Standard V: analysis, recommendations and actions

Ethical and Professional Standards

1 Work, words, proof

- V(A): do the work first (diligence, reasonable basis)
- V(B): tell the client what matters (communication)
- V(C): keep the proof (record retention)
- The exam judges the process, not the outcome

IN THE LESSON

- Picture a builder who signs off a bridge after a quick glance at the drawings.
- Even if the bridge stands, something went wrong, because nobody can show why it was safe to sign.
- Standard five rests on three habits.
- First, do the work before you recommend anything.
- That is Standard five A, diligence and reasonable basis.
- Second, tell the client what matters, honestly and in plain words.
- That is five B, communication with clients.
- Third, keep the proof of both.
- That is five C, record retention.
- The exam judges the process, not the outcome.
- A lucky recommendation with no basis is still a breach, and a sound one that turns out wrong is not.

2 V(A): what a reasonable basis means

- Diligence, independence, thoroughness
- Outside research: judge assumptions and rigour
- Also judge its timeliness and objectivity
- Test: could you explain your basis to a stranger?

IN THE LESSON

- Start with Standard five A.
- It says a member must use diligence, independence and thoroughness when analysing investments and making recommendations, and must have a reasonable and adequate basis, backed by appropriate research.
- Let us unpack that.
- Diligence is careful effort.
- Independence is reaching your own view instead of borrowing one or bending to pressure.
- Thoroughness is covering the factors that matter.
- You may rely on research from a colleague or an outside provider, but only after you have judged its assumptions, its rigour, its timeliness and its objectivity.
- Ask yourself one question.
- Could I explain today, to a sensible stranger, why I was entitled to believe this recommendation?

3 Before you rely on someone else's model

A model

Understand it → Test on its own data → Stress beyond history

Outside research

Read how it was built → Judge rigour and bias → Check it is current

IN THE LESSON

- Models deserve special care, so look at the picture.
- A quantitative model is a computer calculation that turns inputs into a score or a forecast.
- The top row is what a member must do before relying on one.
- First, understand it: its assumptions, its inputs and where it can fail.
- Second, test it on the data it was built from.
- Third, and this is the step candidates forget, stress it beyond its history, using conditions that history never contained, such as a deep market fall.
- The bottom row shows the same discipline for outside research.
- Read it, judge how it was built, and check that it is still current.
- A famous name or a clever model is a starting point, never the check itself.

4 Case 1: the famous broker's target

Maya Okonkwo copies a famous broker's buy target

Source	famous broker, target price	**Copied**
Her own work	no check of method or figures	**None**
Test	is reputation enough?	**No**
Verdict	Standard V(A)	**Breach**

IN THE LESSON

- Case one.
- Maya Okonkwo, an analyst at Harbourlight, sees that a famous broker has published a buy report on a retailer with a target price.
- She is busy, so she copies the target into her own client recommendation.
- She does not read how it was built or test its assumptions, and she does not look at the company's figures.
- The report may even be right.
- Facts, then standard, then verdict.
- The facts are a borrowed number and no checking.
- The standard is five A.
- Reputation is not a substitute for reasonable effort to judge soundness, so this is a breach.
- The action: read the method, test the assumptions, and write down her own view before recommending.

5 Case 2: the model that never saw a bad year

Felix Adeyemi launches an untested in-house model

Test history	10 years, worst fall 12%	**Calm**
Stress beyond history	35% fall = 2.9 × the worst	**Not done**
Limits in marketing?	only past results shown	**No**
Verdict	Standard V(A) and V(B)	**Breach**

IN THE LESSON

- Case two.
- Felix Adeyemi, chief investment officer at Harbourlight, replaces fundamental analysis with a ranking model built in house.
- It was tested on ten years of data, and in that history the worst market fall was twelve per cent.
- The model was never tested under any other condition, yet the marketing describes only its past results.
- A thirty five per cent fall is nearly three times worse than anything in its history.
- Standard five A needs the model understood and tested before use, including under adverse conditions outside its data.
- It was not, so this is a breach.
- The action: validate it independently and stress it first, and disclose its limits, which also touches five B.

6 Case 3: the dissent on the committee

Maya Lin dissents but the committee work is sound

Committee vote	4 for, 1 against	**Buy**
Her objection	target price a little high	**Opinion**
Is the basis reasonable?	thorough, independent	**Yes**
Verdict	may stay named	**No breach**

IN THE LESSON

- Case three is a no breach case.
- Harbourlight's five member committee votes four to one to rate Rook Energy a buy.
- Analyst Maya Lin voted no because she preferred a lower price target.
- But she accepts that the committee's analysis was thorough, independent and well supported, and she leaves her name on the report.
- Is that a breach?
- No.
- A member who disagrees with a group decision does not have to remove her name, provided the group's conclusion rests on a reasonable and adequate basis.
- She may record her dissent.
- It would be different if she believed the work was shallow or pressured.
- Then she should ask for her name to be taken off.
- Here the basis is sound, so nothing needs fixing.

7 Case 4: relying on a colleague, carefully

Omar Haddad uses Rosa Alvarez's forecast after checks

Source	colleague's sector forecast	**Relied on**
Omar's checks	assumptions, inputs, objectivity	**Done**
Cross-check	tested against own estimate	**Done**
Verdict	Standard V(A)	**No breach**

IN THE LESSON

- Case four, another no breach.
- Omar Haddad needs a sector forecast and a colleague, Rosa Alvarez, has already built one.
- Omar does not simply paste it in.
- He reads her assumptions, checks that the inputs are current and that no one with a stake in the stock influenced them, and tests the result against his own estimate.
- Then he uses the forecast, with credit to Rosa.
- Is that allowed?
- Yes.
- Standard five A lets a member rely on a colleague or an outside provider after judging assumptions, rigour, timeliness and objectivity.
- Omar did exactly that.
- The lesson is that reliance is not the breach.
- Reliance without examination is.
- The difference from Case one is the checking.

8 V(B): the five parts of communication

- 1. Nature and costs of services (affiliates, third parties)
- 2. The process, and prompt notice of material changes
- 3. Significant risks and limitations
- 4. Important factors included; 5. Fact apart from opinion

IN THE LESSON

- Now Standard five B, communication with clients.
- Think of a holiday price that leaves out the resort charge.
- Every sentence is true, yet you were not told.
- The Standard now has five parts.
- One, disclose the nature of the services and their costs, including costs that arise at affiliates and third parties.
- Two, describe the investment process, and promptly disclose any material change to it.
- Three, disclose significant risks and limitations.
- Four, include the important factors in a recommendation.
- A summary may be short, but must not leave out a factor material to the conclusion.
- Five, separate fact from opinion.
- Notice the word ongoing.
- The duty continues after the client signs, so it is not met by one onboarding document.

9 Case 5: the fee that was only part of it

Samir Khan: client assets $750,000

Advisory fee, disclosed	750,000 × 0.80%	**$6,000**
Affiliate funds + platform, hidden	750,000 × 0.50%	**$3,750**
True yearly cost	6,000 + 3,750	**$9,750 = 1.3%**
Verdict	Standard V(B)	**Breach**

IN THE LESSON

- Case five.
- Samir Khan advises a client with seven hundred fifty thousand dollars.
- His proposal states the advisory fee, eight tenths of one per cent, which is six thousand dollars a year.
- It does not mention that the money goes into funds run by Harbourlight's affiliate, charging four tenths of a per cent, nor the platform that holds them, charging one tenth.
- Samir thinks the client is experienced and will know.
- The full yearly cost is nine thousand seven hundred fifty dollars, one point three per cent.
- Costs through affiliates and third parties must be disclosed, and a sophisticated client is no excuse.
- This is a breach of five B.
- The action: restate the full cost in writing.

10 What the client heard and what it cost

Yearly cost ($)

Told to client	**6,000**
Left out	**3,750**
Real total	**9,750**

Left out is 62.5% of what was told

IN THE LESSON

- Here are the same figures as bars.
- The first bar is the six thousand dollars the client was told about, the advisory fee.
- The second bar is the thirty seven hundred fifty dollars of affiliate and platform charges that were left out.
- The third bar is the real yearly cost, nine thousand seven hundred fifty dollars.
- Notice what the second bar says.
- What was left out is more than six tenths of what was disclosed.
- This is not a rounding detail, and it is what material means in this Standard.
- Would a reasonable client decide differently if they knew?
- If the answer is yes, it must be said, and it must be said before the client decides, and again whenever the costs change.

11 Case 6: telling clients too late

Process changed in March, clients told in January

Change made	March, fund method replaced	**Material**
Clients told	next January	**10 months**
Good intention?	wanted one clear letter	**Irrelevant**
Verdict	Standard V(B)	**Breach**

IN THE LESSON

- Case six, where a well meant action is still a breach.
- In March, Harbourlight's chief investment officer moves a fund from fundamental analysis to a quantitative model.
- He plans to explain it properly in the annual letter, which goes out the following January, so that clients get one clear message.
- His intention is kind, but ten months pass in which clients hold something different from what they chose.
- Standard five B requires prompt disclosure of a material change to the investment process.
- Waiting for a convenient letter is not prompt.
- This is a breach.
- The action: tell clients when the change is made, or before, and explain it again in the letter.

12 Case 7: sparing the client a worry

Nina Brandt leaves out a customer risk

Biggest customer	27 ÷ 60 of sales	**45%**
Contract under review	known, left out	**Omitted**
Profit forecast	stated as fact	**Not labelled**
Verdict	Standard V(B)	**Breach**

IN THE LESSON

- Case seven, another well meant breach.
- Nina Brandt writes a one page summary on a small manufacturer.
- She knows that one customer buys forty five per cent of its sales, twenty seven million out of sixty million, and that this customer is reviewing its contract.
- She leaves it out because she does not want to alarm the client.
- She also states next year's profit forecast as plain fact.
- Summaries are allowed to be short, but the risk is material, and opinion must be separated from fact.
- Both are failures of five B.
- The action: add the concentration risk, and label the forecast as her estimate.
- Protecting a client from information is never the same as serving them.

13 From fact to opinion

- Reported sales
- Calculated margin
- Next year's profit
- Two-year price
- Will dominate

IN THE LESSON

- Separating fact from opinion is easier to see on a line.
- A fact can be checked.
- An opinion is a judgement.
- Most statements sit between the two.
- On the far left is pure fact, such as reported sales.
- Next comes a calculation from facts, such as a margin worked out from those sales.
- Then an estimate, such as next year's expected profit.
- Then a forecast resting on many assumptions, such as a share price in two years.
- On the far right is a belief, such as the firm will dominate its market.
- Clients are entitled to know which kind of statement they are reading.
- The rule is not to avoid opinions.
- It is to label them so the client can weigh them.

14 Case 8: the short summary done well

Dev Raman: one page summary of a long report

Format	one page, full report on request	**Short**
Material factors	drivers and two key risks	**All there**
Fact versus opinion	forecast labelled as estimate	**Clear**
Verdict	brevity is allowed	**No breach**

IN THE LESSON

- Case eight is a no breach case.
- Dev Raman sends a busy client a one page summary of a forty page report.
- He includes the conclusion, the three factors that drive it, and the two biggest risks, one of them the same customer concentration issue.
- He labels the revenue forecast as his estimate and the reported figures as fact, and he tells the client the full report is available on request.
- Is brevity a breach?
- No.
- The Standard permits a summary.
- The test is not length.
- The test is whether a factor material to the conclusion has been left out, and whether fact and opinion are kept apart.
- Nothing is missing here.
- Short and complete beats long and padded.

15 Mistakes that cost marks so far

- 1. Reputation is not diligence
- 2. A complex model still needs stress tests
- 3. Reliance on a checked colleague is allowed; dissent is too
- 4. Disclaimers and onboarding do not cure omissions
- 5. Sophisticated client: costs are still disclosed

IN THE LESSON

- Before the third subsection, here are the traps.
- One, treating a famous source as proof.
- Reputation is not diligence.
- Two, trusting a model because it is complex.
- You must understand and stress test it.
- Three, thinking reliance on colleagues is itself a breach, or that you must remove your name whenever you disagree with a group.
- Neither is true once the work is judged and the basis is reasonable.
- Four, treating a general disclaimer or onboarding paper as enough.
- The duty is ongoing, and a disclaimer never cures a missing known risk.
- Five, leaving out costs because the client is sophisticated, or because a figure is unknown in advance.

16 V(C): records belong to the firm

- Keep records of analysis, advice and communications
- They are evidence of a reasonable basis at the time
- Records are firm property, not the member's
- Follow local rules; else at least 7 years

IN THE LESSON

- Now Standard five C, record retention.
- Picture a customer who says they were promised something, and the shop has no receipt and no note.
- Who is believed?
- The Standard says members must develop and maintain appropriate records to support their analyses, recommendations, actions and communications with clients and prospects.
- The purpose is evidence.
- If a regulator or a client asks why you acted, records show a reasonable basis existed at the time.
- Two facts matter for cases.
- Records are the property of the firm, not the member, so a leaver may not take them without consent.
- And retention follows local rules, or at least seven years where none exist, with electronic business messages counted as records.

17 Case 9: copies in the leaver's bag

Tessa Lin copies her files before joining a rival

What she took	notes and models, copied	**Taken**
Employer's consent	none given	**No**
Whose property?	the firm's records	**Harbourlight's**
Verdict	Standard V(C)	**Breach**

IN THE LESSON

- Case nine.
- A Harbourlight portfolio manager, Tessa Lin, is leaving to join a rival.
- On her last evening she asks to take copies of her research notes and model files so she can keep recommending the same shares.
- She sees this as her own work.
- But the records are the property of Harbourlight, and she has no consent.
- Taking them breaches five C and is probably a breach of her duty to her employer as well.
- Even more, her old firm now has to defend its advice without them.
- The action: leave the files, and at the new firm rebuild the support from public sources before relying on her old conclusions.
- Memory alone is not a record.

18 Case 10: how long to keep the file

Recommendation dated 12 September 2027

No local rule: 7 years	2027 + 7	**12 Sep 2034**
Local law says 10 years	2027 + 10	**12 Sep 2037**
Shorter period to save space	not acceptable	**Breach**
Verdict	Standard V(C)	**Follow rule**

IN THE LESSON

- Case ten is about dates.
- Harbourlight has no written retention policy, and the regulator sets no period.
- An analyst issues a recommendation on the twelfth of September, twenty twenty seven.
- How long should the file be kept?
- The guidance is at least seven years where no local rule exists, so until the twelfth of September, twenty thirty four.
- Now change the facts.
- If local law required ten years, then law governs, and the file is kept until the twelfth of September, twenty thirty seven.
- The order of authority is the point.
- Follow the local rule when there is one, use seven years when there is none, and never choose a shorter period because storage is inconvenient.
- Also, the missing policy is itself a weakness.

19 Case 11: rebuilding at the new firm

Hana Ito rebuilds her support at the new firm

Old files	left with Harbourlight	**Not taken**
New support	public filings, new valuation	**Rebuilt**
Recommendation issued	after the file existed	**After**
Verdict	Standard V(A) and V(C)	**No breach**

IN THE LESSON

- Case eleven, the last no breach case.
- Hana Ito moves from Harbourlight to a new firm.
- She still believes in a rating she formed before leaving, but she has no files.
- At the new firm she spends a week collecting public filings, rebuilding her valuation and writing down her assumptions, and the new firm keeps the file.
- Only then does she publish a recommendation, and the fresh work leads her to trim the target slightly.
- Is that a breach?
- No, this is exactly what the Standard expects.
- She did not take the old firm's property, she did not rely on memory, and her new records show a reasonable basis.
- Compliant, and a habit worth copying.

20 Case review: cases one to four

Standard V: cases one to four

Case and issue	Breach?
1 Copied broker target	Yes, V(A)
2 Untested model	Yes, V(A)
3 Dissent on committee	No
4 Reliance after checks	No

IN THE LESSON

- Let us line up the cases in tables, so you can see the pattern.
- Case one, the copied broker target, is a breach of five A because reputation replaced checking.
- Case two, the untested model, is a breach of five A, and the missing limits touch five B.
- Case three, the dissent on the committee, is no breach, because the committee basis was sound.
- Case four, relying on a colleague after checking, is no breach either.
- So far two breaches and two clean cases, and the dividing line each time was whether the examination was done.
- The question to ask is whether the work, the words or the proof was missing, and whether the answer changes once you know the facts in full.

21 Case review: cases five to eight

Standard V: cases five to eight

Case and issue	Breach?
5 Hidden affiliate costs	Yes, V(B)
6 Late process notice	Yes, V(B)
7 Risk left out	Yes, V(B)
8 Short complete summary	No

IN THE LESSON

- Now cases five to eight.
- Case five, the hidden affiliate and platform costs, is a breach of five B.
- Case six, the late notice of a process change, is a breach of five B, however kind the intention.
- Case seven, leaving a customer risk out of a summary and stating a forecast as fact, is also a breach of five B, even though Nina meant to spare the client worry.
- Case eight, the short but complete summary, is no breach.
- Notice that two of these breaches came from good intentions.
- Intention is never the test.
- The test is what the client was and was not told, and whether it would have changed their decision if they had known.

22 Case review: cases nine to eleven

Standard V: cases nine to eleven

Case and issue	Breach?
9 Leaver copies files	Yes, V(C)
10 Retention date	7 yrs if no rule
11 Rebuild at new firm	No

IN THE LESSON

- And the last three.
- Case nine, the leaver copying research files, is a breach of five C, because records belong to the firm.
- Case ten, the retention date, is not a breach in itself, but the answer is seven years from the recommendation date where no rule exists, or the longer period where the law sets one.
- Case eleven, rebuilding support at a new firm, is no breach.
- Count the clear no breach cases across all eleven: four, with Case ten a date question.
- Do not assume every case is a trap, and do not hunt for a breach that the facts do not give you.
- Read the facts, name the subsection, decide, and state the action.
- That four step habit wins marks.

23 Part two: stopping breaches before they happen

- Firm: written policies, so good conduct is not luck
- Member: personal habits that work anyway
- Cover V(A) basis, V(B) communication, V(C) records
- Ask: which case would this have stopped?

IN THE LESSON

- Now the second outcome.
- Every case so far was judged after the event.
- A good firm tries to make the breach hard to commit in the first place.
- Think of a hospital that uses checklists: not because surgeons are careless, but because busy people forget.
- The exam asks you to propose practices and procedures, and there are two levels.
- The firm writes down policies, so that good behaviour does not depend on memory or goodwill.
- And the member keeps personal habits that work even where the firm is weak.
- Let us build both, one subsection at a time: reasonable basis first, then client communication, then records.
- For each, ask which of our cases the procedure would have prevented.

24 Reasonable-basis procedures

The firm

Written diligence steps → Vendor and subadviser criteria → Independent model validation → Stress tests beyond history

The member

Note the basis → Scale effort to stakes → Say when it is not enough

IN THE LESSON

- The firm's first job is to write down what reasonable basis means.
- Follow the top row.
- First, set due diligence steps for internal and outside research: who reads it, what is checked, and what is recorded.
- Second, set criteria for approving data vendors and subadvisers, such as their process, track record and independence.
- Third, require independent validation of every model before use, by people who did not build it.
- Fourth, require stress testing beyond the model's data.
- The bottom row shows the member's own habits: write a short note of the basis for each recommendation, scale effort to the stakes, and say plainly when the work is not enough.
- These steps would have caught Cases one and two.

25 Communication procedures that work

A standard client disclosure pack

Services provided	what is and is not included	**Plain words**
All costs	advisory + affiliate + platform	**One total**
Investment process	how decisions are made	**Described**
Risks and limits	specific, not boilerplate	**Named**

IN THE LESSON

- Next, communication.
- Firms can prepare standard disclosures that every client receives and that cover four things.
- The services provided.
- All the costs to the client, including affiliate and third party charges, shown as a total.
- The investment process.
- And its risks and limitations.
- A standard pack means no adviser has to decide, case by case, what to leave out, and it would have prevented Case five.
- Pair it with a review at every client meeting, because the duty is ongoing.
- The trap is thinking onboarding disclosure is enough.
- A client who signed a good document three years ago has not been told about a change made last month.

26 Change triggers and opinion labels

Controls that stop Cases six and seven

Process change	trigger: notify clients promptly	**Case 6**
Forecasts	labelled as opinion	**Case 7**
Summaries	key risks must appear	**Case 7**
Costs	total shown, every layer	**Case 5**

IN THE LESSON

- Two more communication controls.
- First, a trigger for change.
- The policy states that any material change to the investment process must be notified to clients promptly, and names who decides what is material and who sends the notice.
- Without a trigger, Case six happens.
- Second, a labelling rule: forecasts and estimates must be marked as opinion, and reports must show which figures are reported fact.
- A simple template with a facts box and a view box does this and would have fixed Case seven.
- A third control is a check that summaries still carry the key risks.
- Rules like these cost little, and each one removes a judgement call from a busy person.

27 Record procedures that work

A records policy for Harbourlight

Retention period	local rule, else 7+ years	**In writing**
Where held	central firm systems	**Not personal**
Business messages	captured and kept	**Included**
Leavers	no copies without consent	**Rule set**

IN THE LESSON

- Last, records.
- The firm writes a retention policy that meets local rules, and keeps records for at least seven years where there are none.
- It holds the records centrally, in firm systems, because they are firm property.
- That includes business messages, which should not live only on personal phones.
- It also sets a leaver rule: no copying of files without consent, and a note for new hires on rebuilding support from public sources.
- Compare Harbourlight in the item we saw: no written policy, and a departing manager asking for copies.
- Each gap is a procedure waiting to be written.
- The member's habit is simple.
- Save the basis for every recommendation in the firm's system, the same day.

28 Which control stops which case

Procedures matched to the cases

Breach	Control that prevents it
Copied broker target	Research due diligence
Untested model	Validation and stress test
Hidden costs	Standard disclosure pack
Late process notice	Change trigger

IN THE LESSON

- Let us match controls to cases, because the exam does this in reverse.
- Given a breach, which procedure would have prevented it?
- For the copied broker target, a written due diligence step for outside research.
- For the untested model, independent validation and a stress test before use.
- For the hidden costs, a standard disclosure pack showing every layer as one total.
- And for the late notice of a process change, a trigger that sends notice promptly.
- The summary template and the retention policy, which we met a moment ago, follow the same logic.
- Notice that each control targets one cause, not a person.

29 Practices for the individual member

- Keep a file note of basis and checks
- Test every outside source and model first
- Check what clients have really been told
- Label opinions; raise gaps with compliance

IN THE LESSON

- The firm will not always be well run, so the member needs their own practices too.
- Keep a short file note for every recommendation: what you relied on, what you checked, and what you doubted.
- Treat any outside source or model as unproven until you have tested it.
- Ask what your client has actually been told about costs, and tell them if the answer is not everything.
- Label your opinions.
- If a committee conclusion has no reasonable basis, ask for your name to be removed, but if the work is sound, feel free to dissent in writing and stay named.
- Finally, raise gaps in procedure with compliance rather than working around them.
- The exam rewards the answer that is proactive and specific.

30 Recap: Standard V in one table

Standard V: the three parts

Part	Core duty and its control
V(A) Basis	Examine it; validate models
V(B) Communication	All costs, process, risks; update
V(C) Records	Firm-owned; 7+ years
Preventing breaches	Written policy plus habits

IN THE LESSON

- Let us recap.
- Standard five A, diligence and reasonable basis.
- Do the work, scaled to the stakes.
- Judge colleague and outside research, and understand and stress test models.
- Disagreement with a sound group view does not force you off the report.
- Standard five B, communication.
- Disclose services and all costs, the process and any material change, the risks and limits, the important factors, and keep fact apart from opinion.
- Summaries are fine if nothing material is left out.
- The duty is ongoing.
- Standard five C, records.
- Keep records that support your work.
- They belong to the firm.
- Follow local rules, or keep at least seven years.
- Procedures turn all of this into habit.

31 Try three quick questions

1. Analyst relies on a checked colleague forecast. Breach?
   Answer: No: V(A) allows reliance after judging it
2. Process change told to clients nine months later. OK?
   Answer: No: V(B) needs prompt disclosure
3. No local rule, no firm policy. Best proposal?
   Answer: Written policy, central, 7+ years

IN THE LESSON

- Now try three questions yourself.
- Pause after each one.
- Question one.
- An analyst relies on a colleague's forecast after judging its assumptions and checking it is current.
- Is that a breach of five A?
- No.
- Reliance is allowed after examination.
- Question two.
- A firm tells clients about a change in its investment process in the next annual letter, nine months later.
- Is that acceptable?
- No.
- Five B requires prompt disclosure of a material change.
- Question three.
- A firm has no retention policy and no local rule exists.
- What does the best practice proposal say?
- Write a policy, hold records centrally, and keep them at least seven years.
- That protects the firm and its clients in the long run.