

# Ethical & Professional Standards

CFA一级强化班

讲师：林正



林正

6年授课，4000+授课课时

## 学位证书

- 金程教育资深培训师
- 英国Essex大学硕士
- CFA持证人
- PMP ( Project Management Professional ) 持证人

## 服务客户

- 中国银行、中国建设银行、民生银行、平安证券、杭州联合银行、杭州银行、国泰君安证券、苏州元禾控股等。

## 工作背景

- 曾历任某外资银行支行行长，总行战略项目经理，十二年的外企银行工作经历，积累了丰富的金融实战经验。
- 现为金程教育资深培训师，熟悉CFA考试重点，CFA全级别授课。

# *Topic Weightings in CFA Level I*

Topics	Weights (%)
Quantitative Methods	8-12
Economics	8-12
Financial Statement Analysis	13-17
Corporate Issuers	8-12
Equity	10-12
Fixed Income	10-12
Derivatives	5-8
Alternative Investments	5-8
Portfolio Management	5-8
<b>Ethical and Professional Standards</b>	<b>15-20</b>

# 课件使用说明

## ● 强化班知识点说明和使用指南

序号	课件元名称（知识点）	必考	高频	低频
1	Explain ethics and professionalism	0	0	1
2	Ethical vs. Legal Standards	0	0	1
3	Proceedings and the hearing panel	1	0	0
4	Code of ethics	0	0	1
5	I(A).Knowledge of the law	0	1	0
6	I(B).Independence and objectivity	1	0	0

- 必考知识点指的是近10年考试中考试频率大于等于75%的考点，在强化班中重点讲解，必须掌握；
- 高频知识点指的是近10年考试中考试频率介于25%到75%的考点，在强化班中重点讲解，必须掌握；
- 低频知识点指的是近10年考试中考试频率小于25%的考点，在基础班中重点讲解，学员可以根据自己的掌握情况在基础班中巩固学习；
- 本学科知识点合计27个，其中必考知识点20个，高频知识点4个，低频知识点3个，掌握必考和高频考点覆盖了近10年98.22%的题目。

# Ethical & Professional Standards

1. Ethics and Trusts in the Investment Profession
2. Code of Ethics and Standards of Professional Conduct
3. Guidance for Standards I-VII
4. Introduction to the Global Investment Performance Standards (GIPS)
5. Ethics Application

*Framework*

# Module



## Code of Ethics and Standards of Professional Conduct

1. Proceedings and the hearing panel

# Proceedings and the hearing panel

- ▣ Proceedings
- ▣ The Panel



# Proceedings

- The CFA Institute **Board of Governors** maintains oversight and responsibility for the **Professional Conduct Program (PCP)**.
- PCP and **Disciplinary Review Committee (DRC)** are responsible for enforcement of the Code and Standards. Professional Conduct inquiries come from a number of sources.
  - Self-disclosure on annual Professional Conduct Statements of involvement in civil litigation or a criminal investigation, or that the member or candidate is the subject of a written complaint.
  - Written complaints about professional conduct received by the Professional Conduct staff.
  - Evidence of misconduct by a member or candidate that the Professional Conduct staff received through public sources, such as a media article or broadcast.
  - A report by a CFA exam proctor of a possible violation during the examination.



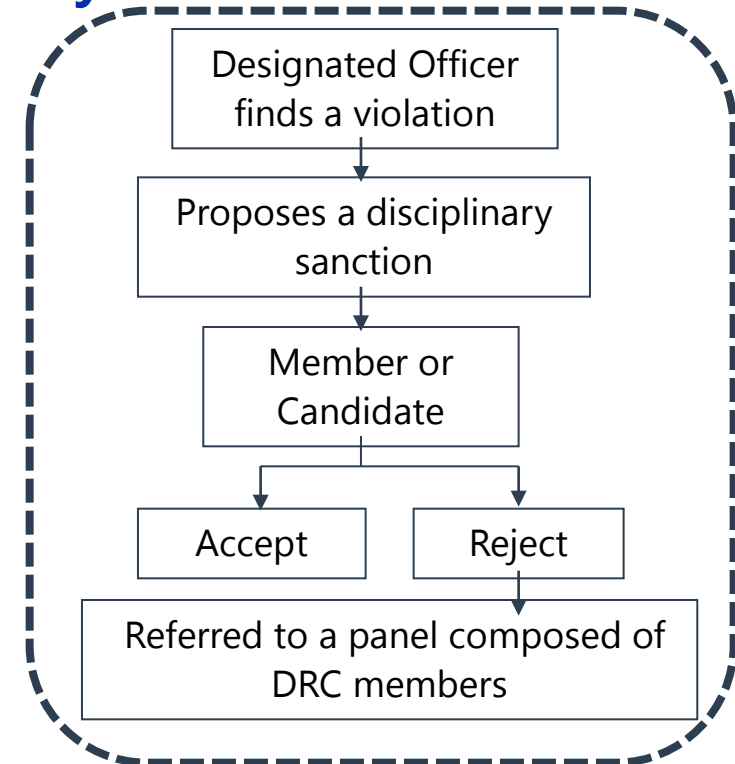
# Proceedings

- Once an inquiry is initiated, Professional Conduct staff **may** requests (in writing) an explanation from the subject member or candidate **and may**:

- Interview the subject member or candidate
- Interview the complainant or other third parties
- Collect documents and records relevant to the investigation

- The Designated Officer **may decide**:

- That no disciplinary sanctions are appropriate
- To issue a cautionary letter
- To discipline the member or candidate



# The Panel

- If the member or candidate does not accept the charges and proposed sanction, the matter is referred to a panel composed of **DRC** (Discipline Review Committee) members.
- Panels review materials and presentations from Professional Conduct staff and from the member or candidate.
- The panel's task is to determine whether a violation of the Code and Standards or testing policies occurred and, if so, what sanction should be imposed.
- Sanctions imposed by CFA Institute may have significant consequences; they include **public censure**, **suspension of membership and use of the CFA designation**, and **revocation of the CFA charter**.  
Candidates enrolled in the CFA Program who have violated the Code and Standards or testing policies may be **suspended or prohibited** from further participation in the CFA Program.

# Example

## Proceedings and the hearing panel

- Holly Baker, CFA, is explaining the CFA Institute Code of Ethics to a client. Which of the following statements could Baker make to most likely reflect disciplinary sanctions the CFA Institute may impose? Sanctions include:
  - A. fines for violations.
  - B. revocation of membership.
  - C. banishment from the industry.
- Correct Answer: B
  - The CFA Institute may revoke membership for violations of the Institute Code of Ethics. CFA Institute Bylaws do not include fines as a sanction and CFA Institute does not have the authority to ban an individual from the business.

# Summary

## Code of Ethics and Standards of Professional Conduct

Proceedings and the hearing panel

# Module



## Guidance for Standards I–VII

I. Professionalism

II. Integrity of Capital Markets

III. Duty To Clients

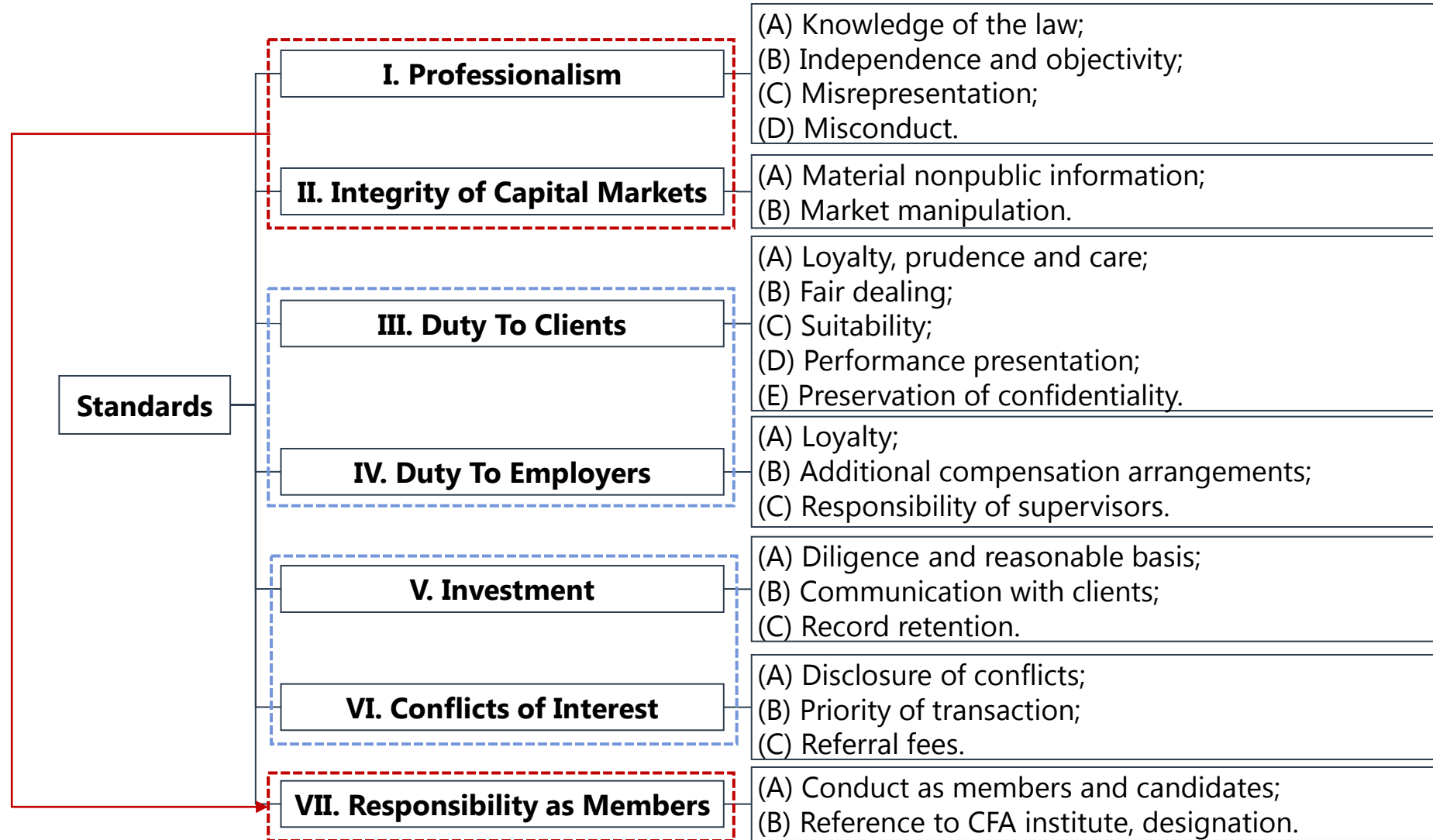
IV. Duty To Employers

V. Investment

VI. Conflicts of Interest

VII. Responsibility as Members

# Guidance for Standards I-VII



# 1. I(A). Knowledge of the law

- ▣ Content
- ▣ Guidance



# 1. Standard I (A): Content

## ● Content

1. Members and Candidates must understand and comply with all applicable laws, rules, and regulations (including the CFA Institute Code of Ethics and Standards of Professional Conduct) of any government, regulatory organization, licensing agency, or professional association governing their professional activities.
2. In the event of conflict, Members and Candidates must comply with the more strict law, rule, or regulation.
3. Must not knowingly participate or assist in any violation of such laws, rules, or regulation.
4. Must dissociate from any violation of such laws, rules, or regulations.



# 1. Standard I (A): Guidance

## ● Guidance - Code and Standards vs. local law

5. Must know and **should** know the laws and regulations related to their professional activities in all countries in which they conduct business.
6. **Must** comply with law directly governing. However, **Not should have detailed knowledge of or be expert** on all laws that could **potentially** govern his activities, **not expert** on compliance.
7. Always adhere to the **most strict** rules and requirements (law or CFA institute Standards) that apply. Members and candidates must not engage in conduct that constitutes a violation of the Code and Standards, even though it may otherwise be legal.
8. Comply with the last applicable law if transferable applicability.

Workplace (Applicable) Stating that residence law applies.	Residence	Comply with
Less strict	More strict	Last applicable is the residence law, more strict than Code → Adhere to the law of more strict country
More strict	Less strict	Last applicable is the residence law, less strict than Code → Adhere to Code and Standards

# 1. Standard I (A): Guidance

## ● Guidance - Participation or association with violations by others

9. Know → attempt to stop the behavior by bringing it to the attention of the employer through supervisor or compliance department → (if unsuccessful) → dissociate and document → even quit without choice.
10. Suspect → Consult → but can't be absolved from requirements to compliance
11. There is **no** requirement under Standards to report violations to governmental authorities, but this may be advisable in some circumstances and required by law in others.
12. Inaction combined with continuing association with those involved in illegal or unethical conduct may be construed as participation or assistance in the illegal or unethical conduct.

# 1. Standard I (A): Guidance

- **Guidance - Investment Products and Applicable Laws**

13. Members and candidates involved in creating or maintaining investment services, investment products, packages of securities and derivatives should be mindful of **where** these products or packages will be sold as well as their places of origination (the place of sales and origination).
14. The applicable laws and regulations of the countries or regions of origination and expected sale should be understood **by those responsible for the supervision of** the services or creation and maintenance of the products or packages.

# 1. Standard I (A): Guidance

- **Guidance - Investment Products and Applicable Laws**

15. Should make reasonable efforts to review whether associated firms that are distributing products or services also abide by the laws and regulations.
16. Should undertake necessary due diligence when transacting cross-border business to understand the multiple applicable laws and regulations, in order to protect the reputation of the firm and themselves.
17. Seek appropriate guidance from the firm's compliance or legal departments and legal counsel outside the organization when uncertain about which laws or regulations in conducting business in multiple jurisdictions.

# Summary

## Guidance for Standards I–VII

### I(A). Knowledge of the law

Code and standards vs. applicable law

How to deal with violation

Investment product and applicable laws

## 2. I(B). Independence and objectivity

---

- ▣ Content
- ▣ Guidance



## 2. Standard I(B): Content

- **Content:**

1. Members and Candidates must use reasonable care and judgment to achieve and maintain independence and objectivity in their professional activities.
2. Must not offer, solicit, or accept any gift, benefit, compensation, or consideration that reasonably could be expected to compromise their own or another's independence and objectivity.

## 2. Standard I(B): Guidance

### ● Guidance

3. Mainly concerning how to deal with internal and external conflicts.
4. Reject gift that could be expected to compromise their own or another's independence and objectivity.

#### **(Best Practice)**

- ✓ Ordinarily, modest and normal gift is OK only if its purpose is not to influence independence.

Benefits may include gifts, invitations to lavish functions, tickets, favors, job referrals, and so on.

5. Gift from corporate: should evaluate both the actual effect on his independence and objectivity and in the eyes of clients.



## 2. Standard I(B): Guidance

### ● Guidance

6. Gift from clients: Receiving a gift, benefit, or consideration from a client can be distinguished from gifts given by entities seeking to influence independence to the detriment of other clients. Client's gift should be disclosed, if not → violate I(B).
  - ✓ **When possible**, prior to accepting “bonuses” or gifts from clients, members and candidates should disclose to their employers such benefits offered by clients.
    - If notification is not possible prior to acceptance, members and candidate must disclose to their employers benefits previously accepted from clients.
  - ✓ Disclosure allows the employer of a member or candidate to make an independent determination about **the extent** to which the gift may affect the member's or candidate's independence and objectivity.

## 2. Standard I(B): Guidance

### ● Guidance - Buy-Side clients

#### 7. **Buy-Side Clients may try to pressure sell-side analysts.**

- ✓ Institutional clients are the primary users of sell-side research, either directly or with soft dollar brokerage.
- ✓ Rating downgrade: some portfolio managers may support sell-side ratings inflation → affect the portfolio's performance and manager's compensation.
- ✓ Portfolio performance is subject to media and public scrutiny, affect the manager's professional reputation.

#### 8. For portfolio managers:

- ✓ It is improper to threaten or engage in retaliatory practices.
- ✓ Although most portfolio managers do not engage in such practices, the perception by the research analyst that a reprisal is possible may cause concern and make it difficult to maintain independence.

## 2. Standard I(B): Guidance

### ● Guidance - Fund manager relationships and Custodial Relationships

9. Members and candidates responsible for hiring and retaining outside managers and third-party custodians should not accept gifts, entertainment, or travel funding that may be perceived as impairing their decisions.
10. Primary and **secondary fund managers** and **third-party custodians** often arrange educational and marketing events to inform others about their business strategies or investment process.
  - ✓ Must review the merits of each offer individually in determining whether they may attend yet maintain independence.

## 2. Standard I(B): Guidance

### ● Guidance - Investment banking relationships

11. Firewall between research and investment banking should be built to minimize conflicts of interest.
  - ✓ Separate **reporting structures** for personnel on the research side and personnel on the investment banking side.
  - ✓ **Compensation arrangement** that minimizes the pressures on research analysts and rewards objectivity and accuracy. Compensation should **not link analyst remuneration directly to** investment banking assignments in which analyst may participate as a team member.
12. It is appropriate to have analysts work with investment **bankers only when the conflicts are adequately and effectively managed and disclosed.**
13. Firms should also regularly review policies and procedures to determine whether analysts are adequately safeguarded and to improve the transparency of disclosures relating to conflict of interests.

## 2. Standard I(B): Guidance

### ● Guidance - Performance Measurement and Attribution

14. Members and candidates working within a firm's investment performance measurement department may also be presented with situations that challenge their independence and objectivity.
15. As performance analysts, their analysis may reveal instances where managers may appeared to **stray from their mandate**. Or the performance analyst may receive requests to **alter the construction of composite indices** due to negative results for a selected account or fund.
16. The member or candidate must not allow internal or external influences to affect their independence and objectivity as they faithfully complete their performance calculation and analysis related responsibilities.

## 2. Standard I(B): Guidance

- **Guidance - Public companies**

17. Analysts should **not be pressured to issue favorable research** by the companies they follow. Can promise to cover the firm, should not promise favorable report about the firm.
18. Due diligence in financial research and analysis involves gathering information from public disclosure documents and also company management and investor-relations personnel, suppliers, customers, competitors, and other relevant sources.

## 2. Standard I(B): Guidance

- **Guidance - Credit rating agency opinions**

19. Members and candidates at rating agencies should ensure that procedures at the agencies **prevent undue influences** from a sponsoring company during the analysis.
20. Should abide by their agencies' and the industry's standards of conduct regarding the analytical process and the distribution of reports.
21. The rating agencies need to develop **the necessary firewalls and protections** to allow the independent operations of their different business lines.
22. When using information provided by credit rating agencies, Should be mindful of the potential conflicts of interest.

## 2. Standard I(B): Guidance

### ● Guidance - Influence during the Manager Selection/Procurement Process

- 23. The need for members and candidates to maintain their independence and objectivity extends to the **hiring or firing** of those who provide many business services beyond investment management.
- 24. When serving in a hiring capacity, members and candidates should not solicit gifts, contributions, or other compensation that may affect their independence and objectivity. Solicitations do not have to benefit members and candidates personally to conflict with Standard I(B).
  - ✓ **Requesting contributions to a favorite charity or political organization** may also be perceived as an attempt to influence the decision-making process.
- 25. Members and candidates serving in a hiring capacity should refuse gifts, donations, and other offered compensation that may be perceived to influence their decision-making process.



## 2. Standard I(B): Guidance

26. When working to earn a new investment allocation, members and candidates should not offer gifts, contributions, or other compensation to influence the decision of the hiring representative.
- ✓ The offering of these items **with the intent to impair the independence and objectivity** of another person would not comply with standard I(B).
  - ✓ Such prohibited actions may include offering donations to a charitable organization or political candidate referred by the hiring representative. **(pay to play scandal)**

## 2. Standard I(B): Guidance

- **Guidance - Issuer-Paid research**

- 27. Remember that this type of research is fraught with potential conflicts.
- 28. Analysts' compensation for preparing such research should be limited, and the preference is for **a flat fee that is not linked to their conclusions or recommendations** (directly or indirectly)
- 29. Must fully disclose potential conflict of interest, including the nature of compensation. If not → misleading investors
- 30. Conduct a thorough analysis of the company's financial statements based on public information, benchmarking within a peer group, and industry analysis.
  - ✓ Distinguish between **fact and opinion**.

## 2. Standard I(B): Guidance

### ● Guidance - Travel Funding

31. The benefits related to accepting paid travel extend beyond the cost savings to the member or candidate and his firm, such as the chance to talk exclusively with the executives of a company or learning more about the investment options provided by an investment organization.
32. **Best practice:** always use **commercial transportation** rather than accept paid travel arrangements from an outside company.
33. Should commercial transportation be unavailable, may accept modestly arranged travel to participate in appropriate information-gathering events, such as a property tour.

### ● Guidance – Social Activities

34. When seeking corporate financial support for conventions, seminars, or even weekly society luncheons, should evaluate both the actual effect on their independence and whether their objectivity might be perceived to be compromised in the eyes of their clients.

# Summary

## **Guidance for Standards I–VII**

### **I(B). Independence and objectivity**

Buy-side clients, fund manager and custodial relationships,  
public companies, manager selection

Performance, investment banking

Issuer-paid research, travel funding, rating agency

# 3. I(C). Misrepresentation

- ▣ Content
- ▣ Guidance

### 3. Standard I(C): Content

- **Content:**

1. Must not knowingly make any misrepresentations relating to investment analysis, recommendations, actions, or other professional activities.
2. Once finding misrepresentation (e.g. typographical error), correct the error as soon as possible, or violate I (C).

### 3. Standard I(C): Guidance

#### ● Guidance

3. A misrepresentation is any **untrue statement or omission of a fact** or any statement that is otherwise false or misleading.
- ✓ Must **not knowingly omit** or misrepresent information or give a false impression of a firm, organization, or security in oral representations, advertising (whether in the press or through brochures), electronic communications, or written materials (whether publicly disseminated or not).
  - ✓ Omission of a fact or outcome: Although not every model can test for every factor or outcome, should ensure that the analyses incorporate a broad range of assumptions—from very positive scenarios to extremely negative scenarios.

### 3. Standard I(C): Guidance

- Omissions

4. **The omission of a fact or outcome is misleading**, especially given growing use of technical analysis. Many members and candidates rely on **models** and processes to scan for new investment opportunities, to develop investment vehicles, and to produce investment recommendations and ratings. Findings from models **shall not be presented as fact**.
5. Omissions are also important in regards to what information is provided concerning the **performance measurement and attribution process**.
  - ✓ Member and candidates should encourage their firms to develop strict policies for **composite development to prevent cherry picking** — situations in which selected accounts are presented as representative of the firm's abilities. The omission of all accounts appropriate for the defined composite may misrepresent to clients the success of the manager's implementation of its strategy.



### 3. Standard I(C): Guidance

- **Guidance - Impact on Investment Practice**

6. Guarantee the investment performance

- ✓ **Prohibit: Guaranteeing specific return** which is inherently volatile, because it is misleading to investors.
- ✓ **Not prohibit:** Providing clients with information on investments that have guarantees built into the structure of the product **or** for which an institution has agreed to cover any losses.

7. Members and candidates must not misrepresent any aspect of their practice, including (but not limited to) their **qualifications or credentials**, the qualifications or services provided by their firm, their performance record and the record of their firm, and the characteristics of an investment.

- ✓ A company is prohibited from saying “we can provide all services you need”. Proper way is to provide **a list of services** available.

### 3. Standard I(C): Guidance

#### 8. Investing through outside managers

- ✓ If invest in areas outside a firm's core competencies through **outside managers**, must disclosed intended use of external managers, members and candidates must not represent those managers' investment practices as their own. For further detail, refer to V(B).

#### 9. Using third-party information

- ✓ Should exercise care and diligence when using **3rd-party information**.
- ✓ When it affects the professional's business practices, investment professional should be responsible for the misrepresentation.

### 3. Standard I(C): Guidance

#### ● Guidance - Performance Reporting

10. Members and candidates may misrepresent the success of their performance record through presenting **benchmarks that are not comparable to their strategy.**
  - ✓ Clients can be misled if the benchmark's results are not reported on a basis comparable to that of the fund's or client's results.
  - ✓ **Best practice:** selecting the most appropriate available benchmark from a universe of available options.
11. The transparent presentation of appropriate performance benchmarks is an important aspect in providing clients with information that is useful in making investment decisions.
12. Standard I(C) does not require that a benchmark always be provided in order to comply. Some investment strategies may not lend themselves to displaying an appropriate benchmark because of the complexity or diversity of the investments included.

### 3. Standard I(C): Guidance

13. Some investment strategies may use reference indices that do not reflect the opportunity set of the invested assets.
- ✓ A hedge fund comparing its performance with a "**cash plus**" basis.
  - ✓ When such a benchmark is used, members and candidates should take reasonable efforts to ensure that they disclose the reasons behind the use of this reference index to avoid misrepresentations of their performance.
14. Members and candidates should discuss with clients on a continuous basis the appropriate benchmark to be used for performance evaluations and related fee calculations.

### 3. Standard I(C): Guidance

15. Reporting misrepresentations may also occur when **valuations** for illiquid or non-traded securities are available from more than one source. When different options are available, members and candidates may be tempted to switch providers to obtain higher security valuations.
- ✓ Members and candidates should take reasonable steps to provide accurate and **reliable** security pricing information to clients on a **consistent** basis.
  - ✓ Consistency in the reported information will limit misperceptions that misrepresented values may have assisted in manipulating investors into continuing to hold certain securities in their portfolios.
  - ✓ Changing pricing providers should **not** be based solely on the justification that the new provider reports a higher current value of a security.

### 3. Standard I(C): Guidance

#### ● Social Media

16. When communicating through social media channels, members and candidates should provide only the same information they are allowed to distribute to clients and potential clients through other traditional forms of communication.
  - ✓ The online or interactive aspects of social media do not remove the need to be open and honest about the information being distributed.
17. Actions undertaken through social media that knowingly misrepresent investment recommendations or professional activities are considered a violation of Standard I(C).
  - ✓ The perceived anonymity granted through these platforms may entice individuals to misrepresent their qualifications or abilities or those of their employer.

### 3. Standard I(C)

- **Guidance – Plagiarism**

#### **18. Plagiarism**

- ✓ Definition: Copying or using in substantially the same form materials prepared by others **without acknowledging** the source of the material or identifying the author and publisher of such material.
- ✓ Applied in: oral communications (e.g. group meetings), visits with clients, use of audio/video media, and telecommunications.
- ✓ Must not copy (or represent as their own) original idea/material without permission. Must acknowledge and identify the source of ideas/material that is not their own. (e.g. a computer model derived from others' idea)

### 3. Standard I(C)

- **Guidance – Plagiarism**

**19. Forms of plagiarism:**

- ✓ Take a study done by others, change name of the author, and release it as ones own.
- ✓ Using excerpts from others' reports (whether verbatim or slight changes in wording) without acknowledgement.
- ✓ Citing "leading analysts" and "investment experts" without naming specific reference.
- ✓ Using charts and graphs without stating sources.



## ●—— 3. Standard I(C): Guidance - Plagiarism ——●

### ● Guidance - Plagiarism

#### 19. Forms of plagiarism: (cont.)

- ✓ Presenting statistical estimates of forecasts prepared by others and identifying the sources without including the qualifying statements or caveats that may have been used.
- ✓ Copying proprietary computerized spreadsheets or algorithms without authorization of the creators.
- ✓ Preparation of research reports based on multiple sources of information without acknowledging the sources. (e.g. ideas, statistical compilations, and forecasts combined to give the appearance of original work).
  - ❑ Cannot use undocumented forecasts, earnings projections, asset values, etc.
  - ❑ Sources must be revealed to bring the responsibility directly back to the author or the firm involved.

## ●—— 3. Standard I(C): Guidance - Plagiarism ——●

### ● Guidance - Plagiarism

20. In distributing 3rd-party, outsourced research, may use and distribute reports as long as not representing oneself as the author.

✓ May add value for the client by sifting through research and repackaging it for clients.

□ Clients should be fully informed that they are paying for the ability of the member or candidate to find the best research from a wide variety of sources.

✓ Should disclose whether the research presented comes from another source, from either within or outside the member's firm.

□ This allows clients to understand who has the expertise.

## ●—— 3. Standard I(C): Guidance - Plagiarism ——●

### ● Guidance - Plagiarism

21. When citing from mainstream media outlet:

- ✓ Cannot only cite the information from the intermediary, in case of misunderstanding and potential deviation from the viewpoint of the original author.
- ✓ **Best practice: Either** obtain the information directly from the author and cite only that author **or** use the information provided by the intermediary and cite both sources.

### 3. Standard I(C): Guidance

- **Guidance - Work Completed for Employer**

22. Firm may issue future reports without attribution to prior analysts, but a member or candidate cannot reissue a previously released report solely under his or her name.
- ✓ **May** use other people's work (research, models, etc.) within the same firm without committing a violation.
  - ✓ When the original analyst leaves the firm, research and models developed while employed are the property of the firm. The firm retains the right to continue using the work completed after leaving.
    - ❑ The firm may issue future reports without providing attribution to the prior analysts.
    - ❑ A member or candidate cannot reissue a previously released report solely under his or her name.

# Summary

## **Guidance for Standards I–VII**

### **I(C).Misrepresentation**

Factors impacting on investment, performance reporting

Social media

Omissions, plagiarism, work completed for employer

## 4. I(D). Misconduct

- ▣ Content
- ▣ Guidance

## 4. Standard I(D): Content

- **Content**

1. Members and Candidates must not engage in any professional conduct involving dishonesty, fraud, or deceit or commit any act that reflects adversely on their professional reputation, integrity, or competence.

## 4. Standard I(D): Guidance

### ● Guidance

#### 2. Dishonest conduct

- ✓ Any act that involves lying, cheating, stealing, or other dishonest conduct would violate this standard if the offense reflects adversely on professional activities.
- ✓ Do not abuse this standard to settle personal, political, or other disputes unrelated to professional ethics.

#### 3. Absence of appropriate conduct and sufficient effort

- ✓ Member or candidate is expected to conduct the necessary due diligence to understand the nature and risks of investment before making investment recommendations.
- ✓ If not taking such steps, instead, relying on others, is violation.



## 4. Standard I(D): Guidance

### ● Guidance

4. Conduct that damages trustworthiness or competence may include behavior that negatively affects ability to perform professional activities.
  - ✓ E.g. abusing alcohol during business hours. Because it could have a detrimental effect on the ability to fulfill professional responsibilities.
  - ✓ **Personal bankruptcy** may not reflect on the integrity or trustworthiness of the person declaring bankruptcy,
    - But if the circumstances of the bankruptcy involve fraudulent or deceitful business conduct, the bankruptcy may be a violation of this standard.

# Summary

## Guidance for Standards I–VII

### I(D).Misconduct

Any dishonesty, fraud, or deceit or commit any act that reflects adversely on their professional reputation, integrity, or competence

## Guidance for Standards I-VII

- Alan Quanta, CFA, provides credit rating analysis of high-yield bonds using external credit ratings as a foundation. At the end of the last quarter, Quanta's firm, North Investment Bank, held a large position in the bonds of Veyron Corporation, a real estate company with all of its land holdings in a country recently downgraded by several credit rating agencies. The downgrades made Veyron bonds extremely difficult to sell because the bond price has dropped every day since the downgrades. Quanta has been asked by his supervisor to contact the firm's institutional clients to convince them Veyron bonds are still an attractive purchase, especially at these lower prices. Quanta does not consider the Veyron bonds a buy at this price level. According to the CFA Institute Code of Ethics and Standards of Professional Conduct, the most appropriate action for Quanta is to:
  - A. obey his supervisor's request.
  - B. ignore his supervisor's request.
  - C. promote the bonds with appropriate disclosures.

## Guidance for Standards I-VII

- Correct answer: B.
  - Quanta must refuse to promote Veyron bonds until they are an attractive purchase based on fundamental analysis and market pricing. If Quanta followed the request from his supervisor, he would be in violation of Standard I(B)–Independence and Objectivity, as he does not rate Veyron bonds as a buy. His opinion of the Veyron bonds must not be affected by internal pressure or compensation.

## Guidance for Standards I-VII

- Christina Ng, a Level I CFA candidate, defaulted on a bank loan she obtained to pay for her Master's degree tuition when her wedding cost more than expected. A micro finance loan company lent her money to pay off the tuition loan in full including penalties and interest. The micro finance loan company even extended further credit to pay for her parent's outstanding medical bills. Unfortunately, her parent's health problems escalated to the point where Ng had to take extensive time away from work to deal with the issues. She was subsequently fired and consequently defaulted on the second loan. As she was no longer employed, Ng decided to file for personal bankruptcy. Do the loan defaults leading up to Ng's bankruptcy most likely violate Standard I(D)–Misconduct?
  - A. No.
  - B. Yes, with regard to the first loan default.
  - C. Yes, with regard to the second loan default.

## Guidance for Standards I-VII

- Correct answer : A.
- Because while Ng's first loan default, which played a part in the subsequent bankruptcy, is a result of poor financial choices (i.e., paying for higher wedding costs rather than her tuition loan), neither of the loan defaults or bankruptcy involves fraudulent or deceitful business conduct but are based on unfortunate personal circumstances. Therefore, she would most likely not be in violation of Standard I(D)–Misconduct.

## Guidance for Standards I-VII

- Grey recommends the purchase of a mutual fund that invests solely in long-term U.S. Treasury bonds. He makes the following statements to his clients:
- Statement 1: "The payment of the bonds is guaranteed by the U.S. government; therefore, the default risk of the bonds is virtually zero."
- Statement 2: "If you invest in the mutual fund, you will earn a 10 percent rate of return each year for the next several years based on historical performance of the market."
- Did Grey's statements violate the CFA Institute Code and Standards?
  - A. Neither statement violated the Code and Standards.
  - B. Only Statement 1 violated the Code and Standards.
  - C. Only Statement 2 violated the Code and Standards.

## Guidance for Standards I-VII

- Correct answer : C
- This question involves Standard I(C)—Misrepresentation. Statement 1 is a factual statement that discloses to clients and prospects accurate information about the terms of the investment instrument. Statement 2, which guarantees a specific rate of return for a mutual fund, is an opinion stated as a fact and, therefore, violates Standard I(C). If Statement 2 were rephrased to include a qualifying statement, such as "in my opinion, investors may earn. . .," it would not be in violation of the Standards.



## 5. II(A). Material Nonpublic information

- Content
- Guidance

## 5. Standard II(A): Content

### ● Content:

1. Members and Candidates who possess material nonpublic information that could affect the value of an investment must **not act** or **cause others to act** on the information.
  - ✓ Trading or inducing others to trade on material nonpublic information erodes confidence in capital markets, institutions, and investment professionals by supporting the idea that those with inside information and special access **can take unfair advantage of the general investing public.**

## 5. Standard II(A): Guidance

### ● Guidance

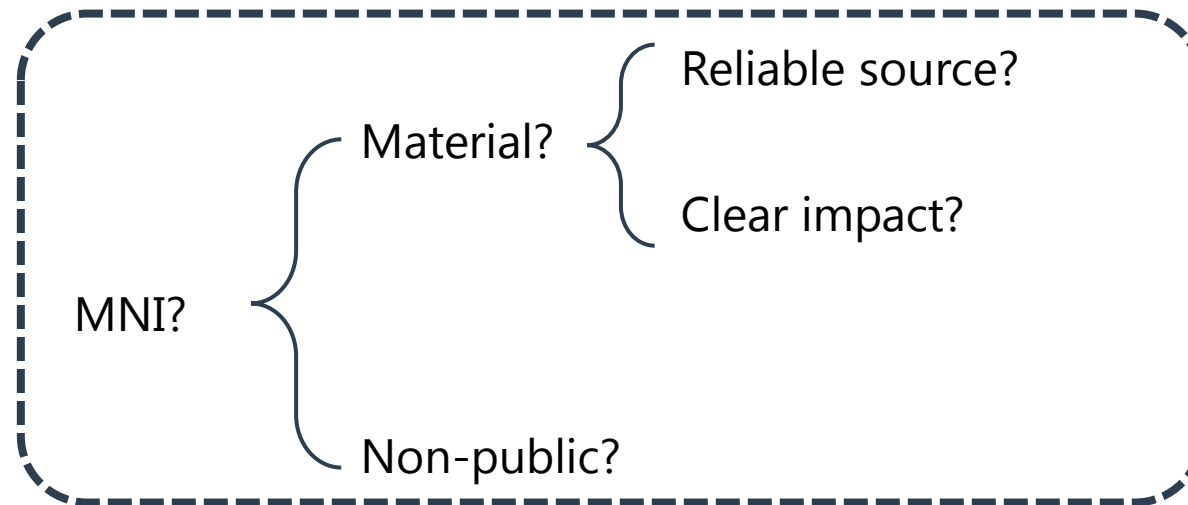
2. Trading or inducing others to trade on material nonpublic information have caused and will continue to cause investors to avoid capital markets because the markets are perceived to be "rigged" in favor of the knowledgeable insider.
3. Must not use such information to :
  - ✓ Directly buy and sell of individual securities or bonds
  - ✓ Influence their investment actions related to derivatives, mutual funds, or other alternative investments.

## 5. Standard II(A): Guidance

### ● Guidance - What Is “Material” Information ?

#### 4. Material Nonpublic

- ✓ Information is “**material**” if its disclosure would likely have an impact on the price of a security **or** if reasonable investors would want to know the information before making an investment decision.
- ✓ Information is “**nonpublic**” until it has been disseminated or is available to the marketplace in general.



## 5. Standard II(A): Guidance

- **Guidance - What Is “Material” Information ?**

5. Substance and specificity determines the materiality

- Company-related information

- ✓ Earnings
- ✓ Mergers, acquisitions, tender offers, or joint ventures
- ✓ Changes in assets or asset quality
- ✓ Innovations products, processes, or discoveries
- ✓ New licenses, patents, registered trademarks, or regulatory approval/rejection of a product

## 5. Standard II(A): Guidance

### ● Guidance - What Is “Material” Information ?

5. Substance and specificity determines the materiality (cont.)

#### ○ Company-related information

- ✓ Developments regarding customers or suppliers (e.g. the acquisition or loss of a contract)
- ✓ Changes in management
- ✓ Changes in auditor notification or the fact that the issuer may no longer rely on an auditor's report or qualified opinion
- ✓ Events regarding the issuer's securities
- ✓ Bankruptcies
- ✓ Significant legal disputes
- ✓ New or changing equity or debt rating issued by third party

## 5. Standard II(A): Guidance

### ● Guidance - What Is “Material” Information ?

- 5. Substance and specificity determines the materiality (cont.)
  - Macro-economy
    - ✓ Government reports of economic trends (employment, housing starts, currency information, etc.)
  - Large orders
    - ✓ Orders for large trades before they are executed
  - Well known analyst
    - ✓ Reports from well known analyst
  - Qualified personnel
    - ✓ Information about trials of a new drug
    - ✓ Additionally, information about trials of a new drug, product, or service under development from qualified personnel involved in the trials is likely to be material, whereas educated conjecture by subject experts not connected to the trials is unlikely to be material.
  - Competitors
    - ✓ Competitor's estimation → not MNI

## 5. Standard II(A): Guidance

### ● Guidance - What constitutes “nonpublic” Information ?

6. Information is “nonpublic” until it has been disseminated or is available to the marketplace.
  - ✓ Not necessary to wait for the slowest method of delivery.
  - ✓ Once the information is disseminated to the market, it is public information that is no longer covered by this standard.
7. Selective disclosure
  - ✓ Disclosure to a room full of analysts does not necessarily make the disclosed information “public.”
  - ✓ Analysts should also be alert to the possibility that they are selectively receiving MNI when a company provides them with guidance or interpretation of financial statements or regulatory filings.
  - ✓ Selective disclosure may violate MNI. If MNI was disclosed selectively, the listed company should issue a press release or reach public dissemination.



## 5. Standard II(A): Guidance

- **Guidance – When can use “nonpublic” Information ?**

8. A member or candidate may use insider information provided legitimately by the source company for the specific purpose of **conducting due diligence** according to the business agreement between the parties for such activities as mergers, loan underwriting, credit ratings, and offering engagements.

## — 5. Standard II(A): Guidance - Mosaic Theory —

### ● Guidance – Mosaic Theory

9. Mosaic theory:

	Material	Non-material
Public	√	√, but unnecessary
Non-public	×	√

- May use conclusions from the analysis of material public and nonmaterial nonpublic information even if those conclusions would have been material inside information had they been communicated directly to the analyst by a company.
  - ✓ A perceptive analyst reaches a conclusion about a corporate action or event through an analysis of public information and items of nonmaterial nonpublic information. → not violate II (A)
  - ✓ Should save and document all the research when applying mosaic theory → **Standard V(C)**.

## ● — 5. Standard II(A): Guidance – Social Media — ●

### ● Guidance – Social Media

10. Members and candidates participating in groups with membership limitations should verify that material information obtained from these sources can also be accessed from a source that would be considered available to the public (e.g., company filings, webpages, and press releases).
- ✓ The use of these platforms would be comparable with other traditional forms of communications, such as e-mails and press releases.
  - ✓ Members and candidates, as required by Standard I(A), should also complete all appropriate regulatory filings related to information distributed through social media platforms.

## — 5. Standard II(A): Guidance – Industry Expert —

### ● Guidance – Industry expert

11. Members and candidates may provide compensation to individuals for their insights without violating this standard. However, members and candidates are **ultimately responsible** for ensuring the information they receive does not constitute material nonpublic information.
- ✓ Members and candidates would be prohibited from taking investment actions on the associated firm until the information became publicly known to the market.
  - ✓ Firms connecting experts with members or candidates often require both parties to sign agreements concerning the disclosure of material nonpublic information.

## 5. Standard II(A): Guidance

- **Guidance - Investment Research Reports**

12. **When a well-known or respected analyst issues a report or makes changes to his or her recommendation, that information alone may have an effect on the market and thus may be considered material. Theoretically, such a report would have to be made public before it was distributed to clients.**
13. The analyst is not a company insider, however, and does not have access to inside information. Presumably, the analyst created the report from information available to the public (mosaic theory) and by using his or her expertise to interpret the information. The analyst's hard work, paid for by the client, generated the conclusions.
14. **Simply because the public in general find the conclusions material does not require that the analyst make his/her work public**. Investors who are not clients of the analyst can either do the work themselves or become clients of the analyst for access to the analyst's expertise.

# Summary

## Guidance for Standards I–VII

### II(A).Material nonpublic information

Material, public, Mosaic

Social media, experts, research reports

## 6. II(B). Market manipulation

- ▣ Content
- ▣ Guidance



## 6. Standard II(B): Content

- **Content:** Members and Candidates must not engage in practices that distort prices or artificially inflate trading volume with the intent to mislead market participants.
- 1. Market manipulation includes:
  - **Info-based:** Dissemination of false or misleading information
    - ✓ Pump up prices by issuing misleading positive info, then dump.
  - **Transaction-based:** Members or candidates knew or should have known that transactions deceive or would be likely to mislead market participants by distorting the price-setting mechanism. It includes:
    - ✓ Artificially affect prices or volume to give misleading impression of price movement, which represent a diversion from the expectations of a fair and efficient market.
    - ✓ Securing a dominant position to exploit and manipulate the price of related derivative and the underlying asset.



## 6. Standard II(B): Guidance

### ● Guidance

2. The **intent** of the action is critical to determining whether it is a violation.
  - ✓ Not prohibit legitimate trading strategies that exploit a diff in market power, info, or other inefficiency.
  - ✓ Not prohibit trade for tax purposes, selling then buying back.
3. To increase liquidity, Futures Exchange made agreements with members to insure the minimum trading volume in exchange for reduction of commission. → If for the interest of clients and disclosed, **not violate**.

# Summary

## Guidance for Standards I–VII

### II(B).Market manipulation

Intent

Info-based, transaction-based

## Guidance for Standards I-VII

- Which of the following actions violate the Standard relating to market manipulation?
  - Action 1: Entering large buy and sell trades between multiple proprietary accounts of the firm with the intent to increase trading volume
  - Action 2: Securing a dominant position in a financial instrument with an intent to influence the price of a related derivative
  - Action 3: Exploiting perceived market inefficiencies through aggressive trading strategies
- A. Action 1 and Action 2 only
- B. Action 1 and Action 3 only
- C. Action 2 and Action 3 only

## Guidance for Standards I-VII

- Correct answer: A.
- Market Manipulation precludes transaction-based manipulation such as attempting to “buy and sell the stock using the accounts in hopes of raising the trading volume and the price.” So, Action 1 violates the Standard. Also, the Standard precludes other transaction-based manipulation such as “securing a controlling, dominant position in a financial instrument to exploit and manipulate the price of a related derivative and/or the underlying asset.” So, Action 2 also violates the Standard.

## Guidance for Standards I-VII

- Christy Pasley, CFA, is the Chief Investment Officer for Risen Investment Funds (RIF) a mutual fund organization. At a meeting between Homeland Builders (HB), a publicly traded company, Pasley learns HB sales are much slower than expected. In fact, HB sales declined more than 20% in the last quarter, but this information has not yet been widely disseminated. Immediately after meeting with HB, Pasley purchases put options on HB stock. Subsequently, HB issues a press release with their most recent sales figures. Has Pasley most likely violated the CFA Institute Standards of Professional Conduct?
  - A. Yes.
  - B. No, because the securities purchased were options.
  - C. No, because the information was obtained directly from the company.

## Guidance for Standards I-VII

- Correct Answer : A
  - As members and candidates who possess material nonpublic information that could affect the value of an investment must not act or cause others to act on the information. Even though the information is disclosed in a meeting with the mutual fund, this has not made the information public and it should not be used until it is more widely disseminated, a violation of Standard II(A). It does not matter that the securities purchased are options rather than stocks.

# 7. III(A). Loyalty, Prudence and Care

- ▣ Content
- ▣ Guidance

## 7. Standard III(A): Content

- **Content:**

1. Members and Candidates have a duty of loyalty to their clients and must act with reasonable care and exercise prudent judgment.
2. Must act for the benefit of their clients and place their clients' interests before their employer's or their own interests.



## 7. Standard III(A): Guidance

### ● Guidance

3. Exercise prudence, care, skill, and diligence.
4. Fiduciary (acting for the benefit of another party) requires higher duty to other business duty.
  - ✓ A fiduciary is someone who acts for the benefit of someone else. In a position of trust, fiduciaries owe undivided loyalty to their clients and must **place clients' interests before their own.**
  - ✓ Prudent man rule: A fiduciary must direct and operate the client's assets according to a higher standard of loyalty and extra care **than** the standard to which most people are held.
  - ✓ Any pooling of funds must be managed in strict accordance to the trust documents.

## 7. Standard III(A): Guidance

### ● Guidance

5. Prudence requires caution and discretion.
  - ✓ The exercise of **prudence by investment professionals** requires acting with care, skill, and diligence in the circumstances that a reasonable person acts in a like capacity and familiar with such matters would use.
  - ✓ In managing a client's portfolio, prudence requires following the investment parameters set by the client and balancing risk and return.
  - ✓ Acting with care requires a prudent and judicious manner in avoiding harm to clients.
6. Standard III(A), is **not a substitute** for legal or regulatory obligations. The duty required in fiduciary relationships exceeds what is acceptable in many other business relationships because a fiduciary is in an enhanced position of trust.

## 7. Standard III(A): Guidance

- **Understanding the Application of Loyalty, Prudence, and Care**

7. Standard III(A) does **not** render all members and candidates fiduciaries. However, Standard III(A) requires members and candidates to work in the client's best interest no matter what the job function.
  - ✓ The conduct may or may not rise to the level of being a fiduciary, depending on the type of client, **whether they are giving investment advice**, and the many facts and circumstances surrounding a particular transaction or **client relationship**.

## 7. Standard III(A): Guidance

### ● Guidance - Identifying the Actual Investment Client

8. Determine the identity of the "client" to whom the duty of loyalty is owed.

#### **4 types of clients:**

- ✓ **Individual:** In the context of an investment manager managing the personal assets of an individual, the client is the owner of the asset.
- ✓ **Beneficiary:** When the manager is responsible for the portfolios of pension plans or trusts, the client is the beneficiaries of the plan or trust. The duty of loyalty is owed to the ultimate beneficiaries.
- ✓ **Mandate:** Members and candidates managing a fund to an index or an expected mandate owe the duty of loyalty, prudence, and care to the stated mandate.
- ✓ **Investing public:** The client may be the investing public as a whole, the goals of independence and objectivity of research surpass the goal of loyalty to a single organization.

## 7. Standard III(A): Guidance

### ● Guidance - Identifying the Actual Investment Client (cont.)

9. Situations involving potential conflicts of interest with respect to responsibilities to clients may be extremely complex because they may involve a number of competing interests.
  - ✓ Not only put obligations to clients first in all dealings but also endeavor to avoid all real or potential conflicts of interest.
10. Even not have responsibilities of direct investment management, “clients” should also be considered.
  - ✓ Must look at roles and responsibilities when making a determination of who their clients are.
  - ✓ Easily identifiable client relationship: company executive and the firm’s public shareholders. At other times, the client may be the investing public as a whole, in which case the goals of independence and objectivity of research **surpass** the goal of loyalty to a single organization.

## 7. Standard III(A): Guidance

### ● Guidance - Developing the Client's Portfolio

11. The duty of loyalty, prudence, and care to client is especially important because the investment manager typically possesses greater knowledge in investment than the client does. This disparity places the individual client in a vulnerable position; the client must trust the manager.
- ✓ The manager in these situations should ensure that the client's objectives and expectations of the account are realistic and suitable to their circumstances and that the risks involved are appropriate.
  - ✓ In most circumstances, recommended investment strategies should relate to the long-term objectives and circumstances of the client.

## 7. Standard III(A): Guidance

- Guidance - Developing the Client's Portfolio (cont.)

12. Particular care must be taken to detect whether the goals of the investment manager or the firm in placing business, selling products, and executing security transactions potentially conflict with the best interests and objectives of the client.
13. Must **follow** any guidelines set by their clients for asset management.
14. Investment decisions must be judged in the context of the **total portfolio** rather than by individual investment within the portfolio.

## 7. Standard III(A): Guidance

### ● Guidance - Soft Commission Policies

15. An investment manager often has discretion over the selection of brokers executing transactions. Conflicts arise when an investment manager uses client brokerage to purchase research services → “soft dollars” or “soft commissions.”
16. Whenever using client brokerage to purchase goods or services that do not benefit the client, should disclose to clients the methods or policies followed in addressing the potential conflict.
  - ✓ A member or candidate who pays a higher commission than he or she would normally pay to purchase goods or services, without corresponding benefit to the very client, violates III (A).



## 7. Standard III(A): Guidance

### ● Guidance - Soft Commission Policies (cont.)

**17. Directed brokerage:** A client will direct a manager to use the brokerage to purchase goods or services for the client. Because brokerage commission is an asset of the client and is used to benefit that client, not the manager, such a practice does not violate any duty of loyalty.

- ✓ Obligated to seek **“best execution” and “best price”**, and assured that the goods or services purchased from the brokerage will benefit the account beneficiaries.
- ✓ “Best execution” refers to a trading process that seeks to maximize the value of the client’s portfolio within the client’s stated investment objectives and constraints.
- ✓ Should disclose to the client and obtain written consent that the client may not get best execution from the directed brokerage if he insists on trading through that broker.

## 7. Standard III(A): Guidance

### ● Guidance - Proxy Voting Policies

18. Voting proxies in an informed and responsible manner.

- ✓ Proxies have economic value to a client.
  - Must ensure properly safeguard and maximize this value.
- ✓ An investment manager who fails to vote, casts a vote without considering the impact of the question, or votes blindly with management on non-routine governance issues may violate III(A).
- ✓ **A cost-benefit analysis** may show that voting all proxies may not benefit the client, so voting proxies may not be necessary in all instances.
  - Members and candidates should disclose to clients their proxy voting policies.

# Summary

## **Guidance for Standards I–VII**

### **III(A).Loyalty, prudence and care**

Fiduciary duty, who's clients

Development of portfolio, soft dollar, proxy voting

## 8. III(B). Fair dealing

- ▣ Content
- ▣ Guidance



## 8. Standard III(B): Content

- **Content:**

1. Must deal fairly and objectively with all clients when:
  - ✓ Providing investment analysis
  - ✓ Making investment recommendations
  - ✓ Taking investment action
  - ✓ Engaging in other professional activities.

## 8. Standard III(B): Guidance

### ● Guidance

2. Fairly ≠ equally
  - ✓ Fairly: Not to discriminate against any clients when disseminating recommendations or taking investment action.
  - ✓ Equally: Not required to treat all clients exactly the same, e.g. reach all clients exactly the same time, by e-mail or telephone.
3. Report types: Initial detailed report, brief update report, by addition to or deletion from a recommended list, or simply by oral communication.
4. **Premium level service is okay**, if not disadvantage or negatively affect other clients. Such services should be disclosed to clients and available to everyone (should not be selective).
5. Trade: Equitable system, pro rata on order size, not on account size.

## 8. Standard III(B): Guidance

### ● Guidance - Investment Recommendations

6. The conduct involves members and candidates whose primary function is the preparation of investment recommendations to be disseminated either to the public or within a firm for the use of others in making investment decisions.
7. **The criterion:** The primary responsibility is the preparation of recommendations to be acted on by others, including those in the member's or candidate's organization.
8. An investment recommendation is any opinion in regard to purchasing, selling, or holding a given security or other investment.
  - ✓ Recommendation may be disseminated in different types. (refer to 3. report types)
  - ✓ A recommendation distributed to anyone outside the organization is considered a communication for general distribution.

## 8. Standard III(B): Guidance

### ● Guidance - Investment Recommendations

9. Ensure that information is disseminated in a manner that all clients have a **fair opportunity** to act **on every recommendation**.

- ✓ Should encourage their firms to design an equitable system to prevent selective or discriminatory disclosure
- ✓ Should inform clients about what kind of communications they will receive.

**10. Material changes** in prior recommendations should be communicated to all current clients; **particular care** should be taken that the information reaches those clients who have acted on or been affected by the earlier advice.

- ✓ Clients who do not know the changed recommendation and who place orders contrary to a current recommendation should be advised of the changed recommendation before the order is accepted.



## 8. Standard III(B): Guidance

### ● Guidance - Investment Action

11. Treat all clients fairly in light of investment objectives and circumstances.
12. When making investments in new offerings or in secondary financings, should distribute the issues to **all** customers who are suitable for the investment and consistent with the policies of **allocating** blocks of stock.
13. If the issue is oversubscribed, should be prorated to all subscribers.
  - ✓ Should be taken **on a round-lot basis to avoid odd-lot distributions**.
  - ✓ If the issue is oversubscribed, should forgo any sales to themselves or immediate families in order to free up additional shares for clients.

## 8. Standard III(B): Guidance

- **Guidance - Investment Action (Cont.)**

14. If the investment professional's **family-member accounts** are managed similarly to the accounts of other clients of the firm, these accounts should not be excluded from buying such shares.
15. Must make every effort to treat all individual and institutional clients in a fair and impartial manner.
- 16. Disclose** to clients and prospective clients the **documented allocation procedures** in place and how the procedures would affect them.
17. Should not take advantage of their position to the detriment of clients.

## — 8. Standard III(B): Recommended Procedures —

### ● Recommended Procedures

Develop and document trade allocation procedures: develop a guiding principles that ensure

- ✓ Fairness to advisory clients, both in priority of execution of orders and in the allocation of the price in execution of block orders or trades,
- ✓ Timeliness and efficiency in the execution of orders,
- ✓ Accuracy of the records as to trade orders and client account positions.

Disclose trade allocation procedures

- ✓ Trade allocation procedures must be fair and equitable.
- ✓ **Disclosure of inequitable allocation methods does not relieve the member or candidate of this obligation.**

## — 8. Standard III(B): Recommended Procedures —

### ● Recommended Procedures

Should develop or encourage their firm to develop written allocation procedures, with particular attention to procedures for block trades and new issues.

- ✓ Document orders and time stamped
- ✓ ***FIFO basis***
- ✓ Develop a policy to calculate execution prices and “partial fills” in a block trade for efficiency
- ✓ ***Same commission, same price***
- ✓ ***Pro rata on basis of order size***
- ✓ Obtain advance indications of interest, allocate securities by client (not portfolio manager), and provide a method for calculating allocations when allocating for new issues.

# Summary

## Guidance for Standards I–VII

### III(B).Fair dealing

Fair is not equal, same opportunity to trade

Fair allocation and its policy, family client is client first

## 9. III(C). Suitability

- ▣ Content
- ▣ Guidance



## 9. Standard III(C): Content

### ● Content

1. When in an advisory relationship with a client, must:
  - ✓ Make a reasonable inquiry into a client or prospective client's investment experience, risk and return objectives, and financial constraints prior to making any investment recommendation or taking investment action, must reassess and update regularly.
  - ✓ Determine that an investment is suitable to the client's financial situation and consistent with written objectives, mandates, and constraints before making an investment recommendation or taking investment action.
  - ✓ Judge the suitability in the context of the client's total portfolio.
2. When responsible for managing a portfolio to a specific mandate, strategy, or style, must only make investment recommendations or take investment actions that are consistent with the stated objectives and constraints of the portfolio.

## 9. Standard III(C): Guidance

### ● Guidance - Developing an Investment Policy

3. In an advisory relationship, must gather client information at the inception of the relationship.
  - ✓ Information includes the client's financial circumstances, personal data (such as age and occupation) that are relevant to investment decisions, attitudes toward risk, and objectives in investing.
  - ✓ Information should be **incorporated into a written investment policy statement (IPS)** that addresses the client's risk tolerance, return requirements, and all investment constraints

### ● Guidance - Understanding the Client's Risk Profile

4. One of the most important factors to be considered in matching appropriateness and suitability of an investment with a client's needs and circumstances is measuring that client's tolerance for risk.

### ● Guidance - Updating an Investment Policy

5. Updating the IPS should be repeated at least annually and also prior to material changes to any specific investment recommendations.



## 9. Standard III(C): Guidance

### ● Guidance - The Need for Diversification

6. An investment with high relative risk may be suitable in the context of the entire portfolio **or** when the client's stated objectives contemplate speculative or risky investments.
7. The manager may be responsible for only a portion of the client's total portfolio, or the client may not have provided a full financial picture.
  - ✓ Members and candidates can be responsible for assessing the suitability of an investment **only on the basis of** the information and criteria actually provided by the client.

### ● Guidance - Managing to an Index or Mandate

8. Responsibility is to invest in a manner consistent with the stated mandate.
9. Those who manage pooled assets to a specific mandate are not responsible for any individual investor.
  - ✓ Only those who have advisory relationship are responsible for individual clients.

## 9. Standard III(C): Guidance

### ● Addressing Unsolicited Trade Requests

10. Unsolicited trades request that a member or candidate knows are unsuitable for a client.
  - The member or candidate should refrain from making the trade until he or she discusses the concerns with the client.
    - ✓ Unsolicited request may be expected to have only a **minimum impact** on the entire portfolio because the size of the requested trade is small or the trade would result in a limited change to the portfolio's risk profile.
      - Necessary client approval for executing unsuitable trades.
      - At a minimum, the client should acknowledge the discussion and accept the conditions that make the recommendation unsuitable.
    - ✓ Unsolicited request expected to have a **material impact** on the portfolio, the member or candidate should use this opportunity to update the investment policy statement.
      - Some clients that decline to modify their policy statements while insisting an unsolicited trade be made.
        - Members or candidates will need to evaluate the effectiveness of their services to the client and ultimately determine whether they should continue the advisory arrangement with the client.
        - Some firms may allow for the trade to be executed in a new unmanaged account.

# Summary

## Guidance for Standards I–VII

### III(C).Suitability

Develop and update IPS, risk, diversification

Unsolicited trade, index or mandate

# 10. III(D). Performance presentation

- ▣ Content
- ▣ Guidance



## 10. Standard III(D): Content

- **Content:**

1. When communicating investment performance information, must make reasonable efforts to make sure that it is fair, accurate, and complete.

## 10. Standard III(D): Guidance

- **Guidance:**

2. The presentation should be **fair, accurate, complete**
3. Prohibit misrepresentations of past performance or reasonably expected performance
  - ✓ **Not state or imply to obtain what was achieved in the past**
4. Include terminated portfolio as part of performance history.
5. The performance of weighted rate of return rather than a single performance.
6. **If the presentation is brief,** must
  - ✓ Make available to clients and prospects, on request, the detailed information supporting that communication.
  - ✓ **Best practice:** brief presentations include a reference to the limited nature of the information provided.

## ● — Standard III(D): Recommended Procedures — ●

### ● Recommended Procedures

#### 7. Apply GIPS standards.

- ✓ For members and candidates who are showing the performance history of the assets they manage, compliance with the GIPS standards is the best method to meet their obligations under Standard III(D).
- ✓ Should encourage firms to comply with the GIPS standards.

## ● — Standard III(D): Recommended Procedures — ●

### ● Recommended Procedures

8. **Compliance without applying GIPS standards.** Can also meet obligations under Standard III(D) by:

- ✓ Considering the knowledge and sophistication of the audience to whom a performance presentation is addressed,
- ✓ Presenting the performance of the weighted composite of similar portfolios rather than using a single representative account,
- ✓ Including **terminated** accounts as part of performance history with a clear indication of when the accounts were terminated,
- ✓ Including disclosures that fully explain the performance results being reported.
  - ❑ Simulated performance using models?
  - ❑ Performance record from prior entity?
  - ❑ ***Is performance gross of fees (investment management fee), net of fees, or after tax?***
- ✓ Maintaining the data and records used to calculate the performance being presented.



# Summary

## Guidance for Standards I–VII

### III(D).Performance presentation

Past not guarantees future return

Brief with detailed on request

# **11. III(E). Preservation of confidentiality**

---

- ▣ Content
- ▣ Guidance



## 11. Standard III(E): Content

- **Content:**

1. 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 or prospective client permits disclosure of the information.

## 11. Standard III(E): Guidance

### ● Guidance

2. Require preservation of the confidentiality of information communicated by clients, prospective clients, and former clients<sup>4</sup>. III(E) is applicable when:
  - ✓ Receiving information because of special ability to conduct a portion of the client's business or personal affairs, and
  - ✓ Receiving information that arises from or is relevant to that portion of the client's business that is the subject of the special or confidential relationship.
3. If disclosure is required by law or the information concerns illegal activities by the client, may have an obligation to report the activities to the appropriate authorities.

### ● Guidance - Status of Client

4. Must continue to maintain the confidentiality of client records even after the client relationship has ended. ***If a client or former client expressly authorizes the disclosure***, may follow the terms of the authorization and provide the information.

## 11. Standard III(E): Guidance

### ● Guidance - Compliance with Laws

5. As a general matter, must comply with applicable law.

- ✓ If applicable law requires disclosure of client information in certain circumstances, members and candidates must comply with the law.
- ✓ ***If applicable law requires maintaining confidentiality***, even if the information concerns illegal activities on the part of the client, should not disclose.
- ✓ When in doubt, should consult with compliance personnel or legal counsel before disclosing confidential information about clients.

## 11. Standard III(E): Guidance

### ● Guidance - Electronic Information and Security

6. Many employers have **strict policies** about how to electronically communicate sensitive client information and store client information on personal laptops, mobile devices or portable disk/flash drives.
7. Standard III(E) does not require members or candidates to become experts in information security technology, but they should have a **thorough understanding of the policies of their employers**. The size and operations of the firm will lead to differing policies for ensuring the security of confidential information maintained within the firm.
8. Members and candidates should encourage their firm to conduct **regular periodic training on confidentiality procedures** for all firm personnel, including portfolio associates, receptionists, and other non-investment staff who have routine direct contact with clients and their records.

## 11. Standard III(E): Guidance

### ● Guidance - Professional Conduct Investigations by CFA Institute

9. Requirements of III(E) are not intended to prevent from cooperating with an investigation by the CFA Institute Professional Conduct Program (PCP).
10. When **permissible** under applicable law, 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.
  - ✓ Encouraged to cooperate with investigations into the conduct of others.
  - ✓ Any information turned over to the PCP is kept in the strictest confidence.
  - ✓ Will not be considered in violation of this standard by forwarding confidential information to the PCP.

## ● — Standard III(E): Recommended Procedures — ●

### ● Recommended Procedures

11. The simplest, most conservative and effective way to comply with III(E) is to avoid disclosing any information received from a client **except to authorized fellow employees who are also working for the client.**
12. In some instances, may want to disclose information from clients that is outside the scope of the confidential relationship and does not involve illegal activities. Before making such a disclosure, should ask the following:
  - ✓ In what context was the information disclosed? If disclosed, is the information relevant to the work?
  - ✓ Is the information background material that, if disclosed, will enable better service to the client?
13. Communication with clients: Members and candidates should be diligent in discussing with clients the appropriate methods for providing confidential information. It is important to convey to clients that not all firm-sponsored resources may be appropriate for such communications.



# Summary

## Guidance for Standards I–VII

### III(E).Preservation of confidentiality

To all former, current, prospective clients

## Guidance for Standards I-VII

- Bronson provides investment advice to the board of trustees of a private university endowment fund. The trustees have provided Bronson with the fund's financial information, including planned expenditures. Bronson receives a phone call on Friday afternoon from Murdock, a prominent alumnus, requesting that Bronson fax him comprehensive financial information about the fund. According to Murdock, he has a potential contributor but needs the information that day to close the deal and cannot contact any of the trustees. Based on the CFA Institute Standards, Bronson should:
  - A. Send Murdock the information because disclosure would benefit the client.
  - B. Not send Murdock the information to preserve confidentiality.
  - C. Send Murdock the information, provided Bronson promptly notifies the trustees.

## Guidance for Standards I-VII

- Correct Answer: B
  - This question relates to Standard III(A)–Loyalty, Prudence, and Care and Standard III(E)–Preservation of Confidentiality. In this case, the member manages funds of a private endowment. Clients, who are, in this case, the trustees of the fund, must place some trust in members and candidates. Bronson cannot disclose confidential financial information to anyone without the permission of the fund, regardless of whether the disclosure may benefit the fund.

## Guidance for Standards I-VII

- Jorge Lopez, CFA, is responsible for proxy voting on behalf of his bank's asset management clients. Lopez recently performed a cost–benefit analysis that showed the proxy-voting policies might not benefit the bank's clients. As a result, Lopez immediately changes the proxy-voting policies and procedures without informing anyone. Lopez now votes client proxies on the side of management on all issues, with the exception of major mergers in which a significant impact on the stock price is expected. Lopez least likely violated the CFA Institute Standards of Professional Conduct in regard to:
  - A. cost-benefit analysis.
  - B. voting with management.
  - C. proxy-voting policy disclosures.

## Guidance for Standards I-VII

- Correct Answer: A
  - Performing a cost–benefit analysis showing that voting all proxies might not benefit the client and concluding that voting proxies may not be necessary in all instances is not a violation of Standard III(A): Loyalty, Prudence, and Care. However, even though voting proxies may not be necessary in all instances, part of a member's or candidate's duty of loyalty under Standard III(A) includes voting proxies in an informed and responsible manner, which is not being done when Lopez automatically votes with management on the majority of issues. In addition, members and candidates should disclose to clients their proxy-voting policies, including any changes to that policy, as required by Standard III(A), which has not been done.

## Guidance for Standards I-VII

- Bradley Ames, a well-known and respected analyst, follows the high-tech industry. In the course of his research, he found that a small, relatively unknown company whose shares are traded over the counter has just signed significant contracts with some company he follows. After considerable amount of investigation, he wrote a research report on the small company and recommend purchase of its shares. He sent his report to all clients through email and then made some telephone calls with VIPs. According to the CFA Institute Code of Ethics and Standards of Professional Conduct, Bradley most likely violate:
  - A. Fair Dealing.
  - B. Priority of transaction.
  - C. None.

## Guidance for Standards I-VII

- Correct Answer : C
  - Based on Standard III(B) Fair Dealing, members and candidates may provide more personal, specialized, or in-depth service to clients who are willing to pay for premium services through higher management fees or higher levels of brokerage. In this case, Bradley fairly deals with the information to his clients.

## 12. IV(A). Loyalty

- ▣ Content
- ▣ Guidance





## 12. Standard IV(A): Content

- **Content:**

1. In matters related to their employment, must act for the benefit of employer and not deprive employer of the advantage of their skills and abilities, divulge confidential information, or otherwise cause harm to their employer.

## 12. Standard IV(A): Guidance

- **Guidance**

2. **Core rule:** Protect the interests of their firms by refraining from any conduct that would injure the firm, deprive it of profit, or deprive it of the member's or candidate's skills and ability.

- **Guidance - Employer Responsibilities**

3. **Encouraged** to provide employer with a copy of the Code and Standards. These materials will inform the employer of the responsibilities of a CFA Institute member or candidate in the CFA Program. The Code and Standards also serve as a basis for questioning employer policies and practices that conflict with these responsibilities.
4. Employers are **not obligated** to adhere to the Code and Standards. Senior management has the additional responsibility to devise compensation structures and incentive arrangements that do not encourage unethical behavior.

## 12. Standard IV(A): Guidance

### ● Guidance - Independent Practice

5. "Undertaking independent practice" means engaging in **competitive business**, as opposed to making preparations to begin such practice.
6. Should abstain from independent competitive activity that could conflict with the interests of their employer.
  - ✓ Although IV(A) does not preclude from entering into an independent business while still employed, those who planning to engage in such practice for compensation must **notify their employer and describe:**
    - ❑ Types of services they will render to prospective independent clients,
    - ❑ The expected duration of the services,
    - ❑ The compensation for the services.
7. Should not render services **until** they **receive consent** from their employer to all of the terms of the arrangement.

## 12. Standard IV(A): Guidance

### ● Guidance - Leaving an Employer

8. **Before leaving**, the following will cause a violation:

- ✓ Misappropriation of trade secrets.
- ✓ Misappropriation of client lists. Memorizing client lists (name and address) is not permitted unless the information does not come from the records of former employer or violate non-compete agreement.
- ✓ Misuse of confidential information.
- ✓ Soliciting employer's clients prior to cessation of employment.
- ✓ Self-dealing. (appropriating for one's own property a business opportunity or information belonging to one's employer)

9. **After leaving**, the following will cause a violation:

- ✓ Violation of terms in existing non-compete contract.
- ✓ Taking records or files (even rejected idea list) to a new employer without the written permission of the previous employer.

## 12. Standard IV(A): Guidance

### ● Guidance - Leaving an Employer (cont.)

10. Once notice is provided to the employer of the intent to resign, must follow the policies and procedures to **notify** clients of planned departure.
11. Once an employee has left the firm, the **skills and experience** that an employee obtained while employed are not “confidential” or “privileged” information.
  - ✓ IV(A) does not prohibit experience or knowledge gained at one employer from being used at another employer.
12. **Simple knowledge of names and existence of clients** is not confidential information unless deemed such by an agreement or by law.
13. Firm records or work performed on behalf of the firm that is stored in paper copy or electronically while employed should be **erased or returned** to the employer unless the firm gives permission to keep those records after employment ends.

## 12. Standard IV(A): Guidance

### ● Guidance - Leaving an Employer (cont.)

14. In some markets, there are agreements between employers within an industry that outline information that departing employees are permitted to take upon resignation, such as the “Protocol for Broker Recruiting” in the United States.

- ✓ Individuals are allowed to take some general client contact information when departing.
  - ❑ To be protected, a copy of the information the individual is taking must be provided to the local management team for review.
  - ❑ Additionally, the specific client information may only be used by the departing employee and not others employed by the new firm.

## 12. Standard IV(A): Guidance

### ● Guidance – Use of Social Media

15. Communications through social media platforms that potentially reach current clients should adhere to the employer's policies and procedures regarding notification of departing employees.
16. Specific accounts and user profiles of members and candidates may be created for solely professional reasons, including firm approved accounts for client engagements. Such **business related accounts** would be considered **part of the firm's assets**, thus requiring members and candidates to transfer or delete the accounts as directed by their firm's policies and procedures.
- ✓ **Best practice** for members and candidates is to **maintain separate accounts** for their personal and professional social media activities.
  - ✓ Members and candidates should **discuss** with their employers how profiles should be treated when a single account includes personal connections and also is used to conduct aspects of their professional activities.

## 12. Standard IV(A): Guidance

### ● Guidance - Whistleblowing

17. Personal interests, and interests of employer, are secondary to protecting the integrity of capital markets and the interests of clients.
18. When an employer is engaged in illegal or unethical activities, actions taken by the employee that would normally violate loyalty to employer (e.g. violating certain policies, contradicting employer instructions, or preserving a record by copying employer records) may be justified. Such action would be permitted only if the **intent** is clearly aimed at protecting clients or the integrity of the market, not for personal gain.

### ● Guidance - Nature of Employment

19. The applicability is based on the nature of the employment-employee versus **independent contractor**. Duties within an independent contractor relationship are governed by the oral or written agreement between the member and the client.



# Summary

## Guidance for Standards I–VII

### IV(A).Loyalty

Independent practice when on job, leaving and social media

whistleblowing

Independent contract

# 13. IV(B).

## Additional compensation arrangements

---

- ▣ Content
- ▣ Guidance



## 13. Standard IV(B): Content

- **Content:**

1. Members and candidates must not accept gifts, benefits, compensation, or consideration that competes with, or might reasonably be expected to create a conflict of interest with their employer's interest unless they obtain written consent from all parties involved.

## 13. Standard IV(B): Guidance

### ● Guidance

2. No gifts, benefits, compensation or consideration are to be accepted which may create a conflict of interest with the employer's interest unless **written consent** is received from **all parties**.
3. "Written Consent" includes any form of communication that can be documented (for example, communication via computer e-mail that can be retrieved and documented).
4. Must obtain permission for additional compensation/benefits because such arrangements may affect loyalty and objectivity and create potential conflicts of interest.
5. There may be instances in which a member or candidate is hired by an employer on a "part-time" basis.
  - ✓ Members and candidates should discuss possible limitations to their abilities to provide services that may be competitive with their employer during the negotiation and hiring process.

# Summary

## **Guidance for Standards I–VII**

### **IV(B).Additional compensation arrangement**

Written consent from employer

# 14. IV(C). Responsibility of supervisors

- ▣ Content
- ▣ Guidance



## 14. Standard IV(C): Content

- **Content:**

1. Members and Candidates must make reasonable efforts to ensure that anyone subject to their supervision or authority complies with applicable laws, rules, regulations and the Code and Standards.

## 14. Standard IV(C): Guidance

- **Guidance**

2. Can delegate, but **not relieve** of supervisory responsibility.
  - ✓ Should instruct about methods to prevent and detect violations of laws, rules, regulations, firm policies, and the Code and Standards.

- **Guidance - Detection Procedures**

3. Exercise reasonable supervision by establishing and implementing written compliance system and ensuring periodic review on the system.



## 14. Standard IV(C): Guidance

### ● Guidance

4. At a minimum, Standard IV(C) requires that members and candidates with supervisory responsibility make reasonable efforts to prevent and detect violations by ensuring the establishment of **effective compliance systems**.
  - ✓ A code of ethics,
  - ✓ Compliance policies and procedures,
  - ✓ Reviewing employee actions to determine whether they are following the rules
  - ✓ Education and training programs,
  - ✓ An incentive structure that rewards ethical conduct, and
  - ✓ Adoption of firm-wide best practice standards (e.g. the GIPS Standards, CFA Institute Asset Manager Code of Professional Conduct).

## 14. Standard IV(C): Guidance

### ● Guidance – Supervision includes detection

5. Exercise reasonable supervision by establishing and implementing written compliance procedures and ensuring that those procedures are followed through periodic review.
6. If a member or candidate has adopted reasonable procedures and taken steps to institute an effective compliance program, then the member or candidate may **not** be in violation of Standard IV(C) if he or she does **not** detect violations that occur despite these efforts.

### ● Guidance - Inadequate Procedures

7. Those who have supervisory responsibility should bring an **inadequate compliance system** to the attention of the firm's senior managers and **recommend corrective action**.
8. If the member or candidate clearly cannot discharge supervisory responsibilities **because of the absence** of a compliance system or because of an **inadequate** compliance system, the member or candidate should **decline in writing** to accept supervisory responsibility until the firm adopts reasonable procedures to allow adequate exercise of supervisory responsibility.

## 14. Standard IV(C): Guidance

### ● Guidance – System for supervision

9. Should know what an **adequate system** is, and make reasonable efforts to see that appropriate procedures are **established, documented, communicated** to covered personnel, and **followed**.
  - ✓ Once such procedures are in place, supervisor must make reasonable efforts to ensure that the procedures are monitored and enforced.
10. **Once knowing a potential violation, supervisor must promptly initiate an investigation to ascertain the extent of the wrongdoing**.
  - ✓ Relying on employee's statements or assurances that the wrongdoing will not recur is **not enough**.
  - ✓ Reporting the misconduct up the chain of command and warning the employee to cease the activity are also **not enough**.
  - ✓ Should take steps to ensure that the violation will not be repeated, by **placing limits** on the employee's activities or **increasing the monitoring** of the employee's activities.

# Summary

## Guidance for Standards I–VII

### IV(C).Responsibility of supervisors

System of supervision

Respond to violation promptly

## Guidance for Standards I-VII

- According to the Standard relating to additional compensation arrangements, a member must not accept a benefit offered by a third party that might create a conflict of interest with his employer's interest unless he obtains written consent:
  - A. only from his employer.
  - B. only from the third party offering the benefit.
  - C. both from his employer and from the third party offering the benefit.
- Correct Answer: C.
  - According to Standard IV (B), Additional Compensation Arrangements, "Members and Candidates must not accept gifts, benefits, compensation, or consideration that competes with or might reasonably be expected to create a conflict of interest with their employer's interest unless they obtain written consent from all parties involved." Therefore, the member is required to obtain consent from the employer and from the third party.

## Guidance for Standards I-VII

- Madeline Smith, CFA, was recently promoted to senior portfolio manager. In her new position, Smith is required to supervise three portfolio managers. Smith asks for a copy of her firm's written supervisory policies and procedures but is advised that no such policies are required by regulatory standards in the country where Smith works. According to the Standards of Practice Handbook, Smith's most appropriate course of action would be to:
  - A. require her firm to adopt the CFA Institute Code of Ethics and Standards of Professional Conduct.
  - B. decline to accept supervisory responsibility until her firm adopts procedures to allow her to adequately exercise such responsibility.
  - C. require the employees she supervises to adopt the CFA Institute Code of Ethics and Standards of Professional Conduct.

## Guidance for Standards I-VII

- Correct Answer : B
  - According to guidance for Standard (IV(C), if a member cannot fulfill supervisory responsibilities because of the absence of a compliance system or because of an inadequate compliance system, the member should decline in writing to accept supervisory responsibility until the firm adopts reasonable procedures to allow the member to adequately exercise such responsibility.

# Example

## Guidance for Standards I-VII

- David works as a portfolio manager for 10 years, and he is planning to leave his current company and to start his own business. Before his leaving, he informs his current clients that he is going to leave the company and open up a new firm running similar business without his employer's permission. In addition, David handles some registration affairs for his new firm after his work. David would most likely violate:
  - A. informing his current clients of his resignation.
  - B. dealing with registration things for his new firm before leaving.
  - C. both A and B.
- Correct Answer : A
  - David is allowed to deal with registration affairs of his firm as long as it does not breach duty to employers. However, notifying clients of his departure without employer's permission is not permitted and would be considered a soliciting behavior.



# 15. V(A).

## Diligence and reasonable basis

---

- ▣ Content
- ▣ Guidance



## 15. Standard V(A): Content

- **Content:**

- Members and Candidates must:

1. Exercise diligence, independence, and thoroughness in analyzing investments, making investment recommendations, and taking investment actions.
2. Have a reasonable and adequate basis, supported by appropriate research and investigation, for any investment analysis, recommendation, or action.

## 15. Standard V(A): Guidance

- **Guidance**

3. The requirements for research conclusions vary in relation to the role in investment decision-making process, but must make reasonable efforts to cover all pertinent issues when arriving at a recommendation.
4. Provide supporting information to clients → enhance transparency.

## 15. Standard V(A): Guidance

### ● Guidance - Defining Diligence and Reasonable Basis

5. In providing investment service, often use a variety of resources (company reports, third-party research, and results from quantitative models).
6. Some attributes to consider:
  - ✓ Global, regional, and country macroeconomic conditions
  - ✓ Current stage of the industry's business cycle,
  - ✓ Company's operating and financial history,
  - ✓ Mutual fund's fee structure and management history,
  - ✓ Output and potential limitations of quantitative models,
  - ✓ Quality of the assets included in a securitization,
  - ✓ Appropriateness of selected peer-group comparisons.
7. Can base decisions only on the information available at the time the decision is made. The steps taken in developing a diligent and reasonable recommendation should minimize unexpected downside events.

## 15. Standard V(A): Guidance

### ● Guidance - Using Secondary or Third-Party Research

8. **Criteria** in forming an opinion on whether research is sound include:

- ✓ Assumptions used,
- ✓ Rigor of the analysis performed,
- ✓ Date/timeliness of the research, and
- ✓ Evaluation of objectivity and independence of recommendations

○ If rely on secondary or third-party research, must make reasonable and diligent efforts to determine whether it is sound. If suspect the soundness, must not rely on that information.

- ✓ **Secondary** research is defined as research conducted by someone else in the member's or candidate's firm.
- ✓ **Third-party** research is research conducted by entities outside the member's or candidate's firm, such as a brokerage firm, bank, or research firm.

○ May rely on others in the firm to determine soundness and use the information in good faith assuming the due diligence process was deemed adequate.

## 15. Standard V(A): Guidance

### ● Guidance - Using Secondary or Third-Party Research (cont.)

- The sources of the information and data will influence the level of the review a member or candidate must undertake.
  - ✓ Information and data taken from internet sources, such as personal blogs, independent research aggregation websites, or social media websites, likely require a **greater** level of review than information from more established research organizations.
- Should verify that the firm has a policy about the **timely and consistent review** of approved research providers to ensure the quality of the research.
- If such a policy is not in place at the firm, the member or candidate should encourage the development and adoption of a formal review practice.

## 15. Standard V(A): Guidance

- **Guidance – Using Quantitatively Oriented Research**

9. Need to have an understanding of the **parameters** used in the model or quantitative research.
10. Although not required to be experts in technical aspects of the models , must understand the **assumptions and limitations** inherent in any model and **how the results were used** in the decision-making process.

## 15. Standard V(A): Guidance

### ● Guidance – Developing Quantitatively Oriented Research

11. Individuals who create new quantitative models and services must exhibit a higher level of diligence in reviewing new products than the individuals who ultimately use the analytical output.
  - ✓ Members and candidates involved in the development and oversight of quantitatively oriented models, methods, and algorithms must **understand the technical aspects** of the products they provide to clients.
  - ✓ A thorough testing of the model and resulting analysis should be completed prior to product distribution.
12. Need to consider the **time horizon** of data input in financial models.
13. In development of a recommendation, may need to test the models by using volatility and performance expectations that represent scenarios **outside the observable databases**.
14. In reviewing computer models or the resulting output, pay attention to the assumptions and rigor of the analysis to ensure that the model incorporates **negative market events**.



## 15. Standard V(A): Guidance

### ● Guidance - Selecting External Advisers and Subadvisers

15. Why adopt external advisers and subadvisers?

- ✓ The progression of financial instruments and allocation techniques leads to the use of **specialized managers** to invest in specific asset classes that **complement** the firm's in-house expertise.

16. Need to ensure that the firm has standardized criteria for reviewing external advisers. Such **criteria** would include, but would not be limited to, the following:

- ✓ Reviewing the adviser's **established code of ethics**
- ✓ Understanding the adviser's **compliance and internal control procedures**
- ✓ Assessing the **quality** of the published return information
- ✓ Reviewing the adviser's **adherence to its stated strategy**

## 15. Standard V(A): Guidance

### ● Guidance - Group Research and Decision Making

17. The conclusions or recommendations of the group report represent the consensus of the group, but may not necessarily be the views of the member or candidate, even though his name is included on the report.
18. If not reflect his or her conclusion, must dissociate from the **group research**?
  - ✓ If the consensus opinion has a reasonable and adequate basis and is independent and objective, need not decline to be identified with the report, even if it does not reflect his opinion.
19. Always recommend "hot" issue indicates **NO** reasonable basis.

# Summary

## Guidance for Standards I–VII

### **V(A).Diligence and reasonable basis**

Define, Others' report, quants oriented research and techniques  
select subadvisers, group research

# 16. V(B).

## Communication with clients

---

- ▣ Content
- ▣ Guidance



## 16. Standard V(B): Content

### ● Content

#### Members and Candidates must:

1. Disclose to clients and prospective clients the basic format and general principles of the investment processes used to analyze investments, select securities, and construct portfolios and must promptly disclose any changes that might **materially affect** those processes.
2. Disclose to clients and prospective clients significant **limitations and risks** associated with the investment process.
3. Use **reasonable judgment** in identifying which factors are important to their investment analyses, recommendations, or actions and include those factors in communications with clients and prospective clients.
4. **Distinguish** between **fact and opinion** in the presentation of investment analysis and recommendations.
  - ✓ "...will be..." → fact
  - ✓ "...may be ..." → opinion

## 16. Standard V(B): Guidance

### ● Guidance - Informing Clients of the Investment Process

5. Keep clients informed on an ongoing basis about changes to the investment process.
6. Understanding the **basic characteristics** of an investment is important in judging suitability on a stand-alone basis, it's **especially important** in determining the **impact** each investment will have on the **characteristics of a portfolio**.
7. Should **inform** clients about the specialization or diversification expertise of external advisers.

### ● Guidance - Different Forms of Communication

8. All means of communications are included here, not just research reports, so in person, over the call, or by the computer are okay.
  - ✓ When providing information to clients through **new technologies**, members and candidates should take reasonable steps to ensure that such delivery would **treat all clients fairly**.
9. If recommendations are **in capsule form** (such as a recommended stock list), should notify clients that additional information and analyses are available upon request.

## 16. Standard V(B): Guidance

### ● Guidance - Identifying Risk and Limitations of Analysis

10. Members and candidates must outline to clients and prospective clients **significant risks and limitations** of the analysis contained in their investment products or recommendations.
- ✓ The type and nature of significant risks will depend on the investment process that members and candidates are following and on the personal circumstances of the client

#### 11. Guidance - Risks

- ✓ In general, the use of leverage constitutes a significant risk and should be disclosed.
- ✓ Adequately disclose the general market-related risks.
- ✓ Risks associated with the use of complex financial instruments that are deemed significant.
- ✓ Other types of risks that members and candidates may consider disclosing include, but are not limited to, counterparty risk, country risk, sector or industry risk, security-specific risk, and credit risk.

## 16. Standard V(B): Guidance

12. Investment securities and vehicles may have **limiting factors** that influence a client's or potential client's investment decision.
- ✓ 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.
13. Members and candidates have to disclose significant risks known to them at the time of the disclosure.
14. Members and candidates cannot be expected to disclose risks they are **unaware** of at the time recommendations or investment actions are made.
- ✓ A **one-time investment loss** that occurs after the disclosure does not constitute a pertinent factor in assessing whether significant risks and limitations were properly disclosed.
  - ✓ Having no knowledge of a risk or limitation that subsequently triggers a loss may reveal a deficiency in the V(A)-Diligence and Reasonable Basis of the research of the member or candidate, but may **not reveal** a breach of Standard V(B).



## 16. Standard V(B): Guidance

### ● Guidance - Report Presentation

15. The member or candidate who prepares the report must include those elements that are important to the analysis and conclusions of the report so that the reader can follow and challenge the report's reasoning.
16. A report writer who has done adequate investigation may emphasize certain areas, touch briefly on others, and omit certain aspects deemed unimportant. As long as the analyst clearly stipulates the **limits** to the **scope** of the report.
17. Investment advice based on **quantitative** research and analysis must be supported by readily available reference material and should be applied in a manner **consistent** with previously applied methodology.
  - ✓ If **changes** in methodology are made, they should be **highlighted**.

## 16. Standard V(B): Guidance

18. Separate opinions from facts:

- ✓ If not indicate that earnings estimates, changes in the dividend outlook, and future market price information are **opinions** subject to future circumstances, thus fail to separate past from future and **violate** V(B).
- ✓ In the case of complex quantitative analyses, analysts **must clearly separate** fact from statistical conjecture and should identify the known limitations of an analysis.
- ✓ Should explicitly discuss with clients and prospective clients the assumptions used in the investment models and processes to generate the analysis.
- ✓ Caution should be used in promoting the accuracy of any model or process to clients because the ultimate output is merely an estimate of future results and not a certainty.

# Summary

## Guidance for Standards I–VII

### V(B).Communication with clients

Different forms of communications, report presentation

Investment process, risk and limitations

Facts and opinions

# 17. V(C). Record retention

- ▣ Content
- ▣ Guidance



## 17. Standard V(C): Content

- **Content:**

1. Members and Candidates must develop and maintain appropriate records to support their investment analysis, recommendations, actions, and other investment-related communications with clients and prospective clients.

## 17. Standard V(C): Guidance

- **Guidance**

2. Records may be maintained either in hard copy or electronic form.

- **Guidance - Records Are Property of the Firm**

3. Records created in professional activities are the property of the firm. When leaving the firm, cannot take those records, including originals or copies of supporting records of his work, to the new employer without the express consent of the previous employer.
4. Cannot use historical recommendations or research reports created at the previous firm because the supporting documentation is unavailable.
5. For future use, must re-create the supporting records at the new firm through **public** sources, or directly from **covered company**, and not from memory or sources through previous employer unless with permission.

## 17. Standard V(C): Guidance

### ● Guidance - New Media Records

6. Members and candidates should understand that employers and local regulators are developing digital media retention policies, but these policies may lag behind the advent of new communication channels.
  - ✓ Such lag places greater responsibility on the individual for ensuring that all relevant information is retained.

### ● Guidance - Local Requirements

7. Fulfilling local regulatory requirements also may satisfy the requirements of Standard V(C), but should explicitly determine whether it does.
8. **If no regulatory guidance in place, CFA Institute recommends maintaining records for at least 7 years.** If there is a legal requirement for retention period, follow the legal requirement.
  - ✓ If legal requirement regarding record maintenance is 5 years, how long should we keep records?

# Summary

## Guidance for Standards I–VII

### V(C).Record retention

Property of firm

local requirement and at least 7 years



# Example

## Guidance for Standards I-VII

- Steve Garcia, a research analyst, works for an investment firm in US. After reading some research reports, he used the opinions of other analysts and wrote "The sales of Ocean Company will increase 50% next year." Which of the following does Steve violate according to the CFA Code and Standards?
  - A. Diligence and reasonable basis
  - B. Communication with clients
  - C. Diligence and reasonable basis& Communication with clients
- Correct Answer: C
  - Steve must make a thorough analysis when writing research reports. He just used the opinions from other analysts, so he violates "diligence and reasonable basis." In his report, the word "will" indicate that he is sure that the increase will happen which actually is not a certain thing. According to the standards, members and candidates should separate opinion from fact.

## Guidance for Standards I-VII

- Noor Hussein, CFA, runs a financial advisory business, specializing in retirement planning and investments. One of her clients asks her to advise the firm's pension fund trustees on available investments in the market including Islamic products. On the day prior to the meeting, Hussein spends an hour familiarizing herself with Islamic investment products and getting updates on local market conditions. The next day, she recommends Islamic investment products to the trustees based on her research and her expertise in retirement planning and investments. The trustees subsequently incorporate Islamic products into their investment allocation. Did Hussein's basis for the recommendation most likely comply with the CFA Code of Ethics?
  - A. Yes.
  - B. No, with regard to Misconduct.
  - C. No, with regard to Diligence and Reasonable Basis.

## Guidance for Standards I-VII

- Correct Answer : C
  - Hussein did not likely act with competence and diligence as required by Standard V(A). One half day of preparation with regard to Islamic investment products would not likely be considered sufficient to give investment advice to pension plan trustees. Misconduct was not violated by Hussein stating she is an expert in retirement planning and investments because this is the area she specializes in.

# Example

## Guidance for Standards I-VII

- Guillermo Sandoval, CFA, owns an asset management firm with offices downtown. To minimize rent expenses, each year Sandoval ships the previous year's research records to a nearby warehouse. There, the reports are digitized and stored in both electronic and hard-copy forms. After five years, all paper copies are destroyed and only electronic copies are retained. Are Sandoval's record-retention procedures in compliance with the CFA Institute Standards of Practice?
  - A. Yes.
  - B. No, because he did not retain the copies in his offices.
  - C. No, because he failed to retain the original documents.
- Correct Answer : A .
  - The Standards do not require on-site storage.

# 18. VI(A). Disclosure of conflicts

- ▣ Content
- ▣ Guidance



## 18. Standard VI(A): Content

- **Content:**

1. Members and Candidates must make full and fair disclosure of all matters that could reasonably be expected to impair their independence and objectivity or interfere with respective duties to their clients, prospective clients, and their employer.
2. Must ensure that such disclosures are prominent, are delivered in plain language, and communicate the relevant information effectively.

## 18. Standard VI(A): Guidance

### ● Guidance

3. Try our best to avoid any potential and actual conflict of interest **when possible**.
4. Disclosures must be prominent and must be made in plain language.
  - ✓ Best practice: update disclosures when the nature of a conflict of interest changes materially.
5. If an analyst was asked to cover the company, when **inherit** the shares of the company in subject.
  - ✓ Must disclose if continue to follow.
  - ✓ Best practice: assign another analyst to follow up the company.

## 18. Standard VI(A): Guidance

### ● Guidance

#### 6. Disclosure to **Employers**

- ✓ Conflict of interest may create problems.
  - ❑ Restrict personal trading, outside board membership, and related activities to prevent situations that could give the appearance of a conflict of interest.
  - ❑ If find conflicts, must report and resolve as quickly and effectively as possible.
- ✓ The same circumstances that generate conflicts to be reported to clients and prospective clients also would dictate reporting to employers, such as ownership of stocks analyzed or recommended.

#### 7. Disclosure to **Clients**:

- ✓ Disclose:
  - ❑ Corporate financing or market making relationship;
  - ❑ Security holding
  - ❑ Directorship
  - ❑ Individual relationship
- ✓ Should also disclose fee arrangements, sub-advisory arrangements or situations involving non-standard fee structures. Equally important is to disclose arrangements in which the firm benefits directly from recommendations.



## 18. Standard VI(A): Guidance

### ● Guidance

#### 8. Cross-Departmental Conflicts

- ✓ Broker-sponsored limited partnerships to invest **venture capital**.
  - ▣ Conflicts exist because not only to follow issues after IPO, but also to promote in the secondary market.

#### 9. Conflicts with Stock Ownership

- ✓ **May** prohibit from owning any such securities → overly burdensome.
- ✓ Sell-side disclose ownership in stock recommended, buy-side disclose procedures for reporting requirements for personal transactions.

#### 10. Conflicts as a Director

- ✓ Duties owed to clients and to shareholders of the company
- ✓ Investment personnel as a director receive the securities or options
- ✓ Board service receiving MNI

# Summary

## Guidance for Standards I–VII

### VI(A).Disclosure of conflicts

To employers, to clients

Conflict of Cross-department, ownership of stock, as director

# 19. VI(B). Priority of transactions

- ▣ Content
- ▣ Guidance



## 19. Standard VI(B): Content

- **Content:**

1. Investment transactions for clients and employers must have priority over investment transactions in which a Member or Candidate is the beneficial owner, which means transactions that ultimately benefit Member or Candidate.

## 19. Standard VI(B): Guidance

- **Guidance**

2. Client > employer > individual
  - ✓ Individual - beneficial owner.
3. After 7 minutes, buy, it's a violation. Must have enough time to let clients have opportunities to respond to your recommendation.

- **Guidance - Avoiding Potential Conflicts**

4. Conflicts between the client's interest and an investment professional's personal interest may occur.
5. Although conflicts of interest exist, it's OK for individual managers, advisers, or fund employees making money from personal investments as long as
  - ✓ The client is not disadvantaged by the trade,
  - ✓ The investment professional does not benefit personally from trades undertaken for clients,
  - ✓ Comply with applicable regulatory requirements

**For example**, trading contrary to recommendation due to payment of college tuition, down payment of house, or margin call, etc.

- **Guidance - Personal Trading Secondary to Trading for Clients**

6. Clients and employers have priority over trades in which a member or candidate is the beneficiary owner.
7. Some clients in certain investment situations require investment personnel to have **aligned interests**. But mustn't adversely affect client investment.

## 19. Standard VI(B): Guidance

- **Guidance - Standards for Nonpublic Information**

8. Prohibit from conveying nonpublic information to any person whose relationship to the member or candidate makes him a beneficial owner of the person's securities. Must not convey this information to any other person if the nonpublic information can be deemed material.

- **Guidance - Impact on All Accounts with Beneficial Ownership**

9. Personal transactions include those for own account, for family (including immediate family members) accounts, and for accounts of direct or indirect pecuniary interest, such as a trust or retirement account.

**10. Family accounts** that are client accounts should be treated like any other firm account, should not be disadvantaged because of that relationship.

✓ Disadvantage parents who are **normal fee-paying clients**: violate III (B) fair dealing

11. If have **beneficial ownership** in the account, may be subject to preclearance or reporting requirements of the employer or applicable law.

# Summary

## Guidance for Standards I–VII

### VI(B).Priority of transactions

Not self-benefit firstly

Clients>employer>personal

Family client is client.

## 20. VI(C). Referral fees

- ▣ Content
- ▣ Guidance





## ●—— 20. Standard VI(C): Content & Guidance ——●

### ● Content:

1. Members and Candidates must disclose to **all** their employer, clients, and prospective clients, as appropriate, any compensation, consideration, or benefit received from, or paid to, others for the recommendation of products or services **in advance**.

### ● Guidance

2. Such disclosure will allow the client or employer to evaluate
  - ✓ **Any partiality** shown in any recommendation of services
  - ✓ The **full cost** of the service.
3. Disclose **nature** of consideration.
  - ✓ For example, flat fee or percentage basis, one-time or continuing benefit, based on performance, benefit in form of research or other noncash benefit, together with the estimated dollar value.
  - ✓ **Consideration** includes all fees, whether in cash , in soft dollar, or in kind.

# Summary

## Guidance for Standards I–VII

### VI(C).Referral fees

all their employer, clients, and prospective clients in advance

## Guidance for Standards I-VII

- Yao Tang, CFA, has a large percentage of his net worth invested in the Australian mining company Outback Mines, which he has held for many years. Tang is in the process of moving to a new employer where he is responsible for initiating research on mining companies. Shortly after his move, Tang is asked to complete a research report on Outback. In order to meet the CFA Institute Standards of Professional Conduct concerning his stock holding, which of the following actions is most appropriate for Tang to take?
  - A. Disclose his stock holding to his employer and to clients.
  - B. Sell his stock holdings to eliminate any potential conflict of interest.
  - C. Refuse to write the report and ask his employer to assign another analyst to complete the analysis.

## Guidance for Standards I-VII

- Correct Answer: A
  - Full disclosure should be made as required by Standard VI(A). This standard does not preclude an analyst from owning shares in a covered company but any ownership needs to be adequately disclosed. As the stock in question has been held for many years it may not be practical to sell it due to issues such as tax consequences. In addition, since the analyst has been hired to initiate coverage of mining companies, the firm may not have other analysts that would be as competent in completing a research report on mining companies.

## Guidance for Standards I-VII

- Ross Nelson, CFA, manages accounts for high-net-worth clients including his own family's account. He has no beneficial ownership in his family's account. Because Nelson is concerned about the appearance of improper behavior in managing his family's account, when his firm purchases a block of securities, Nelson allocates to his family's account only those shares that remain after his other client accounts have their orders filled. The fee for managing his family's account is based on his firm's normal fee structure. According to the Standards of Practice Handbook, Nelson's best course of action with regard to management of his family's account would be to:
  - A. treat the account like other client accounts.
  - B. treat the account like other employee accounts of the firm.
  - C. remove himself from any direct involvement by transferring responsibility for this account to another investment professional in the firm.

## Guidance for Standards I-VII

- Correct Answer : A.
  - Nelson has breached his duty to his family by treating them differently from other clients. They are entitled to the same treatment as any other client of the firm. Nelson should treat his family's account like any other client account [Standard III(B) related to fair dealing and Standard VI(B) related to Priority of Transactions].

# 21. VII(A).

## Conduct as members and candidate

---

- ▣ Content
- ▣ Guidance



## 21. Standard VII(A): Content

- **Content:**

1. Members and Candidates must not engage in any conduct that compromises the reputation or integrity of CFA Institute or the CFA designation or the integrity, validity, or security of the CFA Institute programs.



## 21. Standard VII(A): Guidance

### ● Guidance:

2. Standard VII(A) covers the conduct of CFA Institute members and candidates involved with the CFA Program and **prohibits** any conduct that undermines the public's confidence that the CFA charter represents a level of achievement based on merit and ethical conduct.
3. Conduct covered includes but is not limited to
  - ✓ Giving or receiving assistance (cheating) on any other CFA Institute examination;
  - ✓ Violating the rules and policies of the CFA Program related to exam administration;
  - ✓ Disregarding or attempting to circumvent security measures established by CFA Institute for the CFA exam;
  - ✓ Providing confidential program or exam information to candidates or the public;
  - ✓ Improperly using an association with CFA Institute to further personal or professional goals;
  - ✓ Misrepresenting information on the Professional Conduct Statement or in the CFA Institute Continuing Education Program.

## 21. Standard VII(A): Guidance

- **Guidance - Confidential Program Information**

4. CFA Institute is vigilant about protecting the integrity of the CFA Program content and examination process and **prohibits** candidates from **disclosing confidential material gained during the exam process.**

- **Guidance - Additional CFA Program Restrictions**

5. Violating any of the testing policies, such as the calculator policy, personal belongings policy, or the Candidate Pledge, constitutes a **violation of Standard VII(A).**

- **Guidance - Expressing an Opinion**

6. Expressing opinions regarding the CFA Program or CFA Institute is OK.

# Summary

## **Guidance for Standards I–VII**

### **VII(A).Conduct as members and candidates**

No specific exam content, opinion is ok.

## 22. VII(B). Reference to institute, designation, program

---

- ▣ Content
- ▣ Guidance

## 22. Standard VII(B): Content

- **Content:**

1. When referring to CFA Institute, CFA Institute membership, the CFA designation, or candidacy in the CFA Program, Members and Candidates must not misrepresent or exaggerate the meaning or implications of membership in CFA Institute, holding the CFA designation, or candidacy in the CFA Program.

## 22. Standard VII(B): Guidance

### ● Guidance

2. How to use CFA:

- ✓ adj, not n.
- ✓ Always capitalized.
- ✓ CFA level I ×
- ✓ C.F.A ×
- ✓ Pseudonyms or online profile names created to hide identity should not be tagged with CFA designations.
- ✓ Mustn't cite the expected date of exam completion and award of charter.

3. A candidate who has passed level III but has not received charter can't use CFA designation.

4. In citing the designation in a resume, a charterholder should use the date that he or she received the designation and should cite CFA institute as the conferring body.

- ✓ **Example** : CFA, 2001, CFA Institute ( optional Charlottesville, Virginia, USA )

## 22. Standard VII(B): Guidance

- **Guidance**

6. It's only appropriate to use CFA logo on the business card or letterhead of each individual CFA charterholder. Candidates can mention in their C.V.
7. The order of CFA and CPA doesn't matter.

- **Guidance – CFA Institute membership**

8. Once accepted as a member, must satisfy the followings to maintain status:
  - ✓ Remit annually to CFA Institute a complete Professional Conduct Statement.
  - ✓ Pay membership dues annually.

- **Guidance – Using CFA Designation**

9. If a charterholder fails to meet membership requirements, he forfeits the right to use CFA designation. Until membership is reactivated, can only state that they were charterholders in the past.

## 22. Standard VII(B): Guidance

### ● Guidance – Referring to candidacy

10. When can you state yourself as a candidate?
  - ✓ After receiving registration acceptance letter by CFA Institute
  - ✓ Before exam results have been received
11. If a candidate passes each level of the exam on the first try and wants to state that he or she did so, that is not a violation because it is a statement of fact,
  - ✓ But must not over-promise the competency and future investment results



# Summary

## **Guidance for Standards I–VII**

### **VII(B).Reference to institute, designation, program**

Factual statement, right to use the designation

## Guidance for Standards I-VII

- Millicent Plain has just finished taking Level II of the CFA examination. Upon leaving the examination site, she meets with four Level III candidates who also just sat for their exams. Curious about their examination experience, Plain asks the candidates how difficult the Level III exam was and how they did on it. The candidates say the essay portion of the examination was much harder than they had expected and they were not able to complete all questions as a result. The candidates go on to tell Plain about broad topic areas that were tested and complain about specific formulas they had memorized what did not appear on the exam. The Level III candidates least likely violated the CFA Institute Standards of Professional Conduct by discussing:
  - A. specific formulas.
  - B. broad topic areas.
  - C. the examination essays.

## Guidance for Standards I-VII

- Correct Answer : C
  - Because discussing the level of difficulty of the essay portion of the examination did not violate Standard VII (A) Conduct as Members and Candidates in the CFA Program. Standard VII (A) and the Candidate Pledge were violated by candidates revealing broad topical areas and formulas tested or not tested on the exam.

## Guidance for Standards I-VII

- Jeffrey Jones passed the Level I CFA examination in 2017 and the Level II examination in 2019. He is not currently enrolled for the Level III examination. According to the CFA Institute Standards of Professional Conduct, which of the following is the most appropriate way for Jones to refer to his participation in the CFA Program?
  - A. Jeffrey Jones, CFA (expected 2024)
  - B. Candidate in the CFA Institute CFA Program
  - C. Passed Level II of the CFA examination in 2019

## Guidance for Standards I-VII

- Correct Answer : C
  - Because no designation exists for someone who has passed Level I, Level II, or Level III of the CFA exam [Standard VII(B)]. Persons who have passed a certain level of the exam may state that they have completed that level. A person can only state he is a Candidate if he is currently enrolled in the CFA Program. It is also an improper reference to use “expected” a part of the designation.

# Summary

## **Module: Guidance for Standards I–VII**

**I. Professionalism; II. Integrity of Capital Markets;  
III. Duty To Clients; IV. Duty To Employers; V. Investment;  
VI. Conflicts of Interest; VII. Responsibility as Members**

# Module



## Introduction to the Global Investment Performance Standards (GIPS)

1. Introduction to the Global Investment Performance Standards (GIPS)

# Introduction to GIPS

- ❑ Why were the GIPS Standard created
- ❑ Who can claim compliance
- ❑ Who benefits from compliance
- ❑ Composites
- ❑ Verification





# Introduction to GIPS

## I.I Why were the GIPS Standard created?

- **GIPS are a set of ethical principles based on a standardized, industry-wide approach**
- **Misleading practices that hinder performance comparability:**
  - Representative accounts: showing a top-performing portfolio as representative of a firm's result.
  - Survivorship Bias: excluding "weak performance" accounts that have been terminated.
  - Varying Time Periods: showing performance for selected time periods with outstanding returns.

# Introduction to GIPS

## I.II. Who can claim compliance

- **Complying with the GIPS standards is voluntary**
- **Any firms that actually manage assets can claim compliance with the Standards.**
  - Consultants → can't claim compliance unless actually manage assets.
  - Software (and vendor of software) cannot be compliant → can assist firms in compliance with GIPS
- **Asset owners** may comply with the GIPS standards in the same way **as firms** if they **compete for business**. If they don't compete for business but report their performance to an oversight body, asset owners may choose to comply with the GIPS standards for asset owners.
- **Firm-wide and full compliance**
  - Can't be achieved on a single product or composite.
  - Two options: (1) Fully comply with all requirements; (2) Not comply with all requirements and not claim compliance

# Introduction to GIPS

## I.III. Who benefits from compliance?

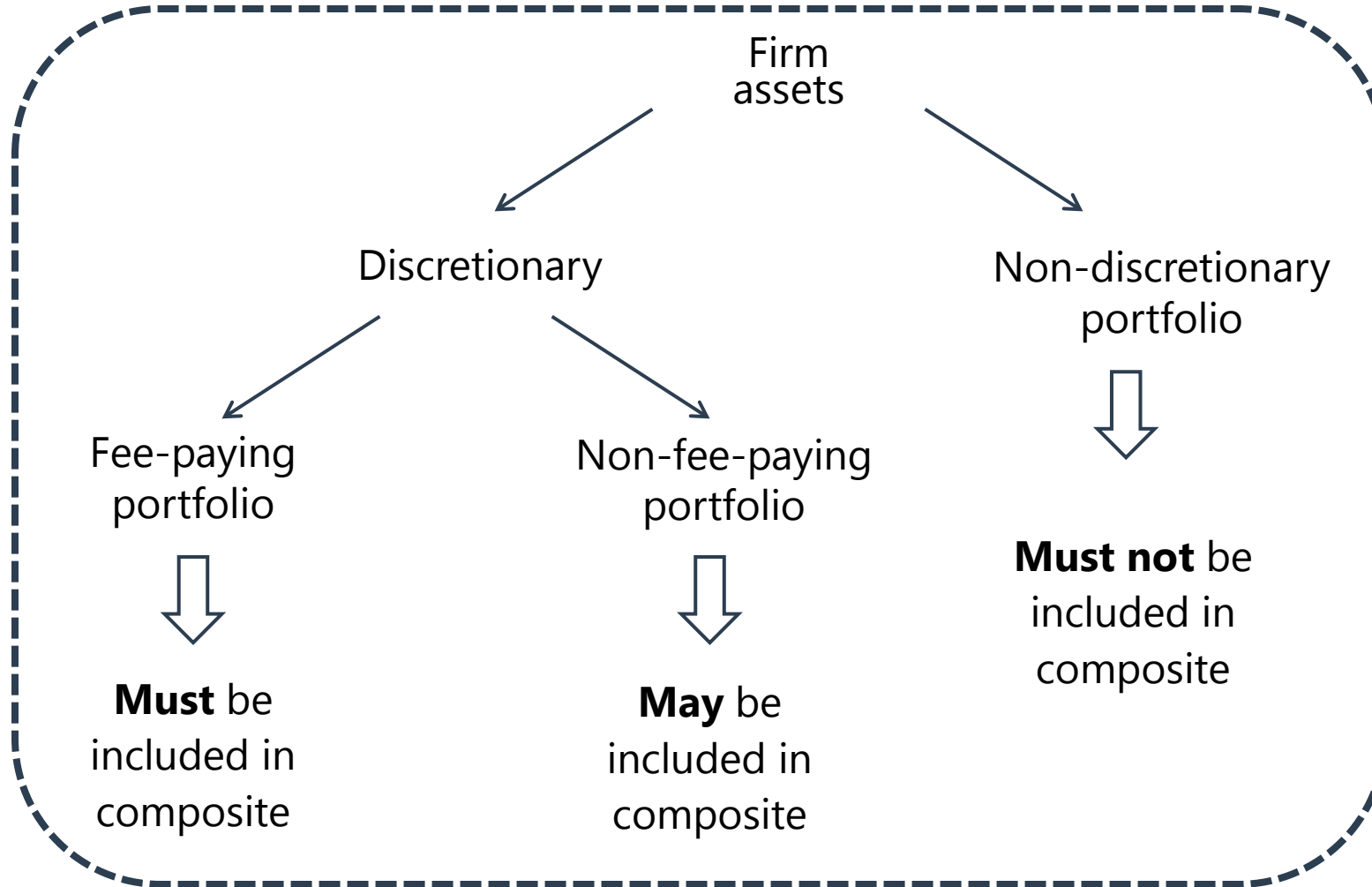
- **Benefit 3 groups: asset managers, prospective clients and asset owners and their oversight bodies.**
- **For firms:**
  - Can assure prospective clients that their track record is complete and fairly presented;
  - Able to participate in competitive bids against other compliant firms throughout the world;
  - Strengthen firm's internal control over performance-related processes.
- **For investors:**
  - Have greater confidence in the integrity of performance presentation of a compliant firm, and can easily compare performance presentation from different firms.
  - Compliance enhances the credibility of firms.
- **For asset owners and their oversight bodies:**
  - Report to the oversight body using the same principles facilitates the understanding of the sources of risk and excess return in the funds under supervision.

# Introduction to GIPS

## II. Composites

- A composite is a grouping of individual discretionary portfolios representing a similar investment strategy, objective, or mandate.
- A composite, such as Global Equities, must include all fee-paying portfolios (current and past) that the firm has managed in accordance with this particular strategy.
- The firm should identify which composite each managed portfolio is to be included in **before** the portfolio's performance is known.
  - This prevents firms from choosing portfolios to include in a composite in order to create composites with superior returns.

## •— Introduction to GIPS – Composite or not? —•



Non-discretionary portfolio excluded in composite but included in firm assets.

# Introduction to GIPS

## III. Verification

- **Verification** is the review of an investment management firm's performance measurement processes and procedures **by an independent third-party "verifier"**.
  - Third-party verification brings credibility to the claim of compliance and supports the overall guiding principles of full disclosure and fair representation of investment performance.
- **Verification tests:**
  - Whether the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis.
  - Whether the firm's processes and procedures are designed to calculate and present performance results in compliance with the GIPS standards.
- A **single verification report** is issued in respect of the whole firm; verification cannot be carried out for a single composite.

# Summary

## Introduction to the Global Investment Performance Standards (GIPS)

Introduction to GIPS

# 问题反馈

- 如果您认为金程**课程讲义/题库/视频**或其他资料中**存在错误**，欢迎您告诉我们，所有提交的内容我们会在最快时间内核查并给与答复。
- **如何告诉我们？**
  - 将您发现的问题通过扫描右侧二维码告知我们，具体的内容包含：
    - ✓ 您的姓名或网校账号
    - ✓ 所在班级
    - ✓ 问题所在科目(若未知科目，请提供章节、知识点和页码 )
    - ✓ 您对问题的详细描述和您的见解
- **非常感谢您对金程教育的支持，您的每一次反馈都是我们成长的动力。**

