Question #1 of 21

Question ID: 1390965

Todd Gable, CFA, was attending a noon luncheon when he overheard two software executives talking about a common vendor, Datagen, about how wonderful they thought the company was, and about a rumor that a major brokerage firm was preparing to issue a strong buy recommendation on the stock. Gable returned to the office, checked a couple of online sources, and then placed an order to purchase Datagen in all of his discretionary portfolios. The orders were filled within an hour. Three days later, a brokerage house issued a strong buy recommendation and Datagen's share price went up 20%. Gable then proceeded to gather data on the stock and prepared a report that he dated the day before the stock purchase.

Gable has:

A) violated the Standards by improper use of inside information.

B) violated the Standards by using the recommendation of another brokerage firm in his report.

C) violated the Standards by not having a reasonable basis for making the purchase of Datagen.

Explanation

Standard V(A) requires members to have a reasonable and adequate basis for taking investment actions. Overhearing a conversation does not provide adequate basis. It is not improper to use overheard conversations that do not include inside information, nor is it improper to reference another firm's report to substantiate adequate basis, if the other report is justified.

Question #2 of 21

Question ID: 1459576

Lindsay Gordon is a Level II CFA candidate. Gordon's best friend, Steve Haney, is also a Level II candidate and has registered for the same exam window as Gordon. Because Haney's exam appointment is the day before Gordon's appointment, Gordon suggests that Haney try to remember some of the exam questions and let her know what they asked. After Haney takes his exam, he reminds Gordon that the Code and Standards prohibit candidates from disclosing specific exam questions, and only gives her a general idea of what topics were tested or not tested. Which of the following statements regarding Gordon and Haney is *most accurate*?

A) Neither Gordon nor Haney is in violation of the Code and Standards.

B) Gordon is in violation of the Code and Standards, but Haney is not in violation.

C) Both Gordon and Haney are in violation of the Code and Standards.

Explanation

Both Gordon and Haney violated Standard VII(A) Conduct as Participants in CFA Institute Programs by compromising the integrity of the exam. The Standard prohibits candidates from discussing specific exam questions or which topics were tested or not tested.

(Module 73.1, LOS 73.b)

Question #3 of 21

Question ID: 1115873

Lance Tuipulotu, CFA, manages investments for 400 individuals and families and often finds his resources stretched. When his largest investors petition him to include a 5% to 7% allocation of non-investment-grade bonds in their portfolios, he decides he needs additional help to meet the request. He considers various independent advisors to use as submanagers, but determines that the most qualified advisors would be too expensive. Reasoning that a lower-cost provider would enable him to pass the savings along to his clients, he chooses that provider to invest the new bond allocation. Tuipulotu has violated:

A) Both Standard III(C) Suitability and Standard V(A) Diligence and Reasonable Basis.

B) Standard III(C) Suitability by failing to consider the appropriateness of the non-investment-grade bonds.

C) Standard V(A) Diligence and Reasonable Basis by letting fee structure determine the selection of the submanager.

Explanation

Both Standard III(C) Suitability and Standard V(A) Diligence and Reasonable Basis were violated. Tuipulotu must perform a full IPS review to determine the appropriateness of the new portfolio allocations. Submanagers should not be selected by cost structure alone, as the quality and appropriateness of the submanager is Tuipulotu's responsibility.

Question #4 of 21

Question ID: 1459565

Vijay Gill, CFA, leases office space from Land Bank in exchange for an agreement that Gill will pay Land 20% of any fees paid by Land customers to Gill for investment management services. Gill also has an arrangement with Bloom Insurance Advisors whereby Gill receives a fee for each client referred. Gill only refers clients that request insurance products. Gill meets with Randolph Song, a Land Bank customer, who is interested in Gill's asset management services as well as insurance products. Gill is required to disclose to Song:

A) the terms of the arrangement with Bloom, but not the terms of the arrangement with Land Bank.

B) the terms of the arrangements with both Land Bank and Bloom.

C) neither the Land Bank nor Bloom arrangements, but may disclose them if he chooses to do so.

Explanation

Standard VI(C) Referral Fees requires members to disclose to clients and prospects any consideration or benefit received by the member or delivered to others for the recommendation of any services to the client or prospect. Gill is delivering a benefit to Land Bank and receiving a benefit from Bloom, both of which must be disclosed to Song.

(Module 73.1, LOS 73.a)

Question #5 of 21

Question ID: 1459557

Paul Thomas, CFA, is designing a new layout for research reports his firm writes and issues on individual stocks. In his design, Thomas includes a stock chart on the first page of each report. He does not reference that the charts are copied from an unrecognizable finance website. Thomas has:

A) violated CFA Institute Standards of Professional Conduct because he did not make sure that the information in these charts is accurate.

B) violated CFA Institute Standards of Professional Conduct because he did not state the source of the charts.

C) not violated CFA Institute Standards of Professional Conduct because these charts are widely available over the internet.

Explanation

Standard I(C) Misrepresentation. Members should not copy or use material prepared by others without acknowledging and identifying the source of such material. Using charts and graphs without stating their source is a violation of the Standard.

(Module 73.1, LOS 73.a)

Question #6 of 21

Question ID: 1469330

Ralph Lim and Susan Bland have both passed Level I of the CFA Program. Both are currently enrolled to sit for Level II. Lim's business card reads, "Ralph Lim, CFA Level I." Bland's resume states, "Level II Candidate in the CFA Program." According to CFA Institute Standards of Professional Conduct involving use of the professional designation:

A) Bland violated the Standard, but Lim did not.

B) Both Lim and Bland violated the Standard.

C) Lim violated the Standard, but Bland did not.

Explanation

There is no designation for someone who has passed Level I, Level II, or Level III of the CFA examination. Candidates may state, however, that they have completed Level I, II, or III, as the case may be, in the CFA Program. Thus, Lim violated the Standard, but Bland did not.

Question #7 of 21

Question ID: 1459572

Mary Hiller, CFA, is a senior analyst at a mutual fund. She is also a member of the Board of the Directors of her daughter's Skating Club. She is often asked for advice about the management of the club budget and about possible short-term investments, but she is not paid for this advice. She does not undertake any research to answer these questions, providing information based only on the general practices of the mutual fund at that moment. The only benefit she receives is a free monthly membership for her daughter that would usually cost $182. What should she do before making any recommendations, in order to comply with the CFA Institute requirements?

A) Consult only on her free time and do not accept any benefit greater than $100.

B) Inform her current clients about her outside consulting.

C) Obtain prior permission from her employer.

Explanation

According to Standard IV(A) Loyalty to Employer, it is the employee's duty to inform the employer about any type of outside consulting service, including duration and any compensation. Only after receiving permission from her employer, can she proceed.

(Module 73.1, LOS 73.b)

Question #8 of 21

Question ID: 1459562

Jan Hirsh, CFA, is employed as manager of a college endowment fund. The college's endowment is held by the brokerage firm Advisors, Inc. Over the years, Hirsh has developed a solid relationship with Advisors. Because of this relationship, Advisors has given her their Platinum level service for her personal account. Advisors ordinarily gives the Platinum level only to clients who do a minimum of $2,500 of commission business in a year. Hirsh has never reached the $2,500 commission level and probably will never do so. According to Standard IV(B), Additional Compensation Arrangements, Hirsh needs to:

A) inform her supervisor in writing about the Platinum account. ✓

B) inform her supervisor verbally about the Platinum account. ✗

C) do none of the actions listed here. ✗

Explanation

Having the Platinum account is a benefit from her managing the endowment, which led to the relationship with Advisors. Members should report to their employers any additional compensation or benefits they receive for their services. This must be in writing. Doing $2,500 in business alone will not negate her obligation unless she explicitly tells Advisors that she is willing to accept whatever penalties accompany a Platinum account when a client does less business.

(Module 73.1, LOS 73.a)

Question #9 of 21

Question ID: 1459559

Heidi Krueger, CFA, an investment advisor, applies soft dollars generated from client accounts to purchase a report on the economic impact of world events, and to purchase a new conference table for the office she uses to meet with clients and prospects. Do these purchases violate Standard III(A) Loyalty, Prudence, and Care?

A) Neither of these purchases violates the Standard. ✗

B) Only one of these purchases violates the Standard.

C) Both of these purchases violate the Standard.

Explanation

Using soft dollars for the purchase of office furniture does not benefit clients and is a violation. Purchasing research reports with soft dollars is not a violation, but the advisor should ensure that research purchased with client brokerage will benefit her clients.

(Module 73.1, LOS 73.a)

Question #10 of 21

Question ID: 1390962

An analyst meets with a new client. During the meeting, the analyst sees that the new client's portfolio is heavily invested in one over-the-counter stock. The analyst has been following the stock and thinks it will perform well in the long run. The analyst arranges through a brokerage firm to simultaneously sell a large number of shares of the stock via a series of cross trades from the new client's portfolio to various existing clients. He arranges the trades to be executed at a price that approximates the current market price. This action is:

A) not in violation of the Standards.

B) a violation of Standard III(A), Loyalty, Prudence, and Care.

C) a violation of Standard III(B), Fair Dealing.

Explanation

There is no violation. It is in the best interest of the client to be diversified and selling via a series of cross trades will likely reduce price impact costs when compared to selling directly into the market. The analyst appears to have reasonable basis for putting the securities in the accounts of other clients.

Question #11 of 21

Question ID: 1390966

The following scenarios involve two analysts at Dupree Asset Management, a small New York-based company with about $150 million in assets under management. Dupree restricts personal trading of stocks analyzed, corporate directorships, trustee positions, and other special relationships that could reasonably be considered a conflict of interest with their responsibilities to their employer.

- Ray Bolt, CFA, is a senior investment analyst. Bolt was recently elected to the board of trustees of his alma mater, Midwest University, and was appointed as the chairman of the University's endowment committee. Midwest has more than $2 billion in its endowment. Bolt must travel from New York to Chicago eight times a year to attend meetings of the board of trustees and endowment committee. Bolt did not inform Dupree of his involvement with Midwest University.
- Wanda Delvecco, a candidate in the CFA Program, is a junior investment analyst. She recently wrote a research report on Aveco Communications and recommended the stock for Dupree's "buy" list. Delvecco bought 200 shares of Aveco stock for her personal account 12 months before she wrote her research report. Over the past 12 months, the stock's price has been in the $20-42 price range. Delvecco has not informed Dupree of her ownership of Aveco stock.

According to CFA Institute Standards of Professional Conduct, which the following statements about Bolt and Delvecco's actions is CORRECT?

A) Neither Bolt nor Delvecco violated the Standards.

B) Delvecco violated the Standards, but Bolt did not.

C) Both Bolt and Delvecco violated the Standards.

Explanation

Standard VI(A), Disclosure of Conflicts, requires that Bolt inform Dupree of his involvement with Midwest University given that Bolt's new role can be expected to be time consuming and possibly affect his responsibilities at Dupree. Delvecco is required to disclose her ownership of Aveco stock before conducting the research report because such ownership could bias her objectivity in making a recommendation. She should have discussed owning the stock with her supervisor before beginning to write the research report on Aveco.

Question #12 of 21

Question ID: 1459567

Francisco Perez, CFA, CPA, is a portfolio manager for an investment advisory firm. Due to the prominence of his position, he is often invited to attend free marketing and educational events hosted by firms which seek to inform the investment community about their investment processes. One such firm, Unlimited Horizons, has invited Perez to attend free educational events which qualify for Continuing Education credits which could help Perez maintain his CPA designation. Perez should *most likely*:

A) accept the invitation as no cash compensation is involved and the primary intent is to educate and inform the investment community.

B) decline to attend the event as it could result in a violation of Standard I(A) "Knowledge of the Law."

C) decline to attend the event as it could result in a violation of Standard I(B) "Independence and Objectivity."

Explanation

Perez should decline the invitation as it creates the impression of lack of independence. If he does not accept the free continuing education courses, he would have to pay for them some other way so the free courses are a form of compensation. Nothing in the vignette suggests the free classes are illegal.

(Module 73.1, LOS 73.b)

Question #13 of 21

Question ID: 1459568

Nancy Hall, a candidate in the CFA program, is an analyst for a mutual fund. As part of her job she makes company visits to interview executives. On a recent trip she stayed with her sister instead of at a hotel. In her expenses Hall included a hotel charge of $100, which was less than the amount allowed by her employer. After receiving a check for her expenses, Hall disclosed to her supervisor that she had stayed with her sister instead of at a hotel. She also returned the $100 to her employer. According to CFA Institute Standards of Professional Conduct, which of the following statements *best* describes Hall's professional conduct?

A) Hall engaged in professional misconduct.

B) Hall did not engage in professional misconduct because she eventually disclosed this information and returned the $100 to her employer.

C) Hall did not engage in professional misconduct because she did not meet all of the requirements to use the CFA designation.

Explanation

Hall engaged in professional misconduct because her act involved dishonesty, fraud, and deceit.

(Module 73.1, LOS 73.b)

Question #14 of 21

Question ID: 1390967

Gordon McKinney, CFA, works in the trust department of a bank. The bank's trust account holds a large block of a particular company. McKinney learns that this company is going to buy back one million shares at a 15% premium to the market price on a first-come-first-served basis. McKinney immediately tells his mother-in-law to tender her shares but waits until the end of the day to tender the trust's shares. McKinney has *most* likely violated:

A) Standard IV(A), Loyalty to Employer.

B) Standard II(A), Material Nonpublic Information.

C) Standard VI(B), Priority of Transactions.

Explanation

Standard VI(B), Priority of Transactions, applies. If an analyst decides to make a recommendation about the purchase or sale of a security, he must give his customers or employer adequate opportunity to act on this recommendation before acting on his own behalf. Personal transactions include those made for the member's own account and family accounts. Here, McKinney violated Standard VI(B) by acting on his mother-in-law's behalf and then waiting until the end of the day to act on his employer's behalf.

Explanations for other responses:

- Standard IV(A), Loyalty to Employer, does not apply. This standard concerns a member competing with his/her employer (independent practice), for example a member who engages in outside consulting.
- Standard II(A), Material Nonpublic Information, does not apply. The question does not indicate that the information is not public.

Question #15 of 21

Question ID: 1469328

Deloris Johnson, CFA, observed that her supervisor has violated a federal securities regulation. Johnson discussed the matter with her company's compliance department but they have taken no action. According to the CFA Institute Code and Standards of Professional Conduct, Johnson is required to:

A) confront the supervisor and attempt to stop the violation.

B) dissociate from the supervisor's activity.

C) report the violation to securities regulators.

Explanation

Johnson must dissociate herself from her supervisor's activity, for example by asking to be reassigned. The Code and Standards do not require Johnson to report the violation to governmental or regulatory organizations unless doing so is required by applicable law. Johnson has attempted to stop the violation by discussing it with her compliance department. She is not required by the Code and Standards to confront the supervisor.

Question #16 of 21

Question ID: 1459574

Robert Hamilton, a CFA candidate, is preparing a research report on Pets-R-Us for public distribution. Hamilton's preliminary report contains unfavorable earnings forecasts for the next four quarters. As part of his analysis, Hamilton met with Linda Brisson, the president of Pets-R-Us, and asked her to review the preliminary report for factual inaccuracies. Brisson revised Hamilton's earnings forecasts so that the quarterly earnings showed an upward trend and resulted in positive earnings by the fourth quarter. Hamilton included the revised earnings figures in his report without further review. Although the final report included the basic characteristics of Pets-R-Us, it emphasized certain areas such as projected quarterly earnings but only briefly touched on others. According to CFA Institute Standards of Professional Conduct on research reports, Hamilton:

A) did not violate the Standard.

B) violated the Standard because the report did not give similar attention to all areas but instead emphasized quarterly earnings at the expense of other areas.

C) violated the Standard because he did not thoroughly review and analyze any information provided by Brisson.

Explanation

Standard V(B) permits Hamilton to ask company management to review his report for factual inaccuracies, but Hamilton should have taken care to thoroughly review and analyze any information provided by the company. Hamilton is not required to give equal emphasis to all areas but can emphasize certain areas, touch briefly on others, and omit certain aspects deemed unimportant.

(Module 73.1, LOS 73.b)

Question #17 of 21

Question ID: 1115938

Jess Green, CFA is the research director for Castle Investment, Inc., and has supervisory responsibility over eight analysts, including three CFA charterholders. Castle has a compliance program in place. According to CFA Institute Standards of Professional Conduct, which of the following is *least likely* an action that Green should take to adhere to the compliance procedures involving responsibilities of supervisors? Green should:

A) issue periodic reminders of the procedures to all analysts under his supervision.

B) incorporate a professional conduct evaluation as part of the performance review only for the three CFA charterholders.

C) disseminate the contents of the compliance program to the eight analysts.

Explanation

Green should incorporate a professional conduct evaluation as part of his review of all eight analysts under his supervision, not just the three CFA charterholders.

Question #18 of 21

Question ID: 1459558

Lisa Pierce, CFA, has been researching Lander Manufacturing for the past three weeks. She likes the company's history of fulfilling its contracts on time and within budget. She learns from the uncle of a maintenance worker at Lander's headquarters that a group of well-dressed individuals arrived at headquarters in a lime green-colored limousine. Pierce knows from publicly available information that Gilbert Controls needs a large supply of specialized motors in its domestic division. She also knows that the executive officers of Gilbert usually travel in a lime green limousine. Pierce concludes that it is very likely that Gilbert will offer a large contract to Lander. Based on this development and her prior research Pierce would like to acquire Lander Manufacturing shares for her client accounts.

Pierce should:

A) not acquire the shares because she possesses material nonpublic information.

B) not acquire the shares until after she has contacted Lander's management and encouraged them to publicly announce information about the Gilbert Controls contract. She should also wait until Lander has made the announcement and the public has had time to react to it and then make the acquisition.

C) proceed to acquire the shares.

Explanation

Standard II(A) prohibits members from taking investment action if they possess material nonpublic information. Pierce combined information that was not misappropriated, with her knowledge of the company, to reach a conclusion under the mosaic theory, which is permissible under the standards. She can proceed to buy the shares.

(Module 73.1, LOS 73.a)

Question #19 of 21

Question ID: 1469329

Calvin Doggett, CFA, has been contacted by the CFA Institute Professional Conduct Program (PCP) regarding allegations that he has taken investment actions that were unsuitable for his clients. Doggett is questioned by PCP concerning the identity of his clients he considered suitable for investing in a very risky start-up company that eventually went bankrupt.

Doggett will:

A) not violate the Code and Standards by revealing the names, financial condition and investment objectives of his clients to PCP. ✓

B) not violate the Code and Standards only if he reveals the financial condition and investment objectives of his clients on an anonymous basis and does not reveal the names of his clients to PCP. ✗

C) violate the Code and Standards by fully cooperating with a PCP investigation if it means revealing confidential information. ✗

Explanation

Standard III(E) requires members to preserve client confidentiality. An exception to this standard is a PCP investigation. Because PCP will also keep the clients' information confidential, members are expected to fully cooperate with PCP investigations.

Question #20 of 21

Question ID: 1459571

While it would be customary to report both five-year and ten-year performance data, Seminole Equity Partners has been in existence for only eight years. Because of this, Kurt Dambach does not report ten-year data but reports for both five years and since the inception of the fund. This he notes in a footnote at the bottom of the information sheet. This action is:

A) a violation of the Standard concerning prohibition against misrepresentation.

B) in accordance with the Code and Standards since he has indicated the basis in a footnote.

C) a violation of the Standard concerning performance presentation.

Explanation

Members who communicate performance information must ensure that the information is fair, accurate, and complete. Seminole Equity's presentation meets this standard.

(Module 73.1, LOS 73.b)

Question #21 of 21

Question ID: 1115756

Steve Waters, a Level I CFA candidate, has decided to enter into a long position of Farmco stock. Since Farmco is thinly traded, Waters is concerned the order will overwhelm the liquidity of Farmco and the price will surge. Waters engages in a series of block trades in order to accomplish the purchase. According to Standard II(B), Market Manipulation, Waters has engaged in:

A) both transaction-based manipulation and information-based manipulation.

B) neither transaction-based manipulation nor information-based manipulation.

C) transaction-based manipulation, but not information-based manipulation.

Explanation

Waters is not in violation of Standard II(B), Market Manipulation. Transaction-based manipulation includes, but is not limited to, transactions that artificially distort prices or volume. Information-based manipulation includes, but is not limited to, spreading false rumors about a firm in order to induce others to trade.