Standard I: Professionalism, the law, independence and misrepresentation

CFA Level I · Ethical and Professional Standards

You will learn: Name the five parts of Standard I, Professionalism, follow the stricter of the law and the Code, judge gifts and pressure with the reasonable observer test, and spot a misrepresentation by asking what impression the reader is left with.

Running example: Examples use made-up people, firms and countries (Larkspur Asset Management, the analyst Mara Quill, and others) and made-up figures.

1. The five parts of Standard I and how to work a case

- I(A) Knowledge of the Law: obey the rules, follow the stricter. I(B) Independence and Objectivity: judgement not bought or bent. I(C) Misrepresentation: no false or misleading statements. I(D) Misconduct: no dishonesty, fraud or deceit. I(E) Competence: have and keep the skills the role needs (added in the twelfth edition).
- Clue words: law looser or tighter than the Code, think A. Gift, free trip, pressure on an opinion, think B. False claim, key fact left out, copied work, think C. Fraud, deceit, conduct that harms trust, think D. Out of depth in a role or product, think E.
- I(D) can reach beyond work if a personal act bears on trustworthiness, but it is not a general morality clause: an ordinary traffic offence does not breach it. I(E) is judged by the care taken, not by whether an investment made money.
- Routine: what happened, which part is touched, apply the stricter rule, what should the member do. Do not choose an action first and then hunt for a rule that allows it.

2. I(A) Knowledge of the Law

- Members must understand and comply with all applicable laws, rules and regulations, including the Code and Standards. When they differ, follow the stricter. They must not knowingly participate in or assist a violation, and must dissociate from one they find.
- Law less strict than the Code: the Code governs. Law stricter than the Code: the law governs. Code silent, law speaks: the law governs. Whichever rule asks more wins.
- On finding a violation: check the facts and ask a supervisor, compliance or counsel; stop your own part (dissociate, which may mean resigning); document what you knew and did; escalate inside the firm. Reporting to the authorities is not required by the Standard, though local law might require it.
- Knowing participation is a violation. An honest suspicion calls for a careful inquiry, not an accusation.

EASTMARK HAS NO LAW AGAINST TRADING ON MATERIAL NONPUBLIC INFORMATION; ELAN IS TOLD OF A BID

Eastmark law	no ban on the tip	**permits**
The Code	no acting on such facts	**forbids**
Verdict	follow the stricter rule	**do not trade**

Watch out: Treating the Code as a gap filler only; hiding behind a looser law; objecting inside but carrying on with the work (Mara emails her manager but keeps processing 12 back-dated forms a week: still a violation); assuming the Standard forces a report to regulators.

3. I(B) Independence and Objectivity

- Independence is being free from outside influence on your opinion; objectivity is judging fairly on the facts. Members must use reasonable care and judgement to achieve and maintain both.
- Never offer, solicit or accept any gift, benefit, compensation or consideration that could reasonably be expected to compromise your own or another person's independence. Pressure from clients, colleagues or issuers counts too.
- The test is what a reasonable observer, told all the facts, would expect, not how influenced the member feels.
- Modest client gift: allowed, disclose to the employer. Gift from a company you cover: great caution, best refuse. Bonus tied to future results: written consent of all parties. Pressure to bend an opinion: resist, the view stays yours. Company-paid travel: pay your own way.
- Paying your own way removes a conflict; disclosure only describes it.

KOFI ADAIR IS OFFERED A PLANT VISIT PAID BY THE COMPANY HE COVERS

Business class flights	paid by Brightwater	**3,600**
Resort, 2 nights	2 × 450	**900**
Meals		**300**
Total offered	3,600 + 900 + 300	**4,800**
Verdict	attend, but his firm pays the 4,800	**problem gone**

Watch out: Using your own sense of honesty as the test; saying all gifts are banned; treating disclosure as a cure for a big conflict; forgetting that offering a benefit is also covered. Mara changing a sell to a hold after pressure from corporate finance, with her analysis unchanged, is a violation.

4. I(C) Misrepresentation

- Members must not knowingly make any misrepresentation relating to investment analysis, recommendations, actions or other professional activities. It covers investments, qualifications, services and performance. The word is knowingly: an honest, corrected error differs from a deliberate or reckless false statement.
- It is judged by the impression created. Every sentence can be true and still mislead if a key fact is left out, for example that a track record belongs to a different firm and team.
- Forms: guaranteeing a return on a volatile investment; overstating qualifications or services; presenting simulated or hypothetical results as actual, or another firm's record as your own; omitting a key fact; plagiarism, using another's work without credit.
- Exception: recognised factual and statistical sources may be used without citation. Rewording or redrawing another analyst's work does not remove the duty to credit it.

INES GUARANTEES A BOND FUND WILL RETURN AT LEAST 6% A YEAR (50,000 INVESTED)

What that implies	6% × 50,000	**3,000**
A bad year	−8% × 50,000	**−4,000**
Verdict	no guarantee on a volatile fund	**violation**

Watch out: Saying every sentence was true; turning a sincere forecast into a guarantee; rewording instead of crediting; calling public statistics plagiarism. Marketing quoting 11.2% a year for five years, earned at a previous firm by a different team and not saying so, is misleading by omission.

Key takeaways

- Standard I has five parts: Knowledge of the Law, Independence and Objectivity, Misrepresentation, Misconduct, Competence.
- When law and Code differ, the stricter governs; a looser law is never a defence.
- Knowing participation in a violation is itself a violation: dissociate, document, escalate. Reporting to authorities is not required by the Standard.
- Independence is tested by what a reasonable observer would expect. When in doubt, pay your own way.
- Misrepresentation is tested by the impression left, and omission counts. No guarantees on volatile investments.
- Name the part, apply the test, check the facts before you commit.

Quick check

1. Local law is looser than the Code. Which governs?
   Answer: The Code: the stricter rule governs.
2. Analyst takes a luxury trip from a company she covers
   Answer: I(B) breach: the observer test applies.
3. Accurate returns, but from the old firm, not stated
   Answer: I(C): misleading omission.

Summary notes for the Charta whiteboard lesson. Examples use made-up figures. Watch the full lesson at charta-learning.com.