SS1-2 Ethics

Bornelli Asset Management offers traditional long-only funds as well as a variety of hedge funds for both private and institutional clients. Bornelli is a well-managed firm of more than 100 employees. Its board of directors has voted to adopt the Asset Manager Code of Professional Conduct (the Code).

Bornelli has hired Ava Campanelli as chief compliance officer with responsibility for implementing the Code. Campanelli evaluates the firm's business-continuity plan. Under the current plan, the technology division backs up all of the firm's computer systems and client records twice daily. The back-ups are stored in a fireproof storage facility offsite. Bornelli outsources certain emergency plans to a disaster recovery firm. The disaster recovery firm is responsible for developing and implementing plans to communicate with employees and mission-critical vendors and suppliers in the event of a facility or communication disruption. The same firm also provides plans for contacting and communicating with clients in event of an extended disruption.

1. Is Bornelli's disaster recovery plan consistent with both the required and recommended standards of the Asset Manager Code?

A. Yes.

B. No, because the plan lacks a backup plan for monitoring, analyzing, and trading investments.

C. No, because the plan only provides for contacting and communicating with clients during periods of extended disruption.

Solution: B.

According to the guidance provided in Section D(6) of the Asset Manager Code, the level and complexity of business-continuity planning depends on the size, nature, and complexity of the organization involved. Bornelli is a large firm with hedge fund investments and it should have alternative plans for monitoring, analyzing, and trading investments if primary systems become unavailable.

The following information is related to Question 2

Jason Locke, CFA, has recently been hired as the Chief Investment Officer of the Escarpment Regional Government Employees' Pension Fund (the Fund). Currently, he is conducting evaluations of all external managers employed by the Fund to ensure that they are providing the highest possible returns for their mandates, while complying with all applicable laws and regulations.

Locke is evaluating the activity of Niagara Growth Managers (NGM), a local money manager allocated 10 percent of the Fund's assets. He realizes that any reduction in the allocation to this local manager will be met with considerable political pressure. The investment policy statement (IPS) for NGM's portion of the Fund's assets states that NGM is to actively manage an equity portfolio of local small-cap, high-tech companies.

Upon his review of NGM's activity, Locke is concerned about two items that he would like explained. At a meeting with NGM's portfolio manager, Emma Black, CFA, Locke asks her to comment on each item:

IPO Share Allocation

Locke	"The Fund's portfolio received 50,000 shares of an initial public offering (IPO) on 1 April. On 15 May, 30,000 shares were removed at the current market price."
Black	"There was a problem with NGM's IPO allocation algorithm. Initially, you were over-allocated and when we discovered the error, your account was adjusted."
Locke	"Short-term interest should have been credited to the Fund for use of its cash to cover the trade. In any case, this was an IPO of a large international high-tech company. It was not an appropriate investment for the portfolio."

2. With regard to the IPO share allocation, are both NGM's method of trade correction on 15 May and Locke's demand for a short-term interest credit, respectively, consistent with the CFA Institute Standards of Professional Conduct?

A. Yes.

B. No, only the method of trade correction is consistent.

C. No, only the demand for a short-term interest credit is consistent.

Solution: C.

Locke's interest claim is legitimate since the Fund's cash was employed to purchase equities that were later removed from the account. Therefore, the Fund is owed interest for the period in question.

SS3 The Asset Management Industry and Professionalism

3. Fiduciary duty is a standard most likely to be upheld by members of a(n):

D. employer.

E. profession.

F. not-for-profit body.

Solution: B.

Fiduciary duty is an obligation to deliver a high standard of care when acting for the benefit of another party. Professionals must act in the best interest of the client, exercising a reasonable level of care, skill, and diligence. Other entities—including employers, regulators, trade associations, and not-for-profit bodies—may also support an industry but are not the same as professional bodies. Unlike professions, these other entities generally do not exist to set and maintain professional standards.

4. When an ethical dilemma occurs, an investment professional should most likely first raise the issue with a:

A. mentor outside the firm.

B. professional body's hotline.

C. senior individual in the firm.

Solution: C.

When a dilemma occurs, raising an issue internally is often a good starting place and creates an opportunity for an independent internal review. Protecting the client and the firm may take priority over the position of an individual professional raising a concern.