not completely relieve Chan of her duty to ensure that the person to whom she delegated is performing the task. This responsibility includes reviews and training.

Rationale

This Answer is Incorrect

While delegation of supervisory responsibilities is permissible under Standard IV(C), it does not completely relieve Chan of her duty to ensure that the person to whom she delegated is performing the task. This responsibility includes reviews and training.

iii.

Of the three new policies Chan plans to implement with her team, which is required compliance under Standard V(A): Diligence and Reasonable Basis?

- One.
- Two.
- (selected) Three.

Rationale

This Answer is Incorrect

Standard IV(A): Diligence and Reasonable Basis allows the use of third-party research as long as the member has no reason to doubt its validity or objectivity. The other two policies are recommended procedures.

Rationale

This Answer is Incorrect

Standard IV(A): Diligence and Reasonable Basis allows the use of third-party research as long as the member has no reason to doubt its validity or objectivity. The other two policies are recommended procedures.

Rationale

This Answer is Incorrect

Standard IV(A): Diligence and Reasonable Basis allows the use of third-party research as long as the member has no reason to doubt its validity or objectivity. The other two policies are recommended procedures.

Question 108
L2R02TB-AC032-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Wendel Ross is an automotive analyst for a large brokerage firm. While having dinner at a fancy restaurant, he recognized the chairman, CEO, and CFO of a major auto manufacturer seated at the next table. The executives appeared to be celebrating, and Ross overheard the CFO quip that their new model's sales far exceeded expectations. The CEO, Mark Riggins, remarked that the consensus earnings estimate is far too low and that he expects this quarter to be the biggest surprise in the company's history. The next morning, Ross made a substantial trade to acquire the automaker's shares. Did Ross violate the Standards of Professional Conduct?

- (selected) Yes.
- No, because he owed no fiduciary duty to the automaker.
- No, because he did not solicit the information.

Rationale
✔ **Yes.**
The Standard prohibits trading on material, nonpublic information regardless of how it was obtained.

Rationale
✖ **No, because he owed no fiduciary duty to the automaker.**
The Standard prohibits trading on material, nonpublic information regardless of how it was obtained.

Rationale
✖ **No, because he did not solicit the information.**
The Standard prohibits trading on material, nonpublic information regardless of how it was obtained.

Question 109

L2ET-PQ0214-1502

LOS: LOS-5650

Lesson Reference: Lesson 3: Standard III: Duties to Clients

Difficulty: hard

Emily Liu is a portfolio manager for the private accounts of several high-net-worth individuals. Liu has entered into a soft dollar agreement with a broker in order to purchase research that is used to benefit all client accounts. A large account has indicated they do not wish to be involved in a soft dollar arrangement, and in order to make up for the lack of participation in the fund, Liu has to intentionally trade more frequently in the accounts of other clients in order to keep using the research across all accounts. According to Standard III(B) Fair Dealing. Liu is:

- (selected) In violation of the Standard since her trading actions are disadvantaging some clients in favor of the large account that has opted out of soft dollar agreements .
- In violation of the Standard because soft dollar agreements are not allowed under the standard.
- In compliance with the Standard.

Rationale

This Answer is Correct

Liu is violating Standard III(B) because her trading actions are disadvantaging her clients to enhance a relationship with a preferred client. All clients are benefiting from the research being provided and should incur their fair portion of the costs. This does not mean that additional trading should occur if a client has not paid an equal portion of the commission; trading should occur only as required by the strategy. The second option is incorrect since the Standard does not prevent soft dollar agreements.

Question 110
L2ET-TBX104-1502
LOS: LOS-5650
Lesson Reference: Lesson 6: Standard VI: Conflicts of Interest
Difficulty: easy
Robert Bee is an investment advisor with PostionOne Investments and has discretion over several high-net-worth individual accounts. Bee's family entrusts him with the management of their financial affairs: his parents have established a retirement account with PositionOne, while Bee's brother has personally asked Bee to manage a small amount of money on his behalf. Bee has just received an allocation in a hot issue of an Asian Internet company, and in order to avoid the perception of favoring family members, Bee excludes the accounts of his parents and his brother when allocating the issue. According to Standard VI(B): Priority of Transactions, Bee has:

- ○ Not violated the Standard.
- ◉ Violated the Standard by not allocating to his parents' account.
- ○ Violated the Standard by not allocating to his brother's account.

Rationale

This Answer is Correct

Standard VI(B) states that client portfolios should be given priority over accounts of members and candidates and their close family. However, should a family member be a fee-paying client of the member or candidates, then they should treat the family member like other similar client accounts. Since Bee's parents' account is a client account, he has violated the Standard by ignoring this account when allocating the issue.

Question 111
L2ET-PQ0212-1502
LOS: LOS-5650
Lesson Reference: Lesson 3: Standard III: Duties to Clients
Difficulty: hard

Ibrahim Sultar is the Chief Investment Officer for a large sovereign wealth fund, ISI Investments. ISI has exposure to a broad array of different investment products from traditional mutual funds to alternative investments such as hedge funds and private equity funds, alongside several privately managed accounts. At a recent conference, Sultar meets Lynette Simons, CEO of Interborder Capital. Sultar is keen to talk to Simons because ISI has investments in private managed accounts and hedge funds managed by Interborder, and therefore wishes to discuss their client relationship. According to Standard III(A): Loyalty, Prudence, and Care, which of the following statements is *most likely* to be accurate?

- (selected) ISI should be considered a client of Interborder for the private managed accounts only.
- ISI should be considered a client of Interborder for the hedge fund investment only.
- ISI should be considered a client of Interborder for both the private managed accounts and the hedge fund investment.

Rationale

✔ **ISI should be considered a client of Interborder for the private managed accounts only.**

Correct. The first step for members and candidates in fulfilling their duty of loyalty to clients is to determine the identity of the "client" to whom the duty of loyalty is owed. ISI is clearly the client for the private managed accounts that are run for ISI by Interborder Capital; however, members and candidates managing a fund to an expected mandate owe the duty of loyalty, prudence, and care to invest in a manner consistent with the stated mandate, not to an individual investor in the fund.

Rationale

✘ **ISI should be considered a client of Interborder for the hedge fund investment only.**

Incorrect. The first step for members and candidates in fulfilling their duty of loyalty to clients is to determine the identity of the "client" to whom the duty of loyalty is owed. ISI is clearly the client for the private managed accounts that are run for ISI by Interborder Capital; however, members and candidates managing a fund to an expected mandate owe the duty of loyalty, prudence, and care to invest in a manner consistent with the stated mandate, not to an individual investor in the fund.

Rationale

✘ **ISI should be considered a client of Interborder for both the private managed accounts and the hedge fund investment.**

Incorrect. The first step for members and candidates in fulfilling their duty of loyalty to clients is to determine the identity of the "client" to whom the duty of loyalty is owed. ISI is clearly the client for the private managed accounts that are run for ISI by Interborder Capital; however, members and candidates managing a fund to an expected mandate owe the duty of loyalty, prudence, and care to invest in a manner consistent with the stated mandate, not to an individual investor in the fund.

Question 112

L2R02TB-AC054-1512

LOS: LOS-5650

Lesson Reference: Lesson 1: Standard I: Professionalism

Difficulty: medium

Martha Graham was an investment banker and CFA charterholder for 10 years before she was asked to join a political campaign. After her team won the election, she joined the administration of the new official. During that period, she allowed her membership in CFA Institute to lapse. Two years later, she returned to banking. According to the Standards of Professional Conduct, Graham may resume using the CFA designation:

- immediately upon her return by sending a dues payment to CFA Institute.
- only after paying dues and filing her Professional Conduct Statement.
- only after paying dues and passing CFA Institute's reinstatement exam.

Rationale

immediately upon her return by sending a dues payment to CFA Institute.

Standard VII(B) stipulates that when a member allows their membership to lapse, they may not use the CFA designation until they have resumed paying dues, filed their Professional Conduct Statement, and completed the CFA Institute reinstatement procedures.

Rationale

only after paying dues and filing her Professional Conduct Statement.

Standard VII(B) stipulates that when a member allows their membership to lapse, they may not use the CFA designation until they have resumed paying dues, filed their Professional Conduct Statement, and completed the CFA Institute reinstatement procedures.

Rationale

only after paying dues and passing CFA Institute's reinstatement exam.

Standard VII(B) stipulates that when a member allows their membership to lapse, they may not use the CFA designation until they have resumed paying dues, filed their Professional Conduct Statement, and completed the CFA Institute reinstatement procedures.

Question 113
L2ET-PQ0221-1502
LOS: LOS-5650
Lesson Reference: Lesson 3: Standard III: Duties to Clients
Difficulty: hard
Bryony Watson is a portfolio manager registered in a country where the local laws and regulation state that client confidentiality must be maintained at all times. She is also subject to an investigation by the CFA Institute Professional Conduct Program (PCP) regarding her trade allocation procedures. The PCP request information about a client as part of their investigation. In order to comply with Standard III(E)—Preservation of Confidentiality, Watson should:

- (selected) Refuse to disclose client information to the PCP.
- Disclose client information to the PCP.
- Gain her client's permission to disclose information to the PCP.

Rationale

✔ **Refuse to disclose client information to the PCP.**

Correct. The requirements of Standard III(E) are not intended to prevent members and candidates from cooperating with an investigation by the CFA Institute Professional Conduct Program (PCP). When permissible under applicable law, members and candidates shall consider the PCP an extension of themselves when requested to provide information about a client in support of a PCP investigation into their own conduct. In this case, the law states that client confidentiality must be maintained at all times and Watson must follow these local laws and regulations.

Rationale

✖ **Disclose client information to the PCP.**

Incorrect. The requirements of Standard III(E) are not intended to prevent members and candidates from cooperating with an investigation by the CFA Institute Professional Conduct Program (PCP). When permissible under applicable law, members and candidates shall consider the PCP an extension of themselves when requested to provide information about a client in support of a PCP investigation into their own conduct. In this case, the law states that client confidentiality must be maintained at all times and Watson must follow these local laws and regulations.

Rationale

✖ **Gain her client's permission to disclose information to the PCP.**

Incorrect. The requirements of Standard III(E) are not intended to prevent members and candidates from cooperating with an investigation by the CFA Institute Professional Conduct Program (PCP). When permissible under applicable law, members and candidates shall consider the PCP an extension of themselves when requested to provide information about a client in support of a PCP investigation into their own conduct. In this case, the law states that client confidentiality must be maintained at all times and Watson must follow these local laws and regulations.

Question 114
L2ET-TB0009-1412
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Which of the following recommendations most closely aligns with the recommended procedures for compliance under Standard III(B): Fair Dealing?

- ○ Communicate recommendation changes within the firm and to customers separately.
- ○ Involve more people in the recommendation dissemination process.
- ◉ Shorten the time frame between decision and dissemination.

Rationale

This Answer is Correct

The recommended procedures for compliance with Standard III(B): Fair Dealing are to communicate recommendation changes within the firm and to customers simultaneously, limit the number of people involved in the recommendation dissemination process, and shorten the time frame between decision and dissemination.

Question 115
L2ET-PQ0232-1502
LOS: LOS-5650
Lesson Reference: Lesson 6: Standard VI: Conflicts of Interest
Difficulty: hard
Colin Drinkwater works for the pensions department of Edward Duke Financial Advisers. He receives compensation for each referral he makes to Edward Duke's life assurance department that results in a sale. Drinkwater's employer is aware of the referral arrangement, but clients are not informed. With respect to the requirements of Standard VI(C): Referral Fees, which of the following is most accurate?

- Drinkwater is in compliance with the Standards since interdepartmental referral fees are not covered by the Standard.
- Drinkwater is in violation of the Standards since he should disclose the referral arrangement to his clients.
- Drinkwater is in violation of the Standards since interdepartmental referral fees are prohibited under the Standard.

Rationale

Drinkwater is in compliance with the Standards since interdepartmental referral fees are not covered by the Standard.

Incorrect. Drinkwater has violated Standard VI(C) by not disclosing the referral arrangement at Edward Duke to his clients. Standard VI(C) does not distinguish between referral payments paid by a third party for referring clients to the third party and internal payments paid within the firm to attract new business to a subsidiary. Members and candidates must disclose all such referral fees.

Rationale

Drinkwater is in violation of the Standards since he should disclose the referral arrangement to his clients.

Correct. Drinkwater has violated Standard VI(C) by not disclosing the referral arrangement at Edward Duke to his clients. Standard VI(C) does not distinguish between referral payments paid by a third party for referring clients to the third party and internal payments paid within the firm to attract new business to a subsidiary. Members and candidates must disclose all such referral fees.

Rationale

Drinkwater is in violation of the Standards since interdepartmental referral fees are prohibited under the Standard.

Incorrect. Drinkwater has violated Standard VI(C) by not disclosing the referral arrangement at Edward Duke to his clients. Standard VI(C) does not distinguish between referral payments paid by a third party for referring clients to the third party and internal payments paid within the firm to attract new business to a subsidiary. Members and candidates must disclose all such referral fees.

Question 116
L2ET-TB0003-1412
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Keith Slatter is an equity fund manager employed at a firm that currently has no formal policy with regard to keeping employees abreast of the applicable laws, rules, and regulations that apply to the business conducted at the firm. According to the Code and Standards, Slatter's best course of action is to:

- ○ Resign his employment.
- ○ Become the firm expert in compliance and regulation and ensure that employees of the firm are adhering to all relevant rules.
- ◉ Encourage the firm to establish or adopt a code of ethics, for example, the Asset Manager Code of Professional Conduct published by CFA Institute.

Rationale

This Answer is Correct

According to the recommended procedures for compliance with Standard I(A): Knowledge of the Law, members and candidates should encourage their employers to develop or establish a code of ethics that will aid employees in adhering to relevant rules and regulations. The first option is incorrect since resignation is suggested only as a last resort when dissociating from unethical or illegal activity. The second option is incorrect since there is no requirement under the standard for employees to become experts in legal and compliance issues.

Question 117
L2R02TB-AC047-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Barbara White is a portfolio manager with Ajax Advisors. Whenever an oversubscribed issue is offered, she instructs the firm's brokers to purchase shares for her husband's account along with her client accounts. By including an allocation to her husband's account, the client ccounts receive slightly smaller lots in their allocations. Did White violate the Standards of Professional Conduct?

- Yes.
- No, because she did not exclude any client accounts.
- No, because her husband's account is a family client account.

Rationale
Yes.
White's husband's account is, for all intents and purposes, her own. Therefore, she is required to purchase shares for her clients first and, only if any shares remain after satisfying their demand, then purchase for herself.

Rationale
No, because she did not exclude any client accounts.
White's husband's account is, for all intents and purposes, her own. Therefore, she is required to purchase shares for her clients first and, only if any shares remain after satisfying their demand, then purchase for herself.

Rationale
No, because her husband's account is a family client account.
White's husband's account is, for all intents and purposes, her own. Therefore, she is required to purchase shares for her clients first and, only if any shares remain after satisfying their demand, then purchase for herself.

Question 118
L2R02TB-AC018-1512
LOS: LOS-5660
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Black Box Advisors has developed a valuation model that combines fundamental analysis with technical trading indicators to rank stocks. Back-testing of the model shows promise for above average returns. The firm sets up a subscription website that publishes a weekly list of buy and sell recommendations. The advertising section of the website provides the results of simulated portfolios, but describes the source of recommendations only as "a proprietary analytical process." Has the owner of Black Box violated the Standards of Professional Conduct?

- No.
- Yes, she must provide a general description of the investment approach.
- Yes, she must disclose the proprietary algorithms used in the model.

Rationale
No.
The Standard requires members to communicate the basic methods or theoretical approach used to produce their recommendations so that clients and prospects can judge their credibility.

Rationale
Yes, she must provide a general description of the investment approach.
The Standard requires members to communicate the basic methods or theoretical approach used to produce their recommendations so that clients and prospects can judge their credibility.

Rationale
Yes, she must disclose the proprietary algorithms used in the model.
The Standard requires members to communicate the basic methods or theoretical approach used to produce their recommendations so that clients and prospects can judge their credibility.

Question 119

L2ET-TBB204-1412

LOS: LOS-5650

Lesson Reference: Lesson 1: Standard I: Professionalism

Difficulty: medium

According to Standard I(A): Knowledge of the Law, members and candidates must dissociate from illegal and unethical activities of:

- ○ Their employer only.
- ○ Their clients only.
- ● Both their employer and their clients.

Rationale

This Answer is Correct

If a member or candidate has reasonable grounds to believe the imminent or ongoing client or employer activities are illegal or unethical, the member or candidate must dissociate from the activity.

Question 120
L2R02TB-AC046-1512
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Royal Insight is a money management firm handling institutional portfolios. Royal recently landed a contract with Mega Bank to provide investment advisory and portfolio management services. Ken Paine, a research analyst at Royal, currently has a hold recommendation on Mega's stock. Further research and improving economic conditions have caused Paine to consider upgrading his recommendation to buy. According to the Standards of Professional Conduct, Paine must:

- maintain the hold rating for the duration of the contract.
- provide only factual information about Mega Bank.
- issue a buy rating with disclosure of the client relationship.

Rationale
maintain the hold rating for the duration of the contract.
The Standard recognizes that conflicts are sometimes unavoidable and, therefore, requires that they be disclosed.

Rationale
provide only factual information about Mega Bank.
The Standard recognizes that conflicts are sometimes unavoidable and, therefore, requires that they be disclosed.

Rationale
issue a buy rating with disclosure of the client relationship.
The Standard recognizes that conflicts are sometimes unavoidable and, therefore, requires that they be disclosed.

Question 121
L2ET-TBB207-1412
LOS: LOS-5650
Lesson Reference: Lesson 1: Standard I: Professionalism
Difficulty: medium
Which of the following examples of professional conduct is *most likely* to be in violation of Standard I(D): Misconduct?

- ○ An asset manager erroneously reporting the NAV of funds under management to clients.
- ○ A stock market trader engaging in an extramarital affair.
- ◉ A fund manager submitting inflated expenses claims to personally profit at their firm's expense.

Rationale

This Answer is Correct

The first option is unlikely to be a violation of the Standard unless the asset manager fraudulently and deliberately reported an incorrect NAV. The second option is also unlikely to be a violation, since, while the conduct relates to dishonesty, it does not necessarily reflect adversely on the trader's professional activities. The third option is the best answer, since the action clearly involves fraud.

Question 122
L2ET-PQ0215-1502
LOS: LOS-5660
Lesson Reference: Lesson 3: Standard III: Duties to Clients
Difficulty: hard
According to Standard III(B)—Fair Dealing, the use of a "Flash Report" to communicate an update in recommendation is:

- Prohibited.
- Only allowed when the rating is not changed.
- Recommended procedure.

Rationale

Prohibited.
Incorrect. If a detailed institutional recommendation that might take two or three weeks to publish is in preparation, a short summary report including the conclusion, that is, a "Flash Report" might be published in advance. The process of reviewing reports and printing and mailing them, faxing them, or distributing them by e-mail necessarily involves the passage of time, sometimes long periods of time. In large firms with extensive review processes, the time factor is usually not within the control of the analyst who prepares the report. Thus, many firms and their analysts communicate to customers and firm personnel the new or changed recommendations by an update or "Flash Report".

Rationale

Only allowed when the rating is not changed.
Incorrect. If a detailed institutional recommendation that might take two or three weeks to publish is in preparation, a short summary report including the conclusion, that is, a "Flash Report" might be published in advance. The process of reviewing reports and printing and mailing them, faxing them, or distributing them by e-mail necessarily involves the passage of time, sometimes long periods of time. In large firms with extensive review processes, the time factor is usually not within the control of the analyst who prepares the report. Thus, many firms and their analysts communicate to customers and firm personnel the new or changed recommendations by an update or "Flash Report".

Rationale

Recommended procedure.
Correct. If a detailed institutional recommendation that might take two or three weeks to publish is in preparation, a short summary report including the conclusion, that is, a "Flash Report" might be published in advance. The process of reviewing reports and printing and mailing them, faxing them, or distributing them by e-mail necessarily involves the passage of time, sometimes long periods of time. In large firms with extensive review processes, the time factor is usually not within the control of the analyst who prepares the report. Thus, many firms and their analysts communicate to customers and firm personnel the new or changed recommendations by an update or "Flash Report".