CHARTA LEARNING · LESSON NOTES

Ethics, trust, the Code and the ethical decision framework

CFA Level I · Ethical and Professional Standards

You will learn: Explain how a profession earns public trust, tell law from ethics, set out the six principles of the Code of Ethics, use the ethical decision framework on a hard case, and describe how CFA Institute enforces the Code and Standards.

Running example: Examples use made-up people and firms: Fiona Reyes (200,000 invested for 20 years), the adviser Kofi Mensah (50,000 for Mrs Adeyemi), the analyst Dana Whitlock and the junior analyst Leon Hart, all at Harbour Lane Asset Management.

1. How a profession earns trust

- A client cannot check an expert's work, so the client must trust. A profession shares specialised knowledge and skills, commits to serve clients' interests, and has a professional body that sets and enforces the rules.
- Four features earn trust: knowledge kept fresh (long training, exams, continuing competence); a duty to clients; a written code of ethics; and monitoring and enforcement, because a promise nobody checks is only words.
- Trust is not a gift to the profession. It is something the profession builds and keeps earning.

2. Why money managers need strict ethics

- Information asymmetry: the manager sees the trades, costs and conflicts, while the client mostly sees a quarterly statement. Clients also hand over savings they cannot afford to lose.
- Investment results are noisy, so poor or self-serving advice can hide behind bad luck for years. The client depends on the manager's character.
- Trust matters to markets: fair treatment makes people willing to invest, so capital flows to the best ideas at lower cost. Reputation is shared, so one member's misconduct damages trust in every member.

FIONA: A HIDDEN EXTRA POINT OF COST (200,000, 20 YEARS)

Fair product	6% a year	**641,427**
Quietly costly product	5% a year	**530,660**
Cost of the hidden point	after 20 years	**110,767**

Watch out: Treating trust as the client's job: clients cannot judge expert advice, so the duty to protect them falls on the professional and the profession. Forgetting that reputation is shared.

3. Law versus ethics, and why ethics is hard

- Law is the minimum society will enforce. Ethics is what a person ought to do, and is often more demanding. Laws are written after problems happen, so they lag behind new products, and they differ between countries.
- Legal and ethical are two separate questions. Conduct runs from fraud, through legal but needlessly costly, through the legal minimum, to doing what is best for the client. Aim for the last.
- When law and Code differ, follow the stricter. If the law is silent and the Code says disclose, follow the Code. If the law is stricter, follow the law. A good motive never excuses an illegal act; use lawful channels to report wrongdoing.
- Why it is hard: overconfidence (believing you are more ethical than your peers, so you do not watch for warning signs) and situational influences (money, prestige, loyalty, targets), which we underestimate. Misconduct is usually drift, not a plan.

KOFI RECOMMENDS THE DEARER FUND (50,000, BOTH EARN 5% BEFORE FEES)

Fund A, fee 0.4%	net 4.6% a year, 10 years	**78,395**
Fund B, fee 2.0%	net 3.0% a year, 10 years	**67,196**
Law broken?	fee was disclosed	**No**
Ethical?	client's interest put second	**No**

Watch out: Thinking legal means ethical; thinking a good reason excuses an illegal act; believing misconduct only happens to other people.

4. The Code of Ethics and the Standards

- The Code is the big principles; the Standards of Professional Conduct are the specific, enforceable rules. Both bind CFA Institute members and candidates wherever they work. The duty is personal and cannot be passed to a boss.
- Principles 1 to 3: act with integrity, competence, diligence, respect and in an ethical manner with all; place the integrity of the profession and clients' interests above your own; use reasonable care and independent professional judgement.
- Principles 4 to 6: practise and encourage others to practise ethically, reflecting credit on yourself and the profession; promote the integrity and viability of the global capital markets for the benefit of society; maintain and improve your competence and that of others.
- The seven Standards: I Professionalism, II Integrity of Capital Markets, III Duties to Clients, IV Duties to Employers, V Investment Analysis, Recommendations and Actions, VI Conflicts of Interest, VII Responsibilities as a CFA Institute Member or CFA Candidate.

DANA COPIES A BROKER'S BUY RATING INTO HER REPORT

Facts	famous broker's Buy rating copied	**her own work half done**
Principle at stake	reasonable care, independent judgement	**Principle 3**
Verdict	her opinion was not independent	**Violation**

Watch out: Thinking a famous source excuses a borrowed opinion. The test is whether the opinion came from the member's own reasoning.

5. The ethical decision framework

- A checklist for experts under pressure, and a record of how you decided. Step 1, identify: the facts, the stakeholders, the duties owed, and the principles and conflicts at stake.
- Step 2, consider: the situational influences on you, additional guidance, and alternative actions. Step 3, decide and act. Step 4, reflect on what you would do differently.
- Step 2 matters most: naming and writing down the pressures lets you resist them. Seeking guidance is wise, not weak. The framework helps apply the Standards and does not replace them. Reflection is not optional.

LEON'S FRIDAY DEADLINE

Identify	doubtful number, required check skipped	**principle: reasonable care**
Consider	deadline, bonus, habit; ask compliance	**pressures named**
Decide and act	run the check, correct the figure, tell manager	**right course**
Reflect	make the check part of the process	**better next time**

6. How CFA Institute enforces the Code

- The Professional Conduct Program applies to members and candidates. An inquiry starts from a complaint, media or public information, the member's or candidate's own disclosures (including the annual Professional Conduct Statement), or conduct during an examination.
- Staff investigate. Outcomes: no action, a cautionary letter (attention but not discipline, so not a sanction), or a proposed sanction: public censure, suspension, revocation, or for candidates suspension or a ban from the CFA Program.
- The member or candidate may accept or reject a proposed sanction. If rejected, the matter goes to a hearing before a panel. This is separate from any legal or regulatory proceeding: a person can face one, both or neither.

OWEN, A CANDIDATE, IS REPORTED FOR SHARING EXAM QUESTIONS

Trigger	complaint from a colleague	**inquiry opens**
Investigation	by Professional Conduct staff	**ban proposed**
Owen's choice	rejects the sanction	**hearing before a panel**

Key takeaways

- A profession earns trust through expert knowledge, a duty to clients, a code and enforcement.
- Clients cannot judge the work and results are noisy, so managers need strict ethics.
- Law is the minimum; ethics asks what you ought to do; when they differ, follow the stricter.
- Overconfidence and situational influences make good conduct hard.
- The Code has six principles; the Standards turn them into seven areas of rules.
- The framework: identify, consider, decide and act, reflect. Only a rejected sanction reaches a hearing.

Quick check

1. Law allows a practice; the Code forbids it. What to do?
   Answer: Follow the stricter rule: the Code.
2. Which framework step is skipped most, and why does it matter?
   Answer: Consider: pressures such as deadlines and bonuses work best when nobody names them.
3. A candidate rejects a proposed sanction. What next?
   Answer: A hearing before a panel.