CFA Societies Australia

Michaela Francis
Executive Director
CFA Society of Sydney
GPO BOX 4805 Sydney NSW 2001
exec@cfas.org.au

1 June 2018

Dr Mark Brimble
Acting Managing Director
Financial Adviser Standards and Ethics Authority
Australia

Dear Dr. Brimble:

Re: Exposure Draft of Proposed Standard

On behalf of our members in Australia, CFA Institute and CFA Societies Australia (which includes CFA Society Sydney, CFA Society Melbourne and CFA Society Perth), we welcome the opportunity to comment on the Financial Adviser Standards and Ethics Authority's (FASEA) proposed *Code of Ethics for Financial Advisers* (hereafter the "Code").

CFA Institute represents the views of investment professionals before standard setters, regulatory authorities and legislative bodies worldwide on issues that affect the practice of financial analysis and investment management, education and licensing requirements for investment professionals. We represent these professionals on issues that affect the integrity and accountability of global financial markets.

We understand the objectives of the Code are to: 1) shape and reinforce ethical conduct among financial advisers, and 2) encourage higher standards of ethical behavior and professionalism in the financial services industry for consumers' benefit and the ultimate benefit of society. The proposed Code includes several fundamental ethical principles and provides relevant providers with a foundation for ethical conduct.

The classification framework used by FASEA places a priority on protecting consumers' interests. The Code's sections on standards of ethical behavior, standards of client care, and standards of quality process contain client-centric proposals that may help to rebuild trust among clients, which has been diminished by the poor conduct of some financial advisers. However, we believe the Code would be further improved if FASEA adopted our recommendations below.

Accordingly, we suggest changes to the proposed Code that would, in our view, further enhance the Code's effectiveness and practicality, ensuring uniformly high standards throughout the financial advice industry. This letter provides:

- Background on the CFA Institute and CFA Societies of Australia;
- Information on the CFA Institute Code of Ethics and Standards of Professional Conduct;
- Responses to FASEA's request for commentary on the proposed Code; and
- CFA Institute comments on the practical application of the proposed Code.

Background on the CFA Institute

CFA Institute is the leading global association of investment professionals that sets the standard for professional excellence and credentials. We administer the CFA® Program, CIPM® Program, and Investment Foundations™ certificate program and offer world-class education and professional development opportunities.

The organisation champions ethical behavior in investment markets and is a respected source of knowledge in the global financial community. Our end goal is to create an environment where investors' interests come first and markets function efficiently for the ultimate benefit of all members of our society. The Institute is a non-profit organisation and the revenue required to fulfill our stated mission is sourced from membership and candidate fees.

An acknowledged strength of CFA Institute is that it has managed for many decades to establish and sustain the highest standards of technical, professional and ethical excellence of the global investment profession. We have the capacity, capability, track record and desire to support governments, regulators and industry in creating a world-class financial system with the highest ethical standards, including in Australia. CFA Institute has more than 150,000 members in 165+ countries and territories, and 150 member societies. For more information, please visit www.cfainstitute.org.

Background on the CFA Societies of Australia

CFA Societies Australia is a non-profit organisation that represents the local member societies of Sydney, Melbourne and Perth, which are member societies of CFA Institute. Our aim is to help connect members to a global network of investment professionals and to promote fairness and integrity across the investment industry. Our CFA Societies Australia membership base includes portfolio managers, security analysts, investment advisors and other financial professionals who:

- Promote ethical and professional standards within the investment industry;
- Encourage professional development through the CFA Program and continuing education;
- Facilitate the exchange of information and opinions among people within the local investment community and beyond; and
- Work to further the public's understanding of the CFA designation and investment industry.

For more information, please visit www.cfa-australia.com.au/

The CFA Institute Code of Ethics and Standards of Professional Conduct

The CFA Institute Code and Standards (Appendix I of this letter) are fundamental to the values of CFA Institute and essential to its mission to lead the investment profession globally by promoting the highest standards of ethics, education and professional excellence for the ultimate benefit of society. This is critical to maintaining the public's trust in financial markets and in the investment profession.

All CFA Institute members (including holders of the Chartered Financial Analyst® [CFA®] designation) must abide by the Code and Standards and demonstrate their commitment each year to the Professional Conduct Statement. Members are encouraged to notify their employer of this responsibility. Violations may result in disciplinary sanctions by CFA Institute, which can include revocation of membership, and revocation of the right to use the CFA designation. Candidates registered for the CFA examinations are also required to abide by our Code and Standards.

Over time, we have received many queries from asset management firms worldwide on adopting our Code and Standards as their internal code of ethics and conduct. This is now supported through the Asset Manager Code[1], which applies the same principles from the CFA Institute Code and Standards.

As a self-regulatory organisation, we have a Professional Conduct department that enforces our Code and Standards. Only a small percentage of CFA Institute members are investigated and sanctioned. Ensuring compliance would be crucial to the success of the Code of Ethics proposed by FASEA. **FASEA may wish to consider how CFA Institute encourages adherence to its own Code and Standards.[2]** The system works effectively given all CFA Institute members are held to the same high standards and the compliance and disciplinary procedures are clearly defined.

<u>Our Comments on the Exposure Draft</u>

CFA Societies Australia and CFA Institute have reviewed FASEA's proposed Code of Ethics and make the following general comments.

The proposed Code is principles-based and not rules-based. As a result, relevant providers have a large degree of flexibility in interpreting the proposed standards. To

[1] Please visit https://www.cfainstitute.org/ethics/codes/about-asset-manager-code

[2] Please visit https://www.cfainstitute.org/ethics/conduct/sanctions for additional information on matters related to professional conduct and allegations and violations of the CFA Institute Code and Standards.

prevent misunderstanding and misinterpretation, it is important to provide guidance, including recommended procedures for compliance and examples of the application of the standards to help relevant providers grasp their meaning and fulfill their professional responsibilities effectively. Those resources would also help employers, monitoring bodies and investigative authorities establish policies and procedures for compliance, as well as implementation, monitoring and enforcement of those standards.

The CFA Institute Code and Standards (Appendix I) includes additional ethical standards such as Fair Dealing, Communication with Clients and Prospective Clients, Disclosure of Conflicts, and Priority of Transactions. We believe these are important to raise the standards of ethical behavior and professionalism in the Australian investment management industry. These standards are explained:

- *Fair Dealing [Standard III(B)]* - prevents relevant providers from discriminating against any clients when disseminating investment recommendations or taking investment actions. Fair treatment of all parties helps the relevant providers maintain the confidence of the investing public.
- *Client Communication [Standard V(B)]* - developing and maintaining clear, frequent and thorough communication practices (for example, disclose to clients and prospective clients any significant limitations and risks associated with the investment process and distinguish between fact and opinion in the presentation of investment analyses and recommendations) is critical to providing high-quality financial services to clients.
- *Disclosure of Conflicts [Standard VI(A)]* - once a relevant provider has made full and fair disclosure of all matters that could reasonably be expected to impair their independence and objectivity, the relevant provider's employer, clients and prospective clients will have the information needed to evaluate the objectivity of the investment advice or action taken on their behalf.
- *Priority of Transactions [Standard VI(B)]* - to prevent conflicts of interest, client transactions must take precedence over transactions made on behalf of the relevant provider's firm or personal transactions.

Additionally, the focus of FASEA's proposed Code is on investment professionals in relation to clients but there are other areas such as a duty to the integrity of capital markets that should also be included.

For example, practices such as using material nonpublic information, and distorting prices or artificially inflating trading volumes with the intent to mislead market participants have caused and will continue to cause investors to avoid capital markets because the markets are perceived to be rigged in favour of knowledgeable insiders. Hence, to protect the integrity of capital markets, relevant providers must not engage in insider trading and market manipulation. FASEA is welcome to incorporate any of those standards into its Code. The above can be found in our Code and Standards that deals with the *Integrity of Capital Markets [Standards II (A) and (B)].*

The CFA Institute Standards of Practice Handbook, 11th edition (2014) provides: 1) Guidance, 2) Recommended Procedures for Compliance and 3) Application of the Standard. This could be a useful source of reference for your staff. The Handbook can be downloaded from the CFA Institute website here.

In the proposed Code, some of the standards use vague terms, such as "spirit of the law" (Standard 1), "inappropriate" (Standard 2), "broad effects" (Standard 6), and "hold each other accountable" (Standard 12). Standards 7 and 8 include the term "obtain informed consent" without stating how and how often that consent must be sought. While these Standards are meant to operate alongside laws and regulations that may provide specific guidance on these areas, any additional words of clarification within the document would remove potential ambiguity.

Our recommendation: Such statements should be better defined to avoid misinterpretation or ambiguity.

The enforcement standard (Standard 11) is more procedural than principle-based and sits out of place with the other standards. Nor is it clear what the investigation and discipline procedures from the Code Monitoring Body involve. Standard 11 is vague on details, which would need to be clearly outlined.

Our recommendation: Move Standard 11 to a new section headed "Enforcement of the Code" after the Standards Section. Add additional clarification to let stakeholders such as relevant providers know what the consequences would be if the Code is violated.

FASEA has sought specific feedback on the following:

1. How the Code addresses the consumer detriments that have arisen in financial advice, particularly Standard 2, which is intended to ensure that the advice (or referral or other service) that a consumer gets from an Adviser does not produce inappropriate personal advantage to the Adviser.

Standard 2: [A Relevant provider] Must neither advise, refer, nor act in any other manner, where inappropriate personal advantage is derived by the relevant provider.

The proposed Code includes several fundamental ethical standards and provides relevant providers with a foundation for ethical conduct. The classification of the 12 proposed standards into four categories: standards of ethical behavior, standards of client care, standards of quality process and standards of professional commitment, will help relevant providers better understand the scope of this Code and the expectations of the standards in each category.

With proper guidance, this framework would also greatly help other stakeholders such as employers, monitoring bodies and investigative authorities to design relevant, effective compliance systems to monitor and assess professional conduct.   The combination of Standards 2, 5, and 9 highlight the intention of the proposed Code to protect the interest of clients when receiving financial advice. When advisors avoid personal advantage, provide advice in the client's best interest, and offer products competently in good faith, the financial advice industry will be poised to rebuild its reputation which has been diminished by prior consumer detriments.

A code of conduct is only part of the process of transitioning the provision of financial advice into a true profession. The actions of the relevant providers should also reflect the principles of the proposal, while adhering to effective regulations. Combining a set of high ethical expectations, such as those proposed, with robust regulations provide a solid foundation for a market that works for the benefit of the investing public.

To enhance the scope and impact of the proposed Code, FASEA is welcome to incorporate our Code and Standards into its Code. Several of our standards help to address consumer detriments that have arisen in financial advice. For example:

- *Standard I(B) Independence and Objectivity;*
- *Standard III(A) Loyalty, Prudence, and Care;*
- *Standard III(C) Suitability;*
- *Standard V(A) Diligence and Reasonable Basis; and*
- *Standard VI(C) Referral Fees*

These standards are clearly detailed and would certainly help avoid conflicts of interest between consumers and their advisers if implemented properly. The objective is to help professionals act professionally and ethically when they discharge their professional duties, put their clients' interests first to avoid conflicts of interest and protect their clients' interests with their professional knowledge and skills.

Other issues on which FASEA has sought comment in relation to Standard 2 are:

a) What types of personal advantage are appropriate vs. inappropriate?

Advantages that will create conflicts of interest with clients would be considered as inappropriate personal advantage, which may be financial or non-financial. For example, if a relevant provider has special compensation arrangements with their employer that might conflict with client interests, such as bonuses based on short-term performance criteria, commissions, incentive fees, performance fees, and referral fees, these special compensation arrangements would be considered as inappropriate personal advantage. To avoid conflicts of interest, inappropriate personal benefits should not be accepted.

Where conflicts of interests cannot be avoided, a relevant provider must manage and minimise those conflicts by disclosing the conflicts of interests to clients and employers. Such disclosure would allow clients to make intelligent, informed decisions regarding their relevant provider's advice.

Appropriate personal advantage may be any financial or non-financial benefit that is agreed or approved by clients, such as any gift, benefit, compensation, or other consideration. Certainly, personal advantage derived from client relationships should conform to the policies set up by a relevant provider's employer. For example, if a client agrees to pay a cash bonus to his relevant provider for better-than-expected performance or offers his relevant provider two free basketball game tickets for good service, those cash bonuses and free game tickets would be considered "appropriate" personal advantage if they do not violate the policies established by the relevant provider's employer.

b) ***What might be the unintended consequences of the current draft?***

If different stakeholders do not understand well the requirements of the standard and what personal advantage would be considered "inappropriate", negative consequences may arise, such as disputes between clients and relevant providers, complaints from consumers, and unintended violations of the standard due to misunderstanding or misinterpretation. Confusion in stakeholders' minds between right and wrong or lack of understanding of the standard would also pose operational challenges to stakeholders in setting up policies and procedures for compliance, monitoring and enforcement.

c) How might the Standard be expressed to avoid unintended consequences?

FASEA may consider removing "inappropriate" from Standard 2 and state more specifically the expectations of this standard.

The standard might be expressed as below:

[Relevant provider] Must neither advise, refer, nor act in any other professional manner, where the relevant provider will derive personal advantage that reasonably could be expected to compromise his/her independence and objectivity, as well as his/her loyalty, prudence and care to clients.

It would be essential to define what could be considered appropriate or inappropriate personal advantage. Also, giving practical guidance, including recommended procedures for compliance and examples for application of a standard would significantly help stakeholders prepare and act responsibly.

2. How do the other Standards respond to this type of consideration?

As the other standards are also principles-based, it would be useful and prudent to make the standards as clear as possible. This could be done, for example, by providing guidance and offering education and support to equip financial advisers with sufficient relevant knowledge and skills to understand and meet the requirements of the standards. As mentioned above, Standard 6 states that relevant providers must take into account the "broad effects" arising from a client acting on their advice. This is a very open statement and it may be very challenging for relevant providers to interpret "broad effects" to comply with the standard effectively.

If a standard is too general or too broad, relevant providers may not meet the standard without proper guidance. Similarly, it may pose practical difficulties and operational challenges for other stakeholders to respond to the requirements of the standards in terms of setting up policies and procedures for compliance monitoring and assessment, as well as enforcement. Concepts such as “spirit of the law,” “inappropriate,” “broad effects,” and “hold each other accountable” stated in different standards of the proposed Code are open to interpretation. Terms like this should be removed and replaced with clearer language to avoid unintended consequences.

For example, compared to Standard 1 of the proposed Code, our *Standard I(A) Knowledge of the Law* specifically requires members and candidates to understand and comply with all applicable laws, rules, and regulations of any government, regulatory organisation, licensing agency, or professional association governing their professional activities. Our standard also clearly states that in the event of conflict, members and candidates must not knowingly participate or assist in and must dissociate from any violation of such laws, rules, or regulations.

Accordingly, we provide Guidance, Recommended Procedures for Compliance, and Application of the Standard to help different stakeholders, such as members and candidates, employers, clients, and enforcement professionals to better understand the meaning and expectation of each standard. This guidance and clear statements are essential for effective compliance, monitoring, assessment and enforcement purposes.

Our recommendation: FASEA provides guidance on the application of the proposed Code of Ethics and procedures for compliance and enforcement.

3. The practical application of the proposed Code in terms of:

a) Adviser practice

The requirements of the proposed Code are fundamental to relevant providers’ or advisers’ duties to clients, so they should be able to comply with the proposed Code with a good understanding of the meaning and expectations of each Standard. Again, it would be helpful to provide guidance, including recommended procedures for compliance and examples of application of standards as reference materials.

For example, to fulfil the basic provisions of our *Standard III(C)* which deals with *Duties to Clients*, our members and candidates should put the needs and circumstances of each client and the client's investment objectives into a written investment policy statement (IPS). When preparing the IPS, members and candidates must take into consideration: 1) client identification, such as the type and nature of client, the existence of separate beneficiaries, the portion of total client assets managed by the members and candidates, 2) investor objectives, such as return objectives and risk tolerance, 3) investor constraints, for example, liquidity needs, expected cash flows, investable funds, time horizon, tax consideration, and regulatory and legal circumstances, and 4) performance measurement benchmarks.

Such guidance and recommended procedures for compliance would facilitate communication between clients and advisers, as well as advisers and their employers. If all parties were clear on each standard, it would be easier for relevant providers to comply with the Code.

However, insufficient or lack of educational resources and support would be a stumbling block to relevant providers in the discharge of their ethical duties. So, ethics training and continuing professional development courses would be crucial to the successful application of these standards.

b) ***Licensee practice***

Licensees play important roles in safeguarding the interests of their clients and promoting sound ethical culture to guide the values, attitudes, and behavior of employees in their interaction with clients and other stakeholders. Our *Standard IV* on *Duties to Employers* not only requires members and candidates to protect the interests of their firm, but also specifies employers' duties and responsibilities that they owe to their employees if they expect to have content and productive employees. An employer is responsible for a positive working environment, which includes an ethical workplace. *Standard IV(C)* on *Responsibilities of Supervisors* states that senior management has the additional responsibility of devising compensation structures and incentive arrangements that do not encourage unethical behaviour.

By establishing the appropriate policies, procedures, and systems to monitor, assess, support, and enforce the standards of ethical conduct and professionalism of their employees, the licensees can: 1) strengthen the oversight of employees' professional practices, 2) foster sound ethical culture and conduct in the financial services industry, and 3) enhance its firmwide risk management, such as legal and reputational risks.

Licensee practice should also be in line with the objectives of the proposed Code to ensure that they are not in conflict. To achieve that goal, licensees should not only set up relevant policies, procedures, and compliance systems, but also allocate appropriate educational resources to support their relevant providers to meet the requirements of the Code. So, licensees' knowledge of the values and standards of the Code would be key to guide and support their relevant providers to head in the right direction.

c) Education and support

Education and support are indispensable in ensuring the success of the proposed Code. If stakeholders are engaged in understanding the Code, embracing its spirit, and upholding its principles through education and support, the chances of successful application of these ethical standards would increase significantly.

Also, a well-thought-out education and support framework would: 1) help stakeholders identify what resources should be available to enhance their understanding of different standards, 2) guide relevant providers on how to enrich their relevant knowledge and skills to protect clients' best interest in an ever-evolving market environment due to new investment strategies, changing financial technology, etc, and 3) help employers and regulatory authorities consider what education training and resources should be provided to support the implementation and execution of the Code. Resources such as reference materials, FAQ, live chat, glossary, helpdesk and a customer services hotline would be effective tools to support the practical application of the proposed Code.

CFA Institute offers a wide range of education training and resources on ethical decision making, such as interactive webinars, online game-based course for investment professionals, online short case discussion and live training to our members and the public. FASEA may find them useful for planning its education and support resources. For more information about the CFA Institute ethics education resources, please visit https://www.cfainstitute.org/ethics/ethical-decision-making and https://blogs.cfainstitute.org/marketintegrity/.

d) Compliance requirements

Adequate compliance practices are important to the success of the proposed Code. These include having policies, procedures and systems in place to guide, monitor and assess employees' professional and ethical practices, and enforce the policies are important to the success of the proposed Code. For example, our *Standard V(C)* on *Record Retention* requires members and candidates to develop and maintain appropriate records to support their investment analysis, recommendations, actions, and other investment-related communications with clients and prospective clients. Although the responsibility to maintain records generally falls on the firm rather than individuals, we require members and candidates to archive research notes and other documents, either electronically or in hardcopy, that support their current investment-related communications. Doing so will assist their firms in complying with the requirements for preservation of internal or external records.

Licensees and relevant providers should demonstrate their commitment to the proposed Code by developing and maintaining appropriate records. Record retention is extremely important to show whether licensees and relevant providers have done their duties to act for the clients' best interest and act ethically.

Another common challenge for financial advisers is to avoid and manage conflicts of interest. Our *Standard VI(A)* on *Disclosure of Conflicts* protects investors and employers by requiring members and candidates to fully disclose to clients, potential clients, and employers all actual and potential conflicts of interest. They should disclose special compensation arrangements with employers that might conflict with client interests, such as bonuses based on short-term performance criteria, commissions, incentives fees, performance fees and referral fees. Also, they should disclose any materially beneficial ownership interest in a security or other investment that they are recommending. Full and fair disclosure of conflicts is critical to establishing and maintaining investor confidence.

As mentioned in 3c), education and support are crucial to the success of the proposed Code. Ethics training or education should be considered as a required component of continuing professional development. The ethics training would encourage relevant providers familiar with different ethical principles and professional standards to fulfill their responsibilities and provide them with a tool to handle an ethical dilemma that they may face at work and thus choose the best course of action.

Assessment should also be part of the course requirement to test whether relevant providers have gained a good understanding of ethical behavior and professionalism through their training.

CFA Institute has developed an Ethical Decision-Making (EDM) Framework (Appendix II), which is a tool for analysing and evaluating ethical scenarios in the investment profession. The Identify-Consider-Act-Reflect framework advances a decision-making structure for situations that often fall outside the clear confines of “right” and “wrong”. Neither a linear model nor checklist, the framework provides a summary of the key elements of making ethical decisions. FASEA is welcome to reference the CFA Institute EDM Framework and include it as part of its educational resources.

Our recommendation: Ethics training be required as part of compliance with the proposed Code and educational resources be provided to financial advisers to clarify FASEA's expectations of what constitutes ethical behaviour to comply with the Code.

e) Consumer experience

The proposed Code includes several ethical standards to protect consumer interests and improve the consumer experience in several ways. Under the Code, relevant providers are expected to fulfill their professional duties in a certain manner, for example, act in the best interest of each client when providing financial advice, obtain informed consent to act for agreed services and develop a high level of relevant knowledge and skills. These ethical behaviors and professionalism would be effective ways of managing conflicts of interest and building trust with clients, as well as protecting consumers' interests if implemented correctly.

To mitigate consumer detriment, consumers should be informed of the Code by their service provider and have a good understanding of the Code to maintain clear, frequent, and thorough communication with clients as it is critical to providing high-quality services to them. Accordingly, the clarity of the Code would help different stakeholders such as relevant providers and employers to work cohesively to strengthen their compliance system for robust oversight, risk management and professional development. By helping consumers understand relevant providers' roles and responsibilities, and ensuring relevant providers are doing the right thing, the overall consumer experience would improve.

Conclusion

FASEA has taken a great initiative to develop a Code of Ethics for Financial Advisers to raise the standards of ethical conduct and professionalism in the financial services industry. This effort is well-aligned with our mission to lead the investment profession globally by promoting the highest standards of ethics, education and professional excellence for the ultimate benefit of society.

However, the success of this proposed Code requires a holistic approach to: 1) engage various stakeholders in understanding the Code and recognising its benefits, 2) provide sufficient education and support to improve stakeholders' relevant knowledge and skills and meet the requirements of the Code, and 3) set up adequate compliance practices including policies, procedures and systems to guide, monitor and assess relevant providers' professional and ethical practices and enforce the standards.

We recommend that FASEA examine the CFA Institute Code and Standards so that it may incorporate our detailed and clearly defined ethical standards and avoids some of the ambiguities in the proposed Code. We would be pleased to discuss our comments in greater detail, or to provide any other assistance that would be helpful. If you have any questions, please do not hesitate to contact us at exec@cfas.org.au.

Yours sincerely,

Dr. Tony Tan, CFA
Co-Head of Ethics, Standards and Professional Conduct
CFA Institute

Mr. Ganesh Suntharam, CFA
President
CFA Society Sydney

Mr. Graeme Bibby, CFA
President
CFA Society Melbourne

Mr. Robert Huth, CFA
President
CFA Society Perth

APPENDIX I

CFA Institute

CODE OF ETHICS AND STANDARDS OF PROFESSIONAL CONDUCT

PREAMBLE

The CFA Institute Code of Ethics and Standards of Professional Conduct are fundamental to the values of CFA Institute and essential to achieving its mission to lead the investment profession globally by promoting the highest standards of ethics, education, and professional excellence for the ultimate benefit of society. High ethical standards are critical to maintaining the public's trust in financial markets and in the investment profession. Since their creation in the 1960s, the Code and Standards have promoted the integrity of CFA Institute members and served as a model for measuring the ethics of investment professionals globally, regardless of job function, cultural differences, or local laws and regulations. All CFA Institute members (including holders of the Chartered Financial Analyst® [CFA®] designation) and CFA candidates must abide by the Code and Standards and are encouraged to notify their employer of this responsibility. Violations may result in disciplinary sanctions by CFA Institute. Sanctions can include revocation of membership, revocation of candidacy in the CFA Program, and revocation of the right to use the CFA designation.

THE CODE OF ETHICS

Members of CFA Institute (including CFA charterholders) and candidates for the CFA designation ("Members and Candidates") must:

- Act with integrity, competence, diligence, respect and in an ethical manner with the public, clients, prospective clients, employers, employees, colleagues in the investment profession, and other participants in the global capital markets.
- Place the integrity of the investment profession and the interests of clients above their own personal interests.
- Use reasonable care and exercise independent professional judgment when conducting investment analysis, making investment recommendations, taking investment actions, and engaging in other professional activities.
- Practice and encourage others to practice in a professional and ethical manner that will reflect credit on themselves and the profession.
- Promote the integrity and viability of the global capital markets for the ultimate benefit of society.
- Maintain and improve their professional competence and strive to maintain and improve the competence of other investment professionals.

STANDARDS OF PROFESSIONAL CONDUCT

I. PROFESSIONALISM

A. Knowledge of the Law. 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. In the event of conflict, Members and Candidates must comply with the more strict law, rule, or regulation. Members and Candidates must not knowingly participate or assist in and must dissociate from any violation of such laws, rules, or regulations.

B. Independence and Objectivity. Members and Candidates must use reasonable care and judgment to achieve and maintain independence and objectivity in their professional activities. Members and Candidates 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.

C. Misrepresentation. Members and Candidates must not knowingly make any misrepresentations relating to investment analysis, recommendations, actions, or other professional activities.

D. Misconduct. 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.

II. INTEGRITY OF CAPITAL MARKETS

A. Material Nonpublic Information. 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.

B. Market Manipulation. Members and Candidates must not engage in practices that distort prices or artificially inflate trading volume with the intent to mislead market participants.

III. DUTIES TO CLIENTS

A. Loyalty, Prudence, and Care. Members and Candidates have a duty of loyalty to their clients and must act with reasonable care and exercise prudent judgment. Members and Candidates must act for the benefit of their clients and place their clients' interests before their employer's or their own interests.

B. Fair Dealing. Members and Candidates must deal fairly and objectively with all clients when providing investment analysis, making investment recommendations, taking investment action, or engaging in other professional activities.

C. Suitability.

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

D. Performance Presentation. When communicating investment performance information, Members and Candidates must make reasonable efforts to ensure that it is fair, accurate, and complete.

E. Preservation of Confidentiality. Members and Candidates must keep information about current, former, and prospective clients confidential unless:

1. The information concerns illegal activities on the part of the client or prospective client,
2. Disclosure is required by law, or
3. The client or prospective client permits disclosure of the information.

IV. DUTIES TO EMPLOYERS

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

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.

C. Responsibilities of Supervisors. 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.

V. INVESTMENT ANALYSIS, RECOMMENDATIONS, AND ACTIONS

A. Diligence and Reasonable Basis. 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.

B. Communication with Clients and Prospective Clients. Members and Candidates must:

1. Disclose to clients and prospective clients the basic format and general principles of the investment processes they use 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.

C. Record Retention. Members and Candidates must develop and maintain appropriate records to support their investment analyses, recommendations, actions, and other investment-related communications with clients and prospective clients.

VI. CONFLICTS OF INTEREST

A. Disclosure of Conflicts. 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 employer. Members and Candidates must ensure that such disclosures are prominent, are delivered in plain language, and communicate the relevant information effectively.

B. Priority of Transactions. Investment transactions for clients and employers must have priority over investment transactions in which a Member or Candidate is the beneficial owner.

C. Referral Fees. Members and Candidates must disclose to 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.

VII. RESPONSIBILITIES AS A CFA INSTITUTE MEMBER OR CFA CANDIDATE

A. Conduct as Participants in CFA Institute Programs. 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.

B. Reference to CFA Institute, the CFA Designation, and the CFA Program. 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.

APPENDIX II

THE CFA INSTITUTE ETHICAL DECISION-MAKING FRAMEWORK

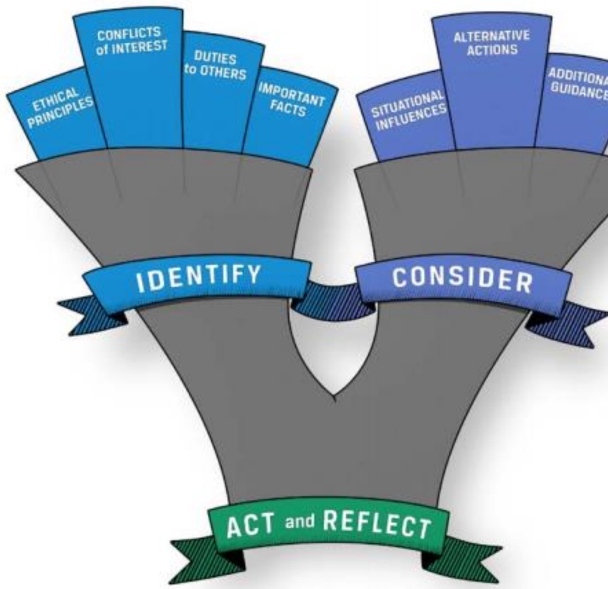
The CFA Institute Ethical Decision-Making Framework is a tool for analyzing and evaluating ethical scenarios in the investment profession. The Identify–Consider–Act–Reflect framework advances a decision-making structure for situations that often fall outside the clear confines of "right" and "wrong." Neither a linear model nor checklist, the framework provides a summary of the key elements of making ethical decisions. The framework is offered with the understanding that there likely will be additional influences, conflicts, and actions unique to each ethical scenario and beyond those detailed below.

IDENTIFY

- ETHICAL PRINCIPLES: Which fundamental investment profession principles—fair dealing, full disclosure, loyalty, or diligence (among others)—are at issue?
- DUTIES TO OTHERS: To whom do you owe a duty—your client(s), employer, colleagues, and/or others? Some duties, such as protecting the integrity of the capital markets, may be more important than others.
- IMPORTANT FACTS: What facts do you know and what additional information do you need to make an informed decision?
- CONFLICTS OF INTEREST: Are there any encumbrances, relationships, or incentives influencing your actions?

ACT

- BY MAKING A DECISION: The specific action required may vary based on the individual aspects of the situation. Your decision may require multiple actions or steps, or none at all.
- BY ELEVATING THE ISSUE TO A HIGHER AUTHORITY: Alternatively, the best course of action may be to elevate your concerns to a more appropriate party. You may remain connected to the scenario, so you may need to follow up with the other individual to ensure appropriate action is taken.



CONSIDER

- SITUATIONAL INFLUENCES: Are outside pressures (such as conformity to group opinion, obedience to authority) or internal biases (such as overconfidence) affecting your decision making?
- ALTERNATIVE ACTIONS: Have you brainstormed multiple solutions and avoided a particular preconceived path?
- ADDITIONAL GUIDANCE: Have you sought the independent, objective assessment of other parties to gain additional perspective?

REFLECT

- ON WHAT YOU'VE LEARNED: Once you have taken action, take the time to review the path taken. The lessons you learn will help you reach ethical decisions more quickly in the future.
- ON STRENGTHS AND WEAKNESSES: Regardless of whether your decisions and actions bring about positive or negative consequences, understanding your strengths and weaknesses will help you make ethical decisions in the future.

CFA Institute

www.cfainstitute.org