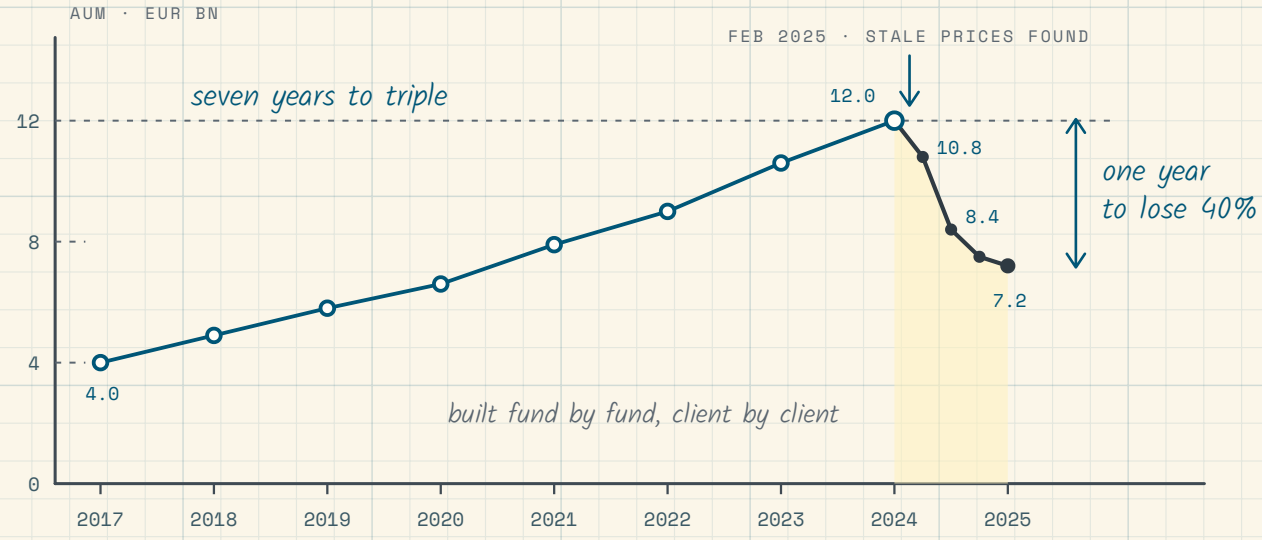
LEARNING GUIDE · CFA® LEVEL I · 2027 CURRICULUM

Ethics and Trust in the Investment Profession

Ethical and Professional Standards, Learning Module 1. One firm, one first-year analyst, one rival that lost its clients' trust: what ethics is, why investing needs so much of it, why good people slip, and four phases for hard calls.

12 decision rules | 14 worked examples | 18 practice questions | 4-phase framework

YEARS TO BUILD, MONTHS TO LOSE — CORVANE ASSET MANAGEMENT · ASSETS · EUR BN



One manager's stale prices: who gained and who paid, Worked 1.1; what it cost the firm, Worked 3.1.

BEFORE YOU START

How to read these notes

The guide follows one firm, Aldmere Capital, and Lena Brandt, a first-year analyst on its bond team and a Level I candidate. A rival, Corvane Asset Management, shows what happens when trust breaks.

fiduciary duty	A term the exam expects you to define and tell apart from its neighbors.
RULE 7	A decision rule. Ethics has no formulas; all twelve rules are on the decision sheet, p. 26.
→ clients first	Reasoning, written out the way you would think it through on exam day.
loyalty	A ringed word: where the trap is hiding.
escalate ✓	The conclusion, double underlined, then a check you can do in ten seconds.
EXAM TRAP	What a wrong option will try to make you believe.

LOS What the curriculum asks of you

- [ ] explain **ethics** · §1
- [ ] describe the role of a **code of ethics** in defining a profession · §1.5, §2.2
- [ ] describe **professions** and how they establish trust · §2
- [ ] describe the need for **high ethical standards** in investment management · §3.1–3.2
- [ ] explain **professionalism** in investment management · §3.3–3.5
- [ ] identify **challenges** to ethical behavior · §4
- [ ] compare and contrast **ethical standards with legal standards** · §5
- [ ] describe a **framework** for ethical decision-making · §6

eight describe-and-explain outcomes: words, not numbers

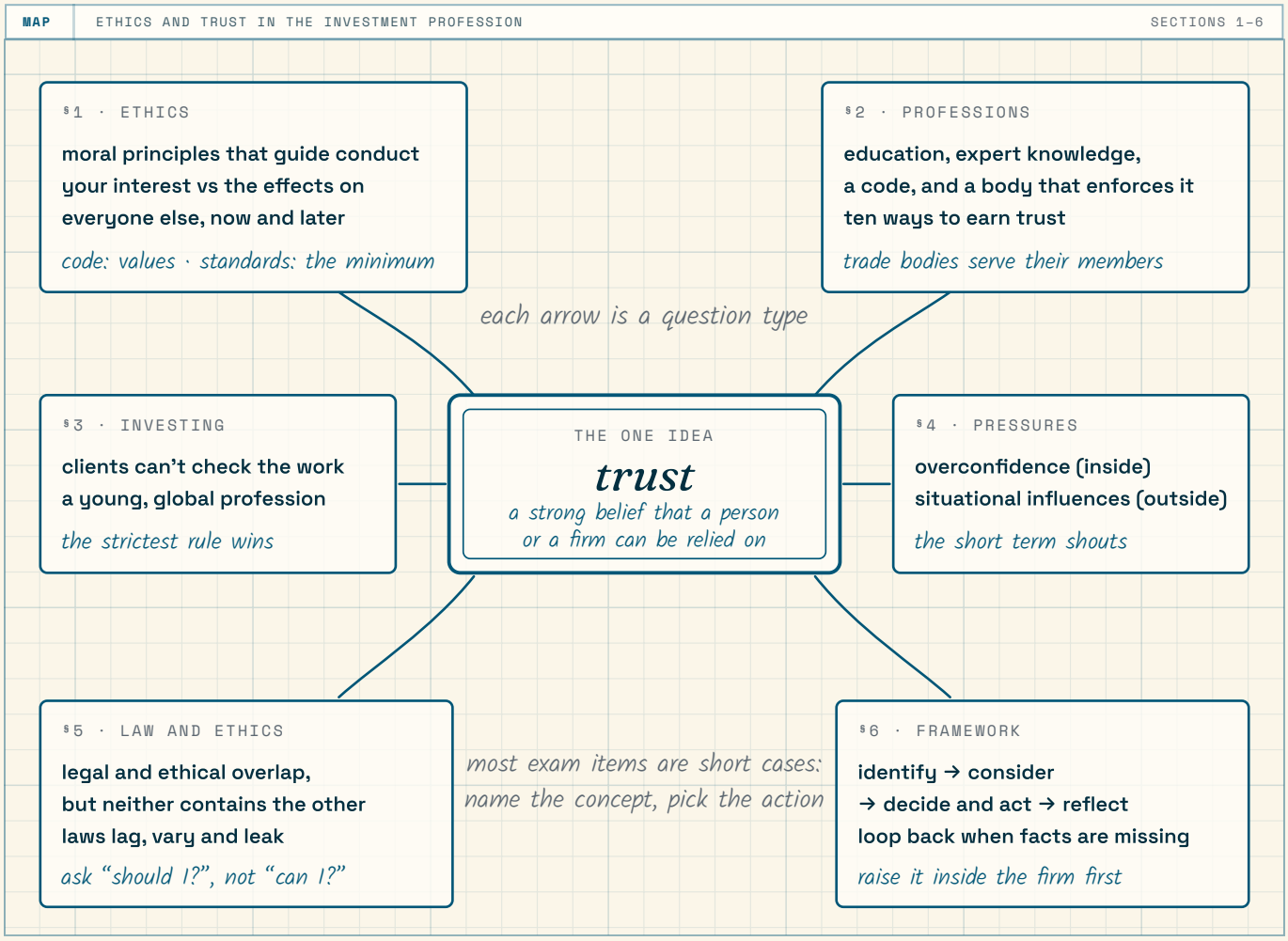
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OVERVIEW

The module on one page

One idea, trust, seen from six sides. Clients hand over their savings to people whose work they can't easily check. Everything in this module is about earning that trust and keeping it.



5 Things to remember

1. Ethics weighs your interest against the effects on **others**.
2. A code states values; standards set the **minimum**.
3. Clients can't check the work, so trust is the product.
4. Pressures around you, more than character, drive lapses.
5. Legal is not always ethical: use the framework.

THE FIRMS ARE FICTIONAL

Aldmere, Corvane, their people and every number about them are invented. CFA Institute, its Code and Standards and its programs are real.

§ 1 · ETHICS

Every decision has other people in it

Ethics is about choices that affect others. In finance, those others are often people you will never meet: fund investors, your clients' families, the market as a whole.

a manager's real product: being believed

Investment firms sell a promise. Savers hand their money to people they rarely meet and expect their interests to be protected. That only works with trust, a strong belief that a person or an institution is reliable. Transparent, open and ethical business practices are what make a manager worth trusting.

WHAT HAPPENED AT CORVANE

Corvane Asset Management grew from €4.0 bn to €12.0 bn in seven years. Its €3.0 bn credit fund held bonds that rarely traded. When their prices fell in 2024, the fund manager kept valuing them at old broker quotes, so the fund looked steady and his bonus stayed safe. The auditors found it in February 2025. Within a year clients had taken out 40% of Corvane's assets, the regulator had fined the firm, and 120 people who had done nothing wrong had lost their jobs.

one person's choice, hundreds of people's problem

1.1 Ethics in one sentence

from the Greek ethos: character

Ethics is a set of moral principles and rules of conduct that guide how we behave. Three building blocks sit underneath. **Beliefs** are what you hold to be true. A **principle** is a basic belief on which a whole system of behavior or reasoning rests. **Values** are what you judge to have worth, and they grow out of your beliefs.

Ethical (moral) principles are beliefs about which conduct is good, acceptable or required, and which is bad, unacceptable or forbidden. They can be one person's own, or shared by a whole community.

1.2 Stakeholders: who else is in the room

A stakeholder is any person or group that a decision could affect, directly or indirectly, and who therefore has a stake in it. For an investment professional the list is long: clients, colleagues, the employer, the communities you live and work in, the profession, trade associations, regulators and everyone else in the financial markets.

One decision can help every stakeholder, help only some, or help some while harming others. And the answer often changes with time.

EXAM TRAP

Stakeholders include those affected indirectly: other investors, the market, the profession, regulators. An answer that names only the client and the firm is usually too narrow.

1.3 Winners now, losers later

Corvane's stale prices looked harmless while nobody knew. Fig. 1.1 follows each stakeholder from the hidden months to the year after the news broke.

FIG. 1.1 WHO GAINED AND WHO LOST CORVANE'S STALE PRICES

	WHILE HIDDEN · 2024	ONCE FOUND OUT · 2025
the fund manager	+ bonus kept	− fired, career over
Corvane, the firm	+ fees kept, inflows	− 40% of assets gone
investors who left early	+ received €12 m extra	+ kept the €12 m
investors who stayed	− carried the €12 m	− repaid late, trust gone
Corvane's other staff	— no change	− 120 jobs lost
other funds, the market	— no change	− every fund doubted
the investment profession	— no change	− less trusted

while hidden: 3 gain, 1 loses · once found out: 1 gains, 6 lose

stale prices don't create the loss: they pick who bears it

WORKED 1.1 Who paid for the stale prices?

given fund net asset value (NAV) €3.0 bn · €600 m of bonds valued at 100, worth 85 · investors redeem €400 m before the news · €m

OVERSTATED $600 \times 15\% = 90 \rightarrow \frac{90}{3{,}000} = 3.0\%$ of the fund's NAV

PAID OUT 400 for units really worth $400 \times 0.97 = 388$

EXCESS $400 - 388 = 12$ ← paid by the investors who stayed

check: 400 × 3.0% = 12 ✓ · the 90 fall happened either way: the stale price only moved €12 m of it from the leavers onto the stayers.

WHY IT MATTERS

Misconduct often shifts value between stakeholders before it destroys any. The short-term winners make it look harmless. The bill comes later, and most of the people who pay it did nothing wrong.

1.4 What makes an act ethical

not "ignore yourself": weigh yourself against everyone else

The study of ethics looks at how consequences and personal character define good conduct. Ethical conduct follows moral principles and balances your own interest against the direct and indirect consequences of your behavior for others. An ethical action passes two tests. It **conforms** to the ethical expectations of society and of the people it touches. And it is **beneficial**: it improves the outcomes for the stakeholders it affects.

Telling a client the true risks and costs of an investment passes both. It is what clients expect, and informed clients decide better, complain less and stay longer, which is good for you and your employer too.

Most communities share five widely recognized principles and build their own rules on top of them:

- honesty
- transparency
- fairness, or justice
- diligence
- respect for others' rights

3-year gap: −1.40 − 2.20 = −3.60 points a year

WORKED 1.2 Two tests for one fund update

given Aldmere Income Fund · 1 year +9.10% · 3 years -1.40% a year, benchmark +2.20% · sales wants the 1-year figure only

EXPECTATIONS — *Clients expect a fair picture of performance. One good year shown alone hides a weak three-year record, with two poor years before it: it fails transparency and honesty.*

BENEFICIAL? — *Maybe more money comes in this quarter. Later come disappointed clients, complaints and lost trust: worse outcomes for clients and for Aldmere.*

DECISION — ***show both periods, with the benchmark*** *both must pass ✓*

EXAM TRAP

"Ethical" is not the same as "allowed". An action can break no rule and still fail both tests. The question is what stakeholders can fairly expect, and whether their outcomes get better or worse.

SEE IT

Ethics is not about ignoring your own interest. Lena may want her fund to sell well. Ethics asks her to weigh that against what it does to the clients reading the update.

1.5 Written down three ways

Groups turn shared principles into rules. The rules take three forms, and the exam expects you to tell them apart.

FORM	WHO SETS IT	WHAT IT DOES
laws and regulations	a governing body: a legislature or a regulator	obligatory and forbidden conduct for everyone in its jurisdiction
code of ethics	a community: an employer, a university, a professional body	a general guide: the group's values and what it expects of members
standards of conduct	the same community, next to its code	specific required behavior: the **minimum** acceptable; clarifies the code

standards are a floor: members may always do more

Members agree to the code and standards when they join, and many communities ask them to confirm it in writing once a year or more often. Codes are displayed prominently to keep them in view and cut the number of violations.

general → code · specific → standard · state → law

WORKED 1.3 Code, standard or law?

given five rules that apply to Lena at Aldmere

RULE	FORM	WHY
"We act with integrity and put clients first."	*code*	a general principle
"Declare any gift worth over €100 within five days."	*standard*	specific, a minimum
"Firms must report suspicious trades to the regulator."	*law*	set by a governing body
"Treat colleagues, clients and rivals with respect."	*code*	a general principle
"Pre-clear every personal trade; hold it 30 days."	*standard*	specific, a minimum

1.6 When a member breaks the code

A violation hurts the whole community: its reputation with clients and the public, and the trust between members, which can split a group from within. To protect its innocent members, the community investigates, repairs what it can, disciplines the violator and, in severe cases, takes away membership.

TRY IT · 60 SECONDS

A rule says: "Analysts must not trade a stock in the ten days before they publish a report on it." Code of ethics or standard of conduct?

answer: a standard: specific, a minimum

§ 2 · PROFESSIONS

What turns a job into a profession?

A profession is an occupation that has organized itself to earn society's trust, and to keep it. Its code of ethics is the public promise.

2.1 A profession, defined

doctors, lawyers, actuaries, accountants, architects, engineers

A profession is an occupational community with its own education, a body of expert knowledge, and a framework of practice and behavior that earns the community's trust, respect and recognition. Its members use their specialized knowledge and skills to serve others. Most professions stress three things: an ethical approach, good service and empathy with the client.

Professions have multiplied over the last century as new areas of expertise appeared. Three groups push for a new one:

GOVERNMENTS, REGULATORS
They want an ethical relationship between experts and society at large.

PRACTITIONERS
They see an advantage in working as recognized professionals.

CLIENTS
They would rather work with professionals than with anyone who claims the skill.

2.2 The role of a code of ethics

the code is a promise made in public

A profession's code of ethics tells the public which principles its members share and how they are expected to behave. That builds confidence that members will use their skills to serve clients and others, not only themselves. Members agree to follow it when they join and, in many professions, confirm it every year.

A code alone guarantees nothing. Some members will break it, so a profession adds standards of conduct to spell it out and a disciplinary process to deal with violations. The code, the standards and the discipline together are what make the promise believable.

EXAM TRAP
A code of ethics does not ensure that every member behaves, and it need not contain detailed standards. Its role is to communicate the shared principles and expected conduct, publicly.

2.3 Profession, guild or trade body?

In most countries, specialists such as doctors and engineers work under some mix of licensed status and technical standards. That sets them apart from the craft guilds and trade bodies many countries also have, in three ways:

	PROFESSION	CRAFT GUILD · TRADE BODY
high ethical standards required of members	yes: the clearest difference	not as a condition
mission	to serve society	to serve its members' trade
conduct rules for practitioners	sets and enforces them	normally does not

supports the industry ≠ sets its standards

Employers, regulators, trade associations and not-for-profit organizations also support an industry, but they are not professional bodies: they generally don't exist to set and maintain professional standards. Many employers still encourage their staff to join the relevant profession, and pay for it, to improve client service and ethical awareness.

three questions: ethics required? serves society? enforces conduct?

WORKED 2.1 Which of these is a professional body?

given four organizations in the news in Lena's first year

ORGANIZATION	WHAT IT DOES	VERDICT
Rhinemark Brewers' Guild	a quality seal for members' beer; protects their trade	*craft guild*
Fund Distributors' Association	lobbies for member firms; runs conferences	*trade body*
Institute of Pension Actuaries	entry exams, a code, yearly learning hours, a disciplinary panel	*profession*
Aldmere Capital	a code and policies for its staff; pays their professional dues	*employer*

THE TEST — *Ethics required of members, a mission to serve society, conduct rules it enforces: only one meets all three.*

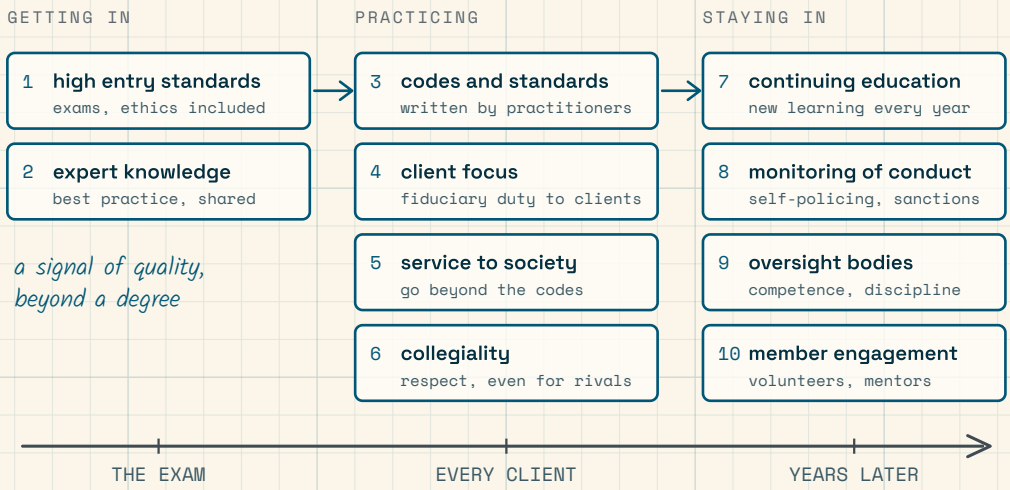
ANSWER — *the Institute of Pension Actuaries — a firm's code binds staff only ✓*

FIDUCIARY DUTY
The obligation to give a high standard of care when acting for someone else's benefit. Professions set it and hold their members to it, and some laws impose it too: the best-interest standard of §5.4. Employers and trade bodies support an industry but don't exist to set such standards.

2.4 Ten ways professions earn trust

A profession's first goal is credibility: the trust of clients and of society. No single feature delivers it. Professions combine ten, which together follow a member from the first exam to the last working year.

FIG. 2.1 TEN TRUST-BUILDERS, FROM ENTRY TO A WHOLE CAREER COMMON TO MOST PROFESSIONS



#	TRUST-BUILDER	WHAT IT MEANS IN PRACTICE
1	**high entry standards**	a promised standard of service, beyond a degree
2	**expert knowledge**	built by skilled practitioners, open to all members
3	**codes and standards**	normalize behavior; more detail than regulation
4	**client focus**	clients and the profession come before oneself
5	**service to society**	raise standards, widen access, support the economy
6	**collegiality**	respect for others' rights and dignity, even rivals'
7	**continuing education**	new learning every year: skills and rules change
8	**monitoring of conduct**	members held to account: self-regulation, sanctions
9	**oversight bodies**	often not-for-profit; track competence, discipline
10	**member engagement**	volunteering, mentoring, shaping the shared values

earned trust buys freedom: less outside control, more self-governance

The ten reinforce each other. Continuing education, usually a yearly requirement of learning hours, keeps entry-level competence from fading; training also adds to human capital, which helps economic growth and social mobility. A profession that earns the community's trust gains more than pride: it may win more freedom from regulators to run its own affairs.

read the verb: expels, must pass, must log…

WORKED 2.2 **Name the trust-builder behind each headline**

given five news items from the Institute of Pension Actuaries' members' letter

HEADLINE	TRUST-BUILDER
"Institute expels a member who misused client money"	*8 · monitoring of conduct*
"New members must now pass three exams, one on ethics"	*1 · high entry standards*
"From next year, members must log 30 learning hours"	*7 · continuing education*
"120 senior members volunteer to mentor first-years"	*10 · member engagement*
"Practitioners update the body of knowledge every 3 years"	*2 · expert knowledge*

2.5 Professions keep evolving

No profession stands still. Demands for transparency and public accountability force it to adapt, technology opens new services and new ways of working, and some of its key processes may be reviewed by a government agency or an independent public body. Professions also involve non-members, such as clients and the public, when they set policy or run disciplinary cases, which builds trust in how they police themselves.

some medical bodies: 500+ years old, still adapting

Even the oldest professions must keep changing, just like the much younger investment profession. Society may recognize an occupation as a profession before it meets every expectation, and new gaps open as expectations rise. Good professions learn from each other, above all on ethics: a new standard in accounting can shape one in investment management.

EXAM TRAP

Recognition is not perfection. A field can be a profession while some of the ten trust-builders are still missing or patchy: few professions implement all of them fully.

TRY IT · 60 SECONDS

A body runs a tough entry exam and publishes a code, but never asks members to keep learning. Which trust-builder is missing, and what is the risk?

answer: 7 · skills fade after entry

§ 3 · INVESTMENT MANAGEMENT

A business built on trust

Clients hand over their savings and can't easily check the work. That gap is why investment management needs higher ethical standards than most trades.

3.1 Clients can't see what you see

the wider the knowledge gap, the more the client must trust

Like doctors and lawyers, investment professionals are trusted to apply a body of formal knowledge with care and judgment. They are expected to know far more than their clients: about finance, about technique, and about the laws and regulations that apply.

Clients may not fully see the **conflicts of interest, risks and fees** involved. So the professional must handle all three, and disclose them fully, in a way that serves the client's best interest. That is why following codes of ethics and professional standards is essential here, and why practice must be guided by care, transparency and integrity.

CONFLICTS
Whose interest does this product serve: the client's, the firm's or the adviser's?

RISKS
What can go wrong, and how badly? Clients often can't judge it alone.

FEES
Small percentages, large sums over time: Worked 5.2.

3.2 Trust is worth money, to clients and to society

In developed economies the profession shapes savings, retirement planning, and the pricing and allocation of capital. Skilled analysis of securities sends capital to its best uses and, with ethical corporate governance, helps attract investors from abroad. Higher trust and better capital allocation cut transaction costs and help clients reach their goals. That is why practitioners, clients, regulators and governments all support a professional investment industry.

lost trust: revenue down, costs up

When trust breaks, a firm pays twice. Revenue falls, because clients leave and new ones don't come. Costs rise, because regulators investigate, lawyers bill and fines arrive. Corvane's numbers are on the next page.

EXAM TRAP
Disclosure is not the whole duty. Telling a client about a conflict, a risk or a fee is required, but you must still handle each one in the client's best interest.

€12 m of compensation: Worked 1.1's loss to the stayers, made good

WORKED 3.1 The price of lost trust at Corvane

given assets €12.0 bn → €7.2 bn · fees 0.70% of assets a year · running costs €60 m → €48 m after job cuts · €m

one-off investigation and lawyers 9 · regulator's fine 15 · investor compensation 12

REVENUE $12{,}000 \times 0.70\% = 84.0 \rightarrow 7{,}200 \times 0.70\% = 50.4$ −40%

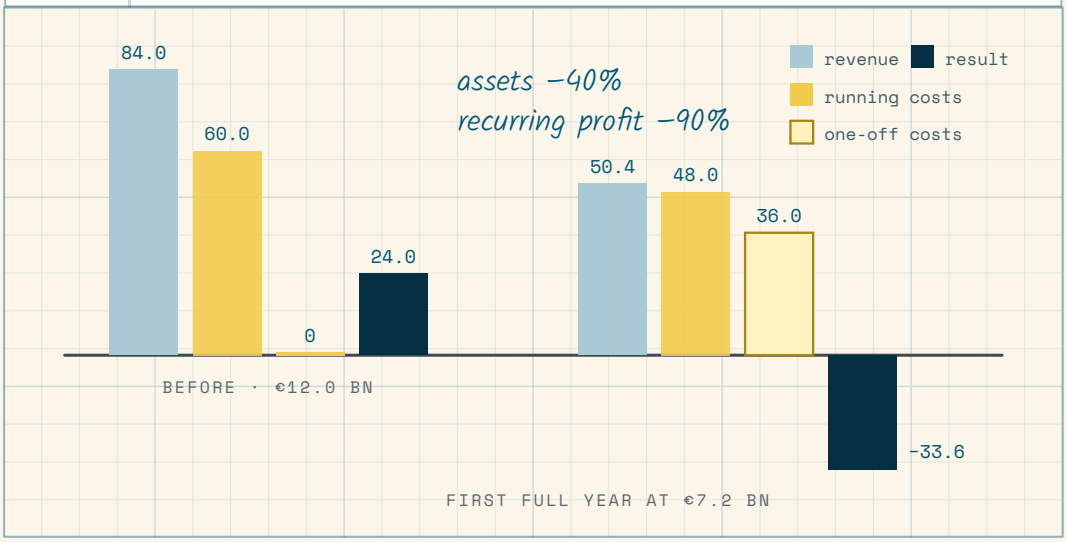
RECURRING PROFIT $84.0 - 60 = 24.0 \rightarrow 50.4 - 48 = 2.4$ −90%

ONE-OFF COSTS $9 + 15 + 12 = 36$

FIRST FULL YEAR $2.4 - 36 = \mathbf{-33.6}$ a loss, from a profit of 24.0

check: revenue fell 40% but running costs only 20%, so recurring profit fell 90%.

FIG. 3.1 REVENUE DOWN, COSTS UP — CORVANE · EUR M A YEAR



SEE IT

Lost trust hits both lines at once: fewer clients, then investigators, lawyers and fines. And running costs can't be cut as fast as clients leave, which is why a 40% fall in assets cost Corvane 90% of its recurring profit.

3.3 A young profession, still growing up

Investment management is a relatively young profession. Public understanding of its practice and its codes is still developing, and recognition by regulators and employers lags behind older professions such as medicine and law.

licensed to practice ≠ member of a professional body

Not everyone in the industry is a professional. Some practitioners have no specific investment training and belong to no professional body, and not all of them are committed to high ethical standards. That makes trust harder to earn for the field as a whole.

The foundations still go back decades: Graham and Dodd's *Security Analysis*, published in 1934, was an early milestone for a shared body of investment knowledge. Today the profession meets most, but not all, of the expectations of a profession. In most countries some certification or license is needed to practice, but joining a professional body often is not. The global trend is to require examined entry and maintained competence. Like every profession, it is still on the way.

ALREADY IN PLACE

- a body of knowledge, built over decades
- codes and standards from professional bodies
- licensing or certification to practice
- a trend toward examined entry

STILL CATCHING UP

- membership is often optional
- public understanding of the practice
- recognition by regulators and employers
- practitioners with no investment training

3.4 Global, and tied to the firms

three drivers: open markets, regulators working together, technology

The profession has gone global as capital markets opened up around the world. Professionals take cross-border roles or move between offices of multinational managers, helped by regulatory coordination across borders and by technology. Professional bodies have grown up in many countries, several have expanded internationally, and actuarial and accounting bodies count investment professionals among their members too.

The profession and investment firms depend on each other to keep trust. Employers and regulators have their own standards and practices, which may differ from those set by professional bodies. Professional bodies typically tell their members how to resolve such differences: for CFA Institute, the answer is on the next page.

§ 3 · INVESTMENT MANAGEMENT

3.5 CFA Institute, the largest professional body

beyond North America in the 1980s; public-company governance since 2015

CFA Institute is the world's largest body for investment management professionals. Its mission is to lead the profession worldwide by promoting the highest standards of ethics, education and professional excellence, for the ultimate benefit of society. Its Code of Ethics and Standards of Professional Conduct promote the integrity of charterholders and set a model for ethical behavior.

WHAT IT ASKS OF MEMBERS AND CANDIDATES

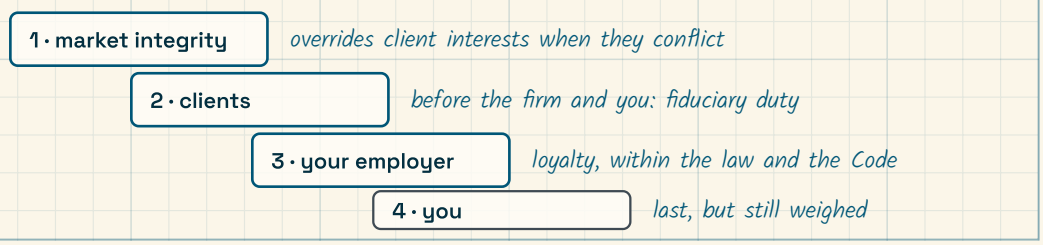
- follow the Code and Standards, and sign a statement every year saying so
- meet the **highest** of its, regulators' and employers' standards
- keep improving their competence, and help others improve theirs

WHAT IT DOES

- body of knowledge (GBIK, CBOK) kept current by practice analysis
- CFA Program exams test core competencies
- research: Financial Analysts Journal, Research Foundation
- local societies: continuing education, events

Where client interests and market interests conflict, the Code and Standards make **market integrity** the overriding duty. Its advocacy serves the same goal: it calls for regulation that aligns the interests of firms with those of their clients.

FIG. 3.2 WHOSE INTERESTS COME FIRST — WHEN DUTIES CONFLICT



legal is only the floor

WORKED 3.2 Whose rule wins?

given at dinner, Lena hears of a takeover to be announced on Monday · local law doesn't ban trading on it · Aldmere's policy covers staff accounts only · her brother asks her to buy for his account

THE LAW — *No ban: legal. But the law is only the floor.*

ALDMERE — *Staff accounts only: her brother's account slips through the gap.*

THE CODE — *CFA Institute treats trading on material nonpublic information as unethical, and its Standards bar causing others to trade on it.*

DECISION — *Meet the highest of the three: no trade, and no tip — strictest wins ✓*

§ 4 · PRESSURES

Good people, bad calls

Most ethical lapses aren't planned by villains. They come from overconfidence and from pressures that people fail to notice.

studying ethics = rehearsing the unfamiliar

Professionals mostly mean well, so why study ethics? Because careers bring unfamiliar situations where the right course isn't obvious, or where more than one choice looks acceptable. Ignore the challenges below and you risk poor decisions, unintended consequences and, for members and candidates, violations of the Code and Standards.

4.1 Overconfidence: "I would never do that"

Ask people to rate their own ethics and most say they are above average, which can't be true of everyone. This is overconfidence, a **behavioral bias**: a tendency to behave in a way that is not strictly rational, because beliefs and emotions get in the way of reasoning. We overestimate how ethically we will act, above all in situations we have never faced, and skip inputs that a good decision needs.

character is not a shield

Overconfidence also makes us lean on internal traits and motives: "I'm honest; I wouldn't lie." Yet studies find that internal traits are generally not the main factor in whether someone behaves ethically in a given situation. The situation is.

4.2 Situational influences: the pull you don't notice

Situational influences are external factors, such as the environment or the culture around you, that shape thinking, decisions and behavior. Decision makers often fail to notice them, or badly underestimate them.

the setting can make people better, too

Experiments in social psychology show that good people with honorable motives can be led into unethical acts in difficult situations, and that even self-described independent thinkers bend to social pressure. In the **bystander effect**, people are less likely to help in an emergency when others are around. The pull works both ways: people behave more ethically when they think someone is watching, or even when a mirror is nearby. Learning to recognize these influences is critical to deciding well.

EXAM TRAP

Overconfidence is an internal trait. Money, prestige and loyalty are situational influences. If a question asks which is "internal", the answer is the bias, not the bonus.

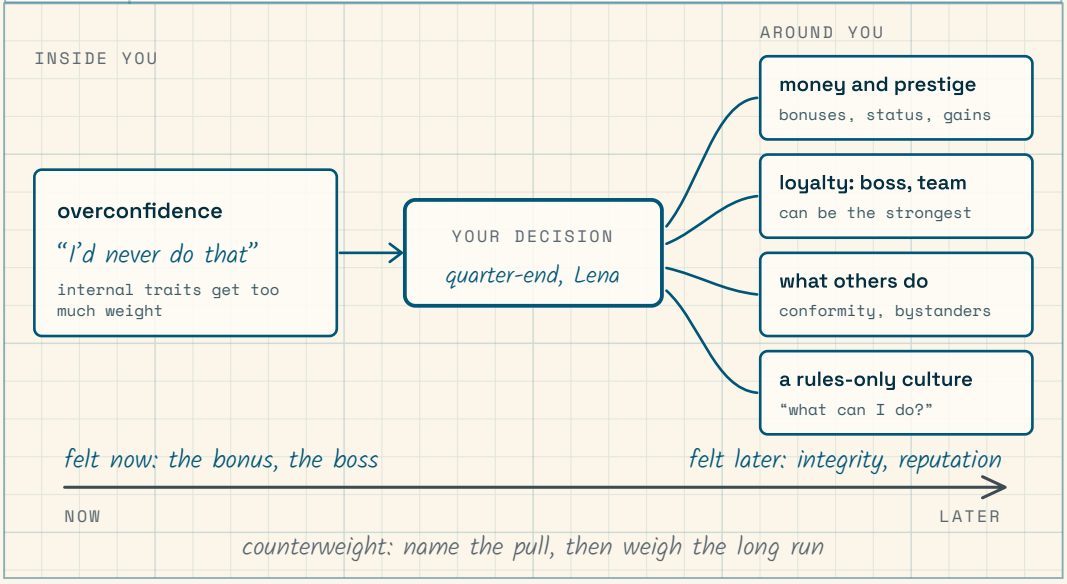
4.3 Money, prestige and loyalty

large rewards pull hardest on short-term thinking

Two common influences in finance are **money and prestige**. Experiments find that just mentioning money makes people less cooperative. Large rewards, such as salaries, bonuses and investment gains, can lead honest people to chase their own short-term interest and ignore the risks to themselves and others, short term and long term.

Loyalty is extremely powerful too: to a supervisor, the firm or colleagues. It can push people into compromises they would reject in another setting, or judge harshly in someone else. Colleagues can pull either way. Some may have urged you to sign up for the CFA Program; others, not bound by the Code and Standards, may urge conduct that is legal locally but falls short of it.

FIG. 4.1 WHERE THE PULL COMES FROM — ONE DECISION, FIVE PRESSURES



4.4 Why the short term wins

long-term costs are real, just quiet

Bonuses, promotions, prestige and loyalty get more weight than they deserve because the brain spots them faster than long-term considerations, such as your own integrity and the integrity of the markets. Those matter just as much, but their consequences feel distant, so they are easy to leave out. The narrower and shorter the focus, the more you overlook long-term risks and costs, to you and to others, and the likelier a lapse. Consciously weighing long-term consequences is the counterweight.

EXAM TRAP

A big bonus is a strong pull, but not always the strongest. Loyalty to the colleagues you work beside every day can outweigh money.

§ 4 · PRESSURES

4.5 When compliance becomes the blind spot

rules answer "can I?"; ethics asks "should I?"

Well-meaning firms build strong compliance programs to make staff follow rules, regulations and policies. That is a good start to an ethical culture, but a focus on rules alone may not be enough. It can oversimplify decisions and hide the larger picture. Taken to the extreme, it becomes one more situational influence: staff adopt a "check the box" mindset and ask **"What can I do?"** instead of **"What should I do?"**

first name the pressures; Lena's choice comes in §6

WORKED 4.1 Lena's quarter-end: name the pressures

given quarter-end valuation · Income Fund 0.25% behind the top quartile · the team's bonus pool grows with the ranking · Ines, the manager who hired Lena and writes her first appraisal, wants an old bond quote kept · a colleague: "we always do it this way" · Lena: "I'd spot real wrongdoing"

WHAT LENA HEARS OR THINKS	KIND	WHICH PULL
a bonus pool that grows with the ranking	situational	*money*
Ines hired her, writes her appraisal, wants the old quote	situational	*loyalty*
"we always do it this way"	situational	*what others do*
"I'd spot real wrongdoing"	internal	*overconfidence*

ANSWER — *three situational, one internal* — only one is about herself ✓

allowed by policy ≠ right

WORKED 4.2 Allowed, but right?

given a bond issuer invites Aldmere's credit team to dinner and a concert, €230 a head, one week before the team decides whether to buy its new bonds · the firm's gift limit is €250

CAN I? — *€230 is under the €250 limit: allowed, once declared (it is over €100, Worked 1.3).*

SHOULD I? — *The timing ties the gift to a live decision. It could sway the team's judgment, or look to clients as if it did.*

OPTIONS — *decline · go after the decision, which can still look like a reward · go, with Aldmere paying its own way*

DECISION — *decline, or let Aldmere pay its own way* — should, not can ✓

TRY IT · 60 SECONDS

A new analyst says: "I'm honest, so the firm's gift procedures don't really apply to me." Internal trait or situational influence?

answer: internal: overconfidence

§ 5 · LAW AND ETHICS

Legal and ethical are not the same

Laws write down many ethical expectations. But some legal acts are unethical, some ethical acts are illegal, and the law usually arrives late.

5.1 Where they agree

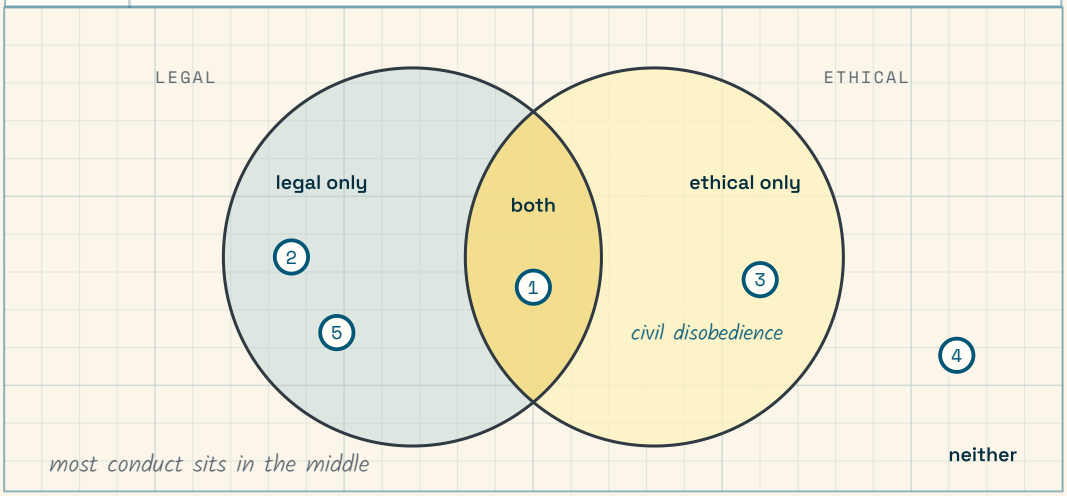
here, compliance is the ethical act

Stakeholders often share ethical expectations, and laws and regulations often write down conduct that leads to better outcomes for society: telling the truth, and making specific written disclosures in marketing materials. Take the risk warnings regulators require in fund documents. Following them means clients invest knowing the risks, so fewer complain or sue when prices fall, and regulators have less reason to investigate, charge or sanction you and your employer. Both protect your reputation and your future. Complying here is ethical: it is beneficial and it meets stakeholders' expectations.

5.2 Where they part

Much conduct is both legal and ethical, but some is one and not the other. Different stakeholders may also judge the same act by different criteria. Fig. 5.1 shows the four zones; the numbered dots are the acts of Worked 5.1.

FIG. 5.1 TWO CIRCLES, FOUR ZONES — TYPES OF CONDUCT



"legal here" is not "ethical everywhere"

Legal but unethical: some countries have no law against trading while in possession of material nonpublic information, yet many investment professionals and CFA Institute consider it unethical. **Ethical but illegal:** civil disobedience, such as a peaceful protest against a law seen as unjust, can be ethical and still break local law. Whistle-blowing, disclosing dishonest, corrupt or illegal activity by an organization or a government, may break the employer's policies or even local laws, yet many consider it ethical.

two questions per act: legal here? ethical?

WORKED 5.1 **Place it on the map**

given five acts, the dots in Fig. 5.1

#	ACT	ZONE
1	Aldmere prints the regulator's risk warning on every fund factsheet	both
2	a trader buys ahead of an unannounced takeover, where no law bans it	legal only
3	an employee leaks proof of fraud to the press, breaking a local secrecy law	ethical only
4	Corvane's manager values bonds at prices nobody would pay	neither
5	where only suitability is required, an adviser picks the costlier of two otherwise identical suitable funds, because it pays a higher commission	legal only

ANSWER 1 both · 2, 5 legal only · 3 ethical only · 4 neither

5.3 Why the law is not enough

Some argue that more regulation and monitoring would build trust in markets. Sometimes it does, but law is not always the best tool against unethical behavior:

1. **Laws follow practice.** Regulators act ahead of problems they foresee, or react after a crisis or large losses.
2. **They take time.** Meanwhile the practice goes on, or grows.
3. **New laws can be vague, conflicting or too narrow,** and closing one gap can open another, similar one.
4. **Laws differ across jurisdictions,** so questionable practices move to places without a relevant law.
5. **Laws are interpreted.** Some participants read them in the way that suits them best, or delay compliance.

no algorithm: judgment

So laws and regulations can't, on their own, ensure ethical behavior. Ethical conduct goes beyond what is legally required, to what communities, professional bodies included, consider right. It takes judgment, the ability to make considered decisions and reach sensible conclusions, because no formula always yields the ethical course. Good judgment weighs the interests of all stakeholders, tries to benefit as many as possible, and limits risks, reputational risk included.

> **EXAM TRAP**
> Wrong options love to say that regulators move quickly, or that more regulation is the best cure for unethical behavior. The module says the opposite: laws lag, and a new law can open the door to a different but similar problem.

§ 5 · LAW AND ETHICS

5.4 Two legal standards for advice

different laws, different beliefs

Laws differ because beliefs and values differ. Some countries require advisers to act in their clients' **best interest**. Others require only that what they recommend be **suitable**. Both can apply in one country, with some advisers held to each.

	BEST-INTEREST (FIDUCIARY) STANDARD	SUITABILITY STANDARD
whose interest first	the client's, always ahead of the adviser's and the employer's	the product must fit the client
before advising	learn the client's goals and risk tolerance; research several options	know enough to judge fit
what to recommend	the option most suitable for the client's long-term goals	any suitable option, even if a similar one costs less
afterwards	monitor the client and the investments: still the best option?	judged when the advice is given

0.90% a year, compounded for ten years

WORKED 5.2 One client, two legal standards

given €200,000 for 10 years · two bond funds, equally suitable, both expected to earn 4.00% a year before charges · fund X charges 1.30% a year, fund Y 0.40%

NET RETURN — X: 4.00 − 1.30 = 2.70% · Y: 4.00 − 0.40 = 3.60%

AFTER 10 YEARS — X: $200{,}000 \times 1.027^{10} = 261{,}056$

Y: $200{,}000 \times 1.036^{10} = 284{,}857$

COST OF X — $284{,}857 - 261{,}056 = \mathbf{23{,}801}$ ← 11.9% of the €200,000

VERDICT — *Recommending X is legal under suitability. A best-interest adviser, comparing the options, recommends Y.*

EXAM TRAP

Under a suitability-only rule it is legal to recommend a suitable product even when a similar, cheaper one exists. Legal, yes: but it is the "legal only" zone of Fig. 5.1.

TRY IT · 60 SECONDS

A new rule caps entry fees on funds. Within months, firms add a new "account set-up" charge instead. Which weakness of law is this?

answer: closing one gap opens another

§ 6 · FRAMEWORK

Four phases for the hard calls

Rules run out and good intentions lose to pressure. A framework slows you down, shows you the whole situation, and leaves you with a decision you can explain.

6.1 Why judgment needs a method

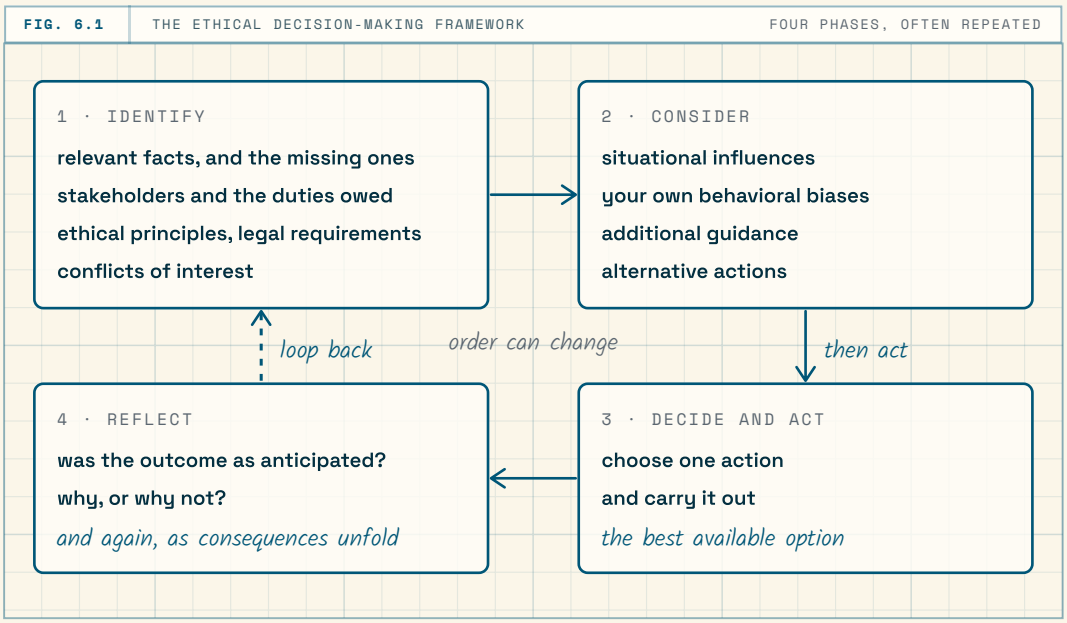
Laws, regulations, professional standards and codes of ethics all guide behavior, but individual judgment is what turns them into principled choices. Firms raise trust by building ethics into everyday decisions, which strengthens both the ability and the motivation of their people to act ethically.

culture is set at the top

Culture comes first. A culture of integrity, built, kept up and shown by senior management, may be the single most important factor in ethical behavior at a firm. A clear code of ethics is the critical first step, but it is not enough: good intentions alone can't carry hundreds of daily decisions made amid conflicts and the urge to protect yourself. Ethical decision-making is a skill, and analysts build it the way they build any other: by working real cases, again and again.

Professionals are used to judging a decision by its profit or loss. The framework adds the ethical view. Without settled principles, a decision that touches many stakeholders can stall, or drift into misconduct that wrecks public trust.

FIG. 6.1 THE ETHICAL DECISION-MAKING FRAMEWORK — FOUR PHASES, OFTEN REPEATED



fresh eyes: someone outside your pressures

Guidance is a critical step: it shows you the situation from other perspectives. Pick at least one adviser who doesn't share your situational influences and biases. If a concern has to be raised, a senior person inside the firm is usually the right first stop: it opens the way to an independent internal review.

§ 6 · FRAMEWORK

6.2 Phase by phase

1 · IDENTIFY

- the important **facts** you have, and the ones you lack but would like
- facts kept apart from opinions, judgments and biases
- **stakeholders** (clients, family, colleagues, employer, market participants) and the **duties** you owe each
- relevant **ethical principles** and legal requirements
- **conflicts of interest**, including conflicting duties: to a client and to your employer, say

2 · CONSIDER

- **situational influences** and your own **behavioral biases**: wanting to please the boss, look successful, be accepted, earn a bonus
- **additional guidance**: a family member, colleague or mentor; compliance; outside legal counsel; firm policies; the Code and Standards
- someone free of your pressures, perhaps outside the firm
- how an ethical peer or role model would act
- **alternative actions**

3 · DECIDE AND ACT

- choose the action that best fits your duties and principles
- if no option is fully acceptable, take the best one available
- carry it out, and be ready to explain and justify it

4 · REFLECT

- was the outcome as anticipated? why, or why not?
- had you found every fact, stakeholder, duty, conflict and principle? weighed the influences and your biases? sought enough guidance? compared enough alternatives?
- reflect again as longer-term consequences appear

6.3 It loops, and it may not end neatly

The process is often iterative, and you may move between the phases in a different order. After identifying the facts and considering the influences, you may find you can't decide without more information. You might seek guidance on how to get it, sketch alternatives based on what you expect it to show, or wait, reflect on what you have learned and start again. Several rounds may show that no fully acceptable answer exists. The framework then helps you find the best decision available.

§ 6 · FRAMEWORK

6.4 What the framework does for you

- shows the situation from several perspectives, including those a short-term, self-focused view misses
- leads to plans less likely to harm stakeholders and more likely to benefit them
- helps you explain and justify the decision to a wider audience
- used consistently, builds judgment and avoids decisions with unanticipated ethical consequences
- ties the code of ethics to real decisions: it brings the code to life
- works for every decision, not only for obvious dilemmas

It guarantees no particular outcome. It makes an unethical decision less likely.

6.5 Lena's quarter-end, worked through

back to Worked 4.1

On the last Wednesday of the quarter, Lena updates the valuation file of the €850 m Aldmere Income Fund. One holding, €34 m face value of Hollin Ports bonds, hasn't traded for three months. The file still carries it at 97.0, a broker quote from last month. Two dealers quote 88.5 and 89.5 today. Ines Vogt, the fund manager who hired Lena, tells her: "Dealers are panicking. Leave it at 97; it will bounce back."

> SEE IT
> *Corvane's 3.0% hole in Worked 1.1 began the same way: one stale quote that nobody questioned.*

facts, then the facts you still need

WORKED 6.1 Phase 1: identify

given €34 m face · file price 97.0 · quotes 88.5 and 89.5 · fund €850 m, 0.25% behind the top quartile

THE GAP	$34 \times (97.0 - 89.0) / 100 = 2.72$
SHARE OF NAV	$\frac{2.72}{850} = 0.32\%$
FACTS	*The price is a month old. Today's quotes average 89.0. At 89.0 the fund falls to 0.57% behind the top quartile.*
MISSING	*What the valuation policy says · any trades or a third quote · Ines's evidence for a rebound*
OPINIONS	*"Dealers are panicking", "it will bounce back": views, not facts.*
STAKEHOLDERS	*Investors buying or selling units this week, those who stay, Aldmere, Ines and the team, Lena, the market.*
PRINCIPLES	*Honesty, objectivity, fairness to every investor; loyalty to the employer, within ethical limits.*
CONFLICT	*a fair price for investors vs loyalty and the bonus*

§ 6 · FRAMEWORK

an outside view found the missing fact: loop back

WORKED 6.2 Phase 2: consider

given Lena's notes from Worked 6.1 · the valuation file closes on Friday

INFLUENCES	*Loyalty to Ines, her first appraisal, the team's bonus pool, "we always do it this way", being new.*
HER BIAS	*Overconfidence: she could be wrong either way, so her own view is not enough.*
GUIDANCE	*Without naming the bond, she calls a mentor from her local CFA society, outside Aldmere and its pressures. The mentor asks: "Who signs off a price that ignores today's quotes?"*
BACK TO 1	*Lena doesn't know: a missing fact. Compliance tells her that after 30 days without a trade the price is the average of two dealer quotes, and any override needs the valuation committee.*
ALTERNATIVES	*(a) keep 97 · (b) change it to 89 herself · (c) ask Ines for evidence, then take it to the valuation committee · (d) go straight to the regulator or the press*

inside first: the firm gets the chance to fix it

WORKED 6.3 Phases 3 and 4: decide, act, reflect

given alternatives (a)–(d) from Worked 6.2

DECIDE	*(a) breaks the policy · (b) isn't her call · (d) skips the firm's own review → (c)*
ACT	*Ines offers no evidence beyond a hunch. Lena tells her what she will do, then sends the committee a short, factual note: the quotes, the policy, the 0.32%.*
OUTCOME	*The committee prices the bonds at 89.0 and reminds the team of the override rule. The fund ends the quarter in the second quartile.*
REFLECT	*As expected? The friction, yes: Ines was cool for a week. The support, no: the committee thanked her. Next time she will ask compliance first.*

check: three months later the bonds trade at 86.0. The stale 97.0 would have overpaid every investor who left in between.

TRY IT · 60 SECONDS

Suppose Ines had refused and the committee had backed her without evidence. Which phase would Lena return to, and whom might she ask next?

answer: consider; compliance, a mentor

TOOLKIT · DECISION SHEET

12 decision rules

Decision sheet

RULE 1 Two tests for an ethical act §1.4

It conforms to stakeholders' ethical expectations, and it is beneficial: it improves their outcomes. Legal or profitable is not enough.

RULE 2 Count every stakeholder, now and later §1.3

Weigh direct and indirect effects on clients, colleagues, the firm, the market and the profession. Short-term winners can hide long-term losers.

RULE 3 Code, standards, law §1.5

A code states values and expectations. Standards of conduct set specific, minimum behavior. Laws come from a governing body.

RULE 4 What makes a profession §2.3

Education, expert knowledge and an enforced framework of conduct. High ethical standards set it apart from guilds and trade bodies.

RULE 5 Disclose what clients can't see §3.1

Conflicts, risks and fees: handle them, and disclose them fully, in the client's best interest.

RULE 6 Clients before the firm and yourself §2.3, §3.5

Fiduciary duty: a high standard of care when acting for someone else's benefit.

RULE 7 The strictest standard wins §3.5

Meet the highest of the law, your employer's policy and the CFA Institute Code and Standards.

RULE 8 Market integrity first §3.5

Where client interests and market integrity conflict, the Code and Standards make market integrity the overriding duty.

RULE 9 Distrust "I would never" §4.1

Overconfidence is an internal trait. The situation, more than character, drives lapses.

RULE 10 Name the pull, weigh the long run §4.3–4.4

Money, prestige and loyalty push short-term thinking. Weighing long-term consequences offsets them.

RULE 11 Ask "should I?", not "can I?" §4.5, §5

Compliant or legal is not the same as ethical. Laws lag, vary across borders and leak.

RULE 12 Identify, consider, decide and act, reflect §6

Loop back when facts are missing. Seek guidance from someone outside your pressures. Raise a concern inside the firm first.

Boxed in pen: the six rules that decide most short cases. Ethics has no formulas; these replace the formula sheet.

TOOLKIT · DEFINITIONS

Say it precisely

Definitions

Behavioral bias — A tendency to behave in a way that is not strictly rational, because beliefs and emotions interfere with reasoning.

Beliefs — What a person holds to be true; they shape values.

Best-interest standard — A legal duty to put clients' interests first and recommend the most suitable option; a fiduciary standard.

Bystander effect — People are less likely to help in an emergency when others are present.

Civil disobedience — Breaking a law seen as unjust, e.g., a peaceful protest: possibly ethical, yet illegal.

Code of ethics — A community's written principles, values and expected behavior; a general guide that members agree to follow.

Compliance culture — A rules-first focus that can oversimplify decisions: "What can I do?"

Conflict of interest — Duties, or a duty and a self-interest, that pull in different directions.

Continuing education — Required new learning each year, often in hours, that keeps members competent after entry.

Ethical action — One that conforms to stakeholders' ethical expectations and benefits them.

Ethical conduct — Behavior that follows moral principles and balances self-interest against the direct and indirect consequences for others.

Ethical decision-making framework — Identify, consider, decide and act, reflect; often iterative.

Ethical (moral) principles — Beliefs about what conduct is good, acceptable or required, and what is bad, unacceptable or forbidden.

Ethics — A set of moral principles and rules of conduct that guide behavior.

Fiduciary duty — The obligation to deliver a high standard of care when acting for another party's benefit.

Judgment — The ability to make considered decisions and reach sensible conclusions.

Laws and regulations — Rules of conduct set by a governing body for everyone in its jurisdiction.

Material nonpublic information — Information not yet made public that would likely affect a security's price.

Overconfidence bias — Overestimating oneself, including the morality of one's own behavior.

Principle — A basic belief on which a system of behavior or reasoning rests.

Profession — An occupational community with specific education, expert knowledge and a framework of practice and behavior that earns trust, respect and recognition.

Situational influences — External factors, such as environment and culture, that shape thinking, decisions and behavior.

Stakeholder — Anyone a decision could affect, directly or indirectly.

Standards of conduct — Specific required behaviors: benchmarks for the minimum acceptable conduct of members.

Suitability standard — A legal duty only to recommend what suits the client, even if a similar option costs less.

Trade body — Serves its members' trade; normally no mission to serve society and no enforced conduct rules.

Trust — A strong belief that a person or an institution is reliable.

Values — What a person judges to have worth or merit.

Whistle-blowing — Disclosing dishonest, corrupt or illegal activity by an organization or a government.

TOOLKIT · RELATIONS

If this, then that

Relations

IF…		…THEN	REMEMBER IT AS
some stakeholders gain now	⇒	often many lose later	*winners now, losers later*
an act meets expectations and helps stakeholders	⇒	an ethical action	*two tests*
a rule is specific and sets a minimum	⇒	a standard of conduct	*a floor, not a ceiling*
a rule states general values	⇒	a code of ethics	*the public promise*
high ethical standards, enforced, to serve society	⇒	a profession, not a trade body	*ethics is the line*
clients can't see conflicts, risks, fees	⇒	disclose them fully	*close the gap*
trust is lost	⇒	revenue ↓ and costs ↑	*the firm pays twice*
law, employer and Code disagree	⇒	follow the strictest	*highest wins*
client interests vs market integrity	⇒	market integrity	*the overriding duty*
"I'm honest, I'd never…"	⇒	overconfidence: internal	*character isn't a shield*
bonus, boss, team, peers	⇒	situational influences	*the setting decides*
a narrow, short-term focus	⇒	long-term risks ignored; lapses likelier	*weigh the long run*
a rules-only culture	⇒	"What can I do?"	*check the box*
facts are missing	⇒	loop back to identify	*iterate*
a concern must be raised	⇒	a senior person in the firm first	*inside first*

TEN TRAPS, ONE LINE EACH

1. *Legal, therefore ethical.*
2. *Standards of conduct as the ideal.*
3. *A code that guarantees conduct.*
4. *Loyalty as an internal trait.*
5. *Character beats the situation.*

…CONTINUED

6. *Regulators act quickly.*
7. *More regulation is the best cure.*
8. *Local law when the Code is stricter.*
9. *The client ahead of market integrity.*
10. *The framework as a fixed sequence.*

PRACTICE · 18 QUESTIONS

Your turn

Exam format: three options, one correct. Most items are short cases: name the concept, then pick the action. Answers, worked out in full, start on p. **33**.

§1 · DEFINITION
easy

1 Ethical conduct *most accurately* means behavior that:

- A follows moral principles and balances self-interest against the direct and indirect consequences for others.
- B complies with every law and regulation that applies to the person.
- C maximizes the long-term value of the person's employer.

§1 · REASONING
medium

2 For two quarters, a fund manager values a fund's rarely traded bonds well above the prices they could be sold for. Investors who redeem their units during those quarters *most likely*:

- A are unaffected, because the error reverses once prices are corrected.
- B gain at the expense of the investors who stay in the fund.
- C lose, because they sell their units below fair value.

§1 · DEFINITION
medium

3 An investment firm's handbook says: "Analysts must not release a rating change to some clients before it is released to all of them." This rule is *best described* as part of:

- A a law or regulation.
- B a code of ethics.
- C the firm's standards of conduct.

§2 · DEFINITION
easy

4 Which feature *most clearly* distinguishes a profession from a craft guild or a trade body?

- A Its members share specialized skills.
- B Its members must uphold high ethical standards.
- C It promotes its members' commercial interests.

PRACTICE

PRACTICE · 18 QUESTIONS

§2 · REASONING
medium

5 An association of wealth planners admits members only after an exam and publishes a code of ethics. In twenty years it has received dozens of complaints about members but has never investigated one or sanctioned anyone. Which way of building trust is it *most clearly* missing?

- (A) High entry standards
- (B) A code that normalizes behavior
- (C) Monitoring of professional conduct

§3 · REASONING
easy

6 A retired engineer cannot tell whether the bond fund her adviser recommends was chosen for her benefit or for the adviser's. This *best* illustrates why investment management depends on:

- (A) trust, because clients often can't judge conflicts, risks and fees for themselves.
- (B) regulation, which removes the need for clients to trust their advisers.
- (C) collegiality among competing advisers.

§3 · CALCULATION
medium

7 An asset manager charges 0.80% a year on €5.0 bn of assets, and its running costs are €30 m a year. After a scandal, assets fall to €3.5 bn and stay there; running costs stay at €30 m, and €6 m of legal costs arrive. Profit in the first full year at €3.5 bn is *closest to*:

(A) −€8.0 m (B) −€2.0 m (C) €4.0 m

§3 · DEFINITION
easy

8 A charterholder finds that local law, her employer's policy and the CFA Institute Code and Standards set different rules for the same situation. She should *most likely* follow:

- (A) local law, because it has legal force.
- (B) her employer's policy, because the employer pays her.
- (C) whichever of the three sets the highest standard.

PRACTICE

PRACTICE · 18 QUESTIONS

§3 · DEFINITION
medium

9 Under the CFA Institute Code and Standards, when a client's interests conflict with the integrity of the market, the overriding duty is owed to:

A. the employer.
B. market integrity.
C. the client.

§4 · REASONING
easy

10 A portfolio manager skips the firm's pre-clearance step for a personal trade and says: "Rules like this are for people who might be tempted. I'm not one of them." The manager is *most likely* showing:

A. overconfidence bias.
B. a situational influence.
C. the bystander effect.

§4 · REASONING
medium

11 The manager who hired an honest junior analyst asks her to keep an outdated price in a fund's valuation file. Which factor is *most likely* to lead her to comply?

A. Her belief that she is an honest person
B. Her loyalty to the manager
C. The ethical principles she holds

§4 · DEFINITION
easy

12 Employees of a firm whose culture focuses mainly on following rules are *most likely* to ask:

A. "Who will this decision affect?"
B. "What should I do?"
C. "What can I do?"

§5 · REASONING
medium

13 Which of the following is *most likely* conduct that many would consider ethical but that may be illegal?

A. A bank clerk passes proof of clients' tax fraud to the tax authority, breaking the country's bank-secrecy law.
B. A trader buys shares ahead of an unannounced takeover, in a market with no law against it.
C. An adviser held only to a suitability standard recommends the costlier of two otherwise identical suitable funds, because it pays a higher commission.

PRACTICE

PRACTICE · 18 QUESTIONS

§5 · REASONING
medium

14 A regulator bans a fee practice after a scandal. Within a year, firms based in a neighboring country without such a ban offer the same practice to the same clients online. This *best* illustrates that laws:

A. are usually designed before problems appear.
B. remove the need for professional judgment.
C. differ across jurisdictions, so questionable practices move.

§5 · CALCULATION
hard

15 Two bond funds are equally suitable for a client who invests €100,000 for five years. Both are expected to earn 5.00% a year before charges; fund X charges 1.50% a year and fund Y 0.50%. An adviser held only to a suitability standard recommends X. Compared with Y, the client's expected wealth after five years is lower by *closest to*:

A. €1,000 B. €5,000 C. €5,850

§6 · DEFINITION
easy

16 In the ethical decision-making framework, seeking advice from someone who doesn't face the same pressures as you belongs to the phase:

A. identify.
B. consider.
C. reflect.

§6 · REASONING
medium

17 Halfway through the consider phase, an analyst realizes she doesn't know whether her client approved a new strategy in writing. She should *most likely*:

A. go back to the identify phase and establish the missing fact.
B. finish the consider phase first, because the phases must be completed in order.
C. decide now, and note the gap when she reflects on the outcome.

§6 · REASONING
medium

18 An analyst finds that a fund is using a stale price, against the firm's valuation policy. Her supervisor dismisses the concern. Her *most appropriate* next step is to:

A. report the fund to the regulator at once, without telling anyone at the firm.
B. raise it with a senior person in the firm, such as the valuation committee or compliance.
C. correct the price in the file herself, since she knows it is wrong.

ANSWER KEY, UPSIDE DOWN

14 C · 15 B · 16 A · 17 A · 18 B

1 A · 2 B · 3 C · 4 B · 5 C · 6 A · 7 A · 8 C · 9 B · 10 A · 11 B · 12 C · 13 A · 14 C

PRACTICE

PRACTICE · WORKED ANSWERS

Rule 1

1 A ✓ **Principles, weighed against consequences**

Ethical conduct follows moral principles and weighs your interest against the direct and indirect effects on others (§1.4). B is legal compliance, which can fall short of ethics (§5). C serves one stakeholder only.

Rule 2

2 B ✓ **Leavers gain, stayers pay**

Leavers are paid the inflated price, so they receive more than their units are worth; the shortfall stays in the fund (Worked 1.1). A misses that the correction lands only on those still invested. C has the direction backwards: they sell above fair value.

Rule 3

3 C ✓ **Standards of conduct**

A specific behavior the firm requires of its staff: a standard of conduct, the minimum acceptable (§1.5). A: no governing body set it. B: a code states general principles, such as fairness to all clients, not this level of detail.

Rule 4

4 B ✓ **High ethical standards**

The requirement to uphold high ethical standards is the clearest difference (§2.3). Guild members share specialized skills too (A). Promoting members' commercial interests (C) describes a trade body.

5 C ✓ **Monitoring of conduct**

Without investigations or sanctions, nobody is held to account (§2.4, trust-builder 8). The entry exam (A) and the code (B) are in place.

Rule 5

6 A ✓ **Trust: the client can't check**

Professionals know far more than clients, who may not see conflicts, risks and fees (§3.1). Regulation doesn't remove the need for trust (B). Collegiality (C) concerns how professionals treat each other.

PRACTICE

PRACTICE · WORKED ANSWERS

lost trust: revenue ↓, costs ↑

7 A ✓ **−€8.0 m**

3,500 × 0.80% = 28 → 28 − 30 − 6 = −8.0

B forgets the legal costs. C keeps the old revenue of 40. Lost trust cuts revenue and adds costs at the same time (Worked 3.1).

Rule 7

8 C ✓ **The highest standard**

Members and candidates must meet the highest of the standards set by CFA Institute, regulators and the employer (§3.5). Legal force (A) and being paid (B) don't lower that bar.

Rule 8

9 B ✓ **Market integrity**

Where client and market interests conflict, market integrity is the overriding obligation (§3.5, Fig. 3.2). Clients (C) come next, then the employer (A).

Rule 9

10 A ✓ **Overconfidence**

Trusting one's own character ("I'm not one of them") to skip a safeguard is overconfidence, an internal bias (§4.1). Nothing external is pushing the manager (B). The bystander effect (C) is about not helping when others are present.

Rule 10

11 B ✓ **Loyalty**

Loyalty to a supervisor is one of the most powerful situational influences (§4.3, Worked 4.1). Her belief in her own honesty (A) may blind her to the problem, but it is not what pushes her to comply. Her principles (C) push the other way.

12 C ✓ **"What can I do?"**

A rules-first culture breeds a check-the-box mindset (§4.5). B and A are the questions of an ethical decision-making approach.

PRACTICE

PRACTICE · WORKED ANSWERS

Fig. 5.1 zones

13 A ✓ **Whistle-blowing**

Exposing fraud may break a secrecy law and still be considered ethical: the "ethical only" zone (Fig. 5.1). B and C are the reverse, legal but unethical.

Rule 11

14 C ✓ **Laws differ across borders**

The practice moved to where no law applies (§5.3). The ban came after the scandal, not before (A). Laws never remove the need for judgment (B).

Worked 5.2, smaller

15 C ✓ **€5,850**

$100{,}000 \times (1.2462 - 1.1877) = 100{,}000 \times 0.0585 = 5{,}850$

$1.045^5 = 1.2462$ and $1.035^5 = 1.1877$. A is one year of the 1% fee gap. B multiplies it by five years but ignores compounding. Legal under suitability, yet not in the client's best interest (Worked 5.2).

Rule 12

16 B ✓ **Consider**

Additional guidance, ideally from someone free of your pressures, is part of the consider phase (§6.2). Identify (A) gathers facts, stakeholders, duties, principles and conflicts; reflect (C) comes after acting.

17 A ✓ **Back to identify**

The framework is often iterative: a missing fact sends you back to identify (§6.3). The phases need not run in a fixed order (B). Deciding without a key fact (C) invites exactly the unanticipated consequences the framework is meant to prevent.

inside first

18 B ✓ **A senior person inside the firm**

Raising it internally first gives the firm the chance to fix it and opens an independent internal review (§6.1, Worked 6.3). Going straight to the regulator (A) skips that step. Changing the price herself (C) overrides a control she has no authority over: option (b) in Worked 6.2.

SCORE YOURSELF

16–18: move on to the Code of Ethics and Standards of Professional Conduct. 12–15: reread the decision sheet and the worked examples behind your misses. Below 12: reread §4 to §6 and redo their worked examples.

PRACTICE

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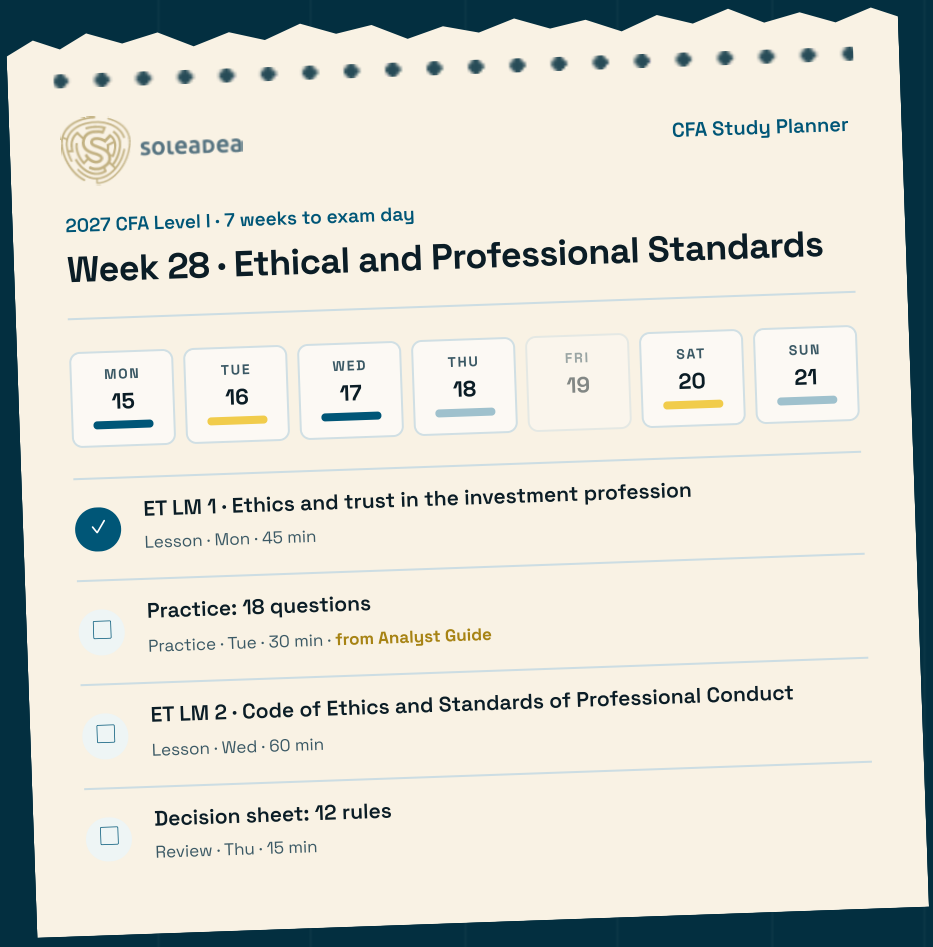


FIG. ∞ THE STUDY PLAN THESE NOTES BELONG TO.

Find the answer. Show your working.

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