CHARTA LEARNING · LESSON NOTES

Standards four and five: duties to employers, and analysis and recommendations

Ethical and Professional Standards

1 A story: the manager with one foot out of the door

- A baker leaving to open her own shop
- Weekend planning: fine. Taking the recipe book: not
- Standard IV: loyalty, extra pay, supervision
- Marlowe Quay: Dana Whitcombe plans to leave

IN THE LESSON

- Imagine a baker who has decided to open her own shop across town.
- For a few more weeks she still works for the bakery that pays her.
- Can she look at shop premises on a Sunday?
- Of course.
- Can she take the secret recipe book home, or phone the regular customers and tell them to follow her?
- No.
- Standard four is that story told for investment firms.
- It asks what loyalty means while you are employed, what you may do once you have gone, and what a supervisor must do when somebody else crosses the line.
- Ines Calloway has just been told that a portfolio manager, Dana Whitcombe, is planning to leave Marlowe Quay.

2 Standard IV at a glance

Three parts, one line each

IV(A) Loyalty	**do not harm the employer**
IV(B) Additional compensation	written consent first
IV(C) Responsibilities of supervisors	prevent and detect
Applies from	first day to last day
After leaving	records stay behind

IN THE LESSON

- Standard four has three parts, and the exam likes to blend them in one story.
- Four A is loyalty.
- Until employment ends, you act in your employer's interest and do not harm it.
- Four B is additional compensation arrangements.
- If a client or anyone else offers you extra pay or a benefit for your work, your employer must know and agree in writing.
- Four C is responsibilities of supervisors.
- If you supervise people, you must make reasonable efforts to prevent and detect breaches by them.
- Keep a short label for each: four A, do not harm the employer; four B, no hidden extra pay; four C, build and use the controls.
- We take them in that order.

3 Dana's timeline: before and after her last day

While employed

Plan in own time: fine → Copy firm files: breach → Solicit clients: breach

After she has left

Memory: fine → Public sources: fine → Valid agreement: may bar

IN THE LESSON

- Here is the first decision flow.
- The top row runs up to the day her employment ends.
- All through it, Dana owes Marlowe Quay full loyalty.
- Planning her new venture in her own time is allowed: she may register a company or look at an office.
- But copying model portfolios, client lists or trading code is a breach, and so is asking clients to move before she has left.
- The bottom row starts when she is gone.
- Now she is free to contact former clients, using her memory or public sources such as a website, unless a valid agreement says she may not.
- What she may never do is use the firm's records.

4 Case 1: Dana's list of actions

Five actions, five verdicts

Registers her company, Saturday	**fine**
Copies model portfolios home	breach
Asks 4 clients to move, pre-resignation	breach
Calls clients from memory, after leaving	fine unless barred
Uses firm's client file, after leaving	breach

IN THE LESSON

- Case one.
- Dana Whitcombe will resign at the end of the month to start Whitcombe Partners.
- Over the next weeks she does five things, and the exam wants a verdict on each.
- Registering the new company on a Saturday is fine, because it is personal time and she is not yet competing.
- Copying her model portfolios to a home drive is a breach, because they are the firm's property.
- Asking four of her clients to move before she resigns is a breach, because it is soliciting while employed.
- After she leaves, phoning clients she remembers is fine unless a valid agreement forbids it.
- Using the firm's client file to do so is still a breach.

5 Case 1: what the breach could cost

Her book: 10 accounts, 120m, fee 0.50%

Fee from her whole book	0.50% × 120m	**600,000**
Four accounts approached	together	**48m**
Fee on those four	0.50% × 48m	**240,000**
Share of her book's fee	240,000 ÷ 600,000	**40%**
Verdict	soliciting while employed	**Breach**

IN THE LESSON

- To see why this matters to an employer, put numbers on it.
- Dana manages ten accounts worth one hundred and twenty million, and the firm charges half a per cent, which is six hundred thousand a year.
- She quietly approaches four of those accounts, together forty eight million.
- If they leave, the firm loses half a per cent of forty eight million, which is two hundred and forty thousand a year.
- That is forty per cent of the fee income from her whole book, taken by someone still on the payroll.
- This is what loyalty protects.
- The verdict does not depend on the size of the loss, though.
- Soliciting while employed is a breach even if every client had stayed put.

6 After she has left: memory, public sources, agreements

- Loyalty ends with the job; confidentiality does not
- Memory and public sources: she may use them
- Firm records, client files, code: they stay behind
- A valid agreement may still restrict her

IN THE LESSON

- What changes after Dana walks out?
- Quite a lot.
- The duty of loyalty ends with employment, so she may now contact former clients and tell them about her new firm.
- She can use what she remembers, and she can use public sources, such as a directory or a website.
- She cannot use the firm's records, which are still the firm's, and she must keep client information confidential for good.
- There is one more check: a valid agreement, for example a restriction signed when she joined.
- If one exists and is enforceable, she must respect it.
- The exam trap is to treat leaving as a clean slate.
- It is not.
- The records stay behind, and so do the agreements.

7 Case 2: the client's bonus offer

Brightwater 80m; fee 0.60%; bonus 20% of excess return

Firm's normal fee	0.60% × 80m	**480,000**
Excess return	8.5% − 6.0%	**2.5 points**
Excess in money	2.5% × 80m	**2.0m**
Bonus offered to Owen	20% × 2.0m	**400,000**
Bonus against fee	400,000 ÷ 480,000	**83%**

IN THE LESSON

- Case two is Four B.
- Owen Lake, another Marlowe Quay manager, runs eighty million for Brightwater Trust.
- His employer charges six tenths of a per cent, four hundred and eighty thousand a year.
- The trust's chair, delighted with him, offers Owen personally twenty per cent of any return above the benchmark.
- The benchmark returns six per cent.
- If Owen earns eight and a half, he beats it by two and a half points, which is two million on this fund.
- Twenty per cent of that is four hundred thousand, over four fifths of his normal fee, paid by a single client on top of his pay.
- That could tilt his effort towards this one account.

8 Judging an extra-pay offer: who must say yes

Four B, step by step

Extra pay or benefit? → Could it skew effort? → Written consent: all parties

IN THE LESSON

- Now the decision.
- Whenever someone offers extra pay for your work, walk along this row.
- First, is it compensation or a benefit beyond what your employer pays you?
- Yes, because the trust would pay Owen directly.
- Second, could it create a conflict, for instance by pulling effort towards one account?
- Yes again, because the bonus rewards him only on this fund.
- Third, who must agree?
- Not just Owen, and not just the chair of the trust.
- The Standard needs written consent from all parties involved, his employer and the client offering the bonus.
- A documented email can count as writing.
- Without that, Owen would be in breach.

9 Case 3: Ines learns of the breach

What Ines has learned, and must do

Model files copied	14 of 22	**64%**
Clients approached	4 of 10	**40%**
First duty	investigate	**promptly**
Meanwhile	limit or watch Dana	**interim limits**
Failure to act	supervisor's breach	**IV(C)**

IN THE LESSON

- Case three is Four C.
- Marlowe Quay's systems team tells Ines Calloway that in the last fortnight Dana copied fourteen of the firm's twenty two model portfolio files, about sixty four per cent, and that she has called four of her ten clients.
- Ines is the supervisor, and her duty is to make reasonable efforts to prevent and detect breaches, and then to act.
- On learning of this one she must investigate promptly, and meanwhile limit or more closely monitor Dana's activities.
- Cutting access to the model files and putting a second person on her trades are the sort of interim limits meant.
- Waiting for the resignation letter would be the supervisor's own failure.

10 A supervisor's response, in order

From alert to action

Breach surfaces → Investigate promptly → Limit the employee

IN THE LESSON

- This is the supervisor's flow.
- On the left, a possible breach surfaces, from a systems alert, a client call or a colleague.
- In the middle, Ines investigates promptly.
- She does not wait for proof, and she does not delegate the whole matter away, because supervision remains her responsibility.
- On the right, she puts interim limits on the employee while the facts are gathered, such as cutting file access, closer review of trades, or removing client contact.
- After that come the findings, the discipline and the fix for the system, and the record of what was done.
- The common error is to wait for certainty.
- The standard asks for prompt action on a reasonable concern.

11 What an adequate compliance system looks like

Five tests for an adequate system

Written	**in plain language**
Sized to the business	not copied
Communicated	training, reminders
Followed	applied in practice
Reviewed periodically	as the firm changes

IN THE LESSON

- Now to the practical side: proposing procedures that head off breaches.
- The first idea is that a code of ethics on its own is not an adequate system.
- Four C expects a compliance system that is written, so everyone can read it.
- It is sized to the firm's business, so a small boutique does not copy a global bank's manual, and a trading firm does not copy a research shop's.
- It is communicated, which means staff are trained and reminded.
- It is followed, because rules that nobody applies are decoration.
- And it is reviewed periodically, because the business and the risks change.
- Here are the five tests as a table.

12 What Marlowe Quay should put in place

Five procedures, each tied to a risk

Compliance officer	with real authority
Outside roles	disclose, consent first
Departures	cut access, recover records
Pay and incentives	no win-at-any-cost
Possible breach	investigate, restrict

IN THE LESSON

- So what would Ines propose after Dana's case?
- Five measures.
- First, name a compliance officer who has real authority, not just a title.
- Second, require written disclosure and written consent before any outside role, such as a paid directorship or consulting, begins.
- Third, a departure procedure: cut system access on the last day, recover firm records and model portfolios, and remind the leaver in writing about confidentiality.
- Fourth, avoid pay arrangements that reward short term performance at any cost, which push people to cut corners.
- Fifth, a breach procedure that says prompt investigation and interim limits.
- Each one matches a weakness that Dana's case exposed.

13 Case 4: the paid directorship

Elsa Brandt: paid board seat, 30,000 a year

Fee offered	per year	**30,000**
Time it would take	12 of 230 days	**5.2%**
Client accounts holding it	3 of 10	**30%**
Needed before she starts	written, from the firm	**Written consent**
If she accepts first	loyalty breach	**IV(A)**

IN THE LESSON

- Case four tests the outside roles procedure.
- Elsa Brandt, an analyst at Marlowe Quay, is offered a paid board seat at a listed company for thirty thousand a year.
- It would take twelve days of her year, out of about two hundred and thirty working days, roughly five per cent of her time.
- Three of the firm's ten client accounts hold that company's shares, so the role touches the firm's clients.
- Without a procedure, Elsa might simply accept.
- With one, she must disclose it in writing and get written consent before it starts, so that the firm can judge the time, the conflict and the access to information.
- Taking the seat first and asking later breaks the firm's procedure and the duty of loyalty.

14 When the system is not adequate

- Judge the procedures: written, sized, followed?
- If inadequate, tell senior management in writing
- Decline to supervise until they are fixed
- Delegating tasks does not delegate responsibility

IN THE LESSON

- One more procedure matters, and it is about the supervisor herself.
- Suppose Ines reviews the firm's controls and decides they are not adequate: perhaps there is no departure procedure and no one checks outside roles.
- She cannot just carry on supervising and hope.
- The Standards expect her to tell senior management in writing that the procedures are inadequate and decline to supervise until they are fixed.
- Written matters, because it leaves a record that she raised the problem.
- Declining matters, because supervising people under a system you know is weak is the very thing four C warns against.
- Delegating tasks does not remove her responsibility either.

15 Mistakes to avoid on Standard IV

- 1. Soliciting clients before the resignation date
- 2. Taking model portfolios or client files when leaving
- 3. Accepting a client's bonus without all consents
- 4. Calling a code of ethics an adequate system

IN THE LESSON

- Four mistakes cost marks.
- One.
- Thinking a manager may solicit clients before resigning, as long as the move is not announced yet.
- Loyalty lasts until the employment ends.
- Two.
- Thinking that once a manager has left she may take her model portfolios and client files with her.
- Memory and public sources are allowed, records are not.
- Three.
- Thinking a client's bonus offer is only the client's business.
- It needs written consent from the employer as well as the client.
- Four.
- Thinking a code of ethics makes a compliance system adequate.
- It must be written, sized, communicated, followed and reviewed.

16 A story: the recommendation behind the recommendation

- A doctor prescribes on a salesman's word
- V(A): a reasonable and adequate basis
- V(B): honest, complete communication
- V(C): records that prove the first two

IN THE LESSON

- Think of a doctor who prescribes a drug because a salesman said it worked.
- If the drug fails, we do not ask only whether it failed.
- We ask whether the doctor had a sound basis for prescribing it.
- Standard five treats investment decisions the same way.
- Five A asks whether you had a reasonable and adequate basis, supported by research and investigation.
- Five B asks whether you communicated honestly with clients, including what the process is, what changed and what the risks are.
- Five C asks whether the records exist to show both.
- Marlowe Quay now has three decisions to defend: a sub adviser, a quantitative strategy, and a change in leverage.

17 Standard V in the order a decision meets it

Basis, then communication

V(A) Reasonable basis → V(B) Tell clients → V(C) Keep records

IN THE LESSON

- Here is the order in which a decision meets the three parts of Standard five.
- On the left, five A comes first, because before any client money moves you need a basis: due diligence on the provider, an understanding of the process, and for a quantitative strategy, testing that goes beyond the data history.
- In the middle, five B follows once money is invested: clients are told the process in outline, the risks and limits, and any material change.
- On the right is five C, the records.
- They hold the evidence for the other two, and they belong to the firm.
- If you can state which row a case is on, you have usually found the answer.

18 Standard V at a glance

What each part requires, and what a breach is

V(A) requires	**diligence, thorough analysis**
V(A) breach	unchecked provider or model
V(B) requires	honest process, risk, change
V(B) breach	hidden change; opinion as fact
V(C) requires	records kept, firm's property

IN THE LESSON

- Let us put the three parts in the grid the exam uses: what the Standard requires, and what a breach looks like.
- What a firm should put in place comes later in the lesson.
- Five A requires diligence and thorough analysis.
- Its breach is relying on a provider or a model nobody has checked.
- Five B requires honest communication of the process, its risks and any change.
- Its breach is hiding a change, or passing opinion off as fact.
- Five C requires records to be kept, and they are the firm's property, so losing them or taking them away is the breach.
- Keep this grid in mind for the cases.

19 Case 5: hiring a sub-adviser

Halden Row: 60m of bonds; 3 of 5 checks passed = 60%

Process seen in writing	check 1	**Pass**
Assumptions tested	check 2	**Pass**
Track record verified	check 3	**Fail**
Key people interviewed	check 4	**Pass**
Risk controls inspected	check 5	**Fail**

IN THE LESSON

- Case five.
- Marlowe Quay wants to hand sixty million of emerging market bonds to an outside sub adviser, Halden Row Partners.
- Under five A, relying on someone else's work does not remove the duty.
- Ines must look at their process, assumptions and record first.
- Her team runs a five point check.
- The process was seen in writing, the assumptions were tested, and the key people were interviewed.
- But the track record has not been verified, because only the sub adviser's own figures were seen, and the risk controls were not inspected.
- Three of five checks passed, sixty per cent.
- That is not a reasonable basis yet.
- The client money waits until the two gaps are closed.

20 Case 6: a quant strategy and its stress test

Kestrel Tilt: 12-year back test; leverage 3×; limit 15%

Worst month in data	−4% × 3	**−12%**
Stress month, twice as bad	−8% unlevered	**−8%**
Stress month, levered	−8% × 3	**−24%**
Clients' monthly loss limit	stated by clients	**−15%**
Verdict	stress breaks the limit	**Not yet**

IN THE LESSON

- Case six.
- Marlowe Quay's research team proposes Kestrel Tilt, a quantitative strategy, run with three times leverage.
- Its twelve year back test shows a worst month of minus four per cent before leverage, so minus twelve per cent with leverage.
- The clients' monthly loss limit is fifteen per cent, so it looks comfortable.
- But five A says a quant strategy must also be tested in stress scenarios beyond its data history.
- A fair stress is a month twice as bad as anything in the data, eight per cent unlevered, and with three times leverage that is a twenty four per cent loss.
- That breaks the fifteen per cent limit.
- Passing the back test alone is not enough.

21 The back test against the stress test

Monthly loss, levered (%)

Back-test worst	**12%**
Client limit	**15%**
Stress month	**24%**

Same strategy, same leverage

IN THE LESSON

- Here are those figures as bars.
- The vertical axis is the monthly loss in per cent.
- The first bar is the worst month in twelve years of data, with leverage, twelve per cent.
- It sits below the client limit, which is the second bar, fifteen per cent.
- The third bar is the stress month, twice the worst the data ever showed, again with leverage: twenty four per cent.
- It is well above the limit.
- Look at what happened.
- The same strategy looks safe on the first bar and unacceptable on the third, and the only difference is whether anyone looked beyond the data.
- A model is a map of the past.
- Five A asks what happens off the map.

22 Judging a Standard V(A) case

Reasonable basis, three questions

Provider examined? → Model stress tested? → Supports the action?

IN THE LESSON

- When you meet a five A case, walk along this flow.
- Start on the left: did the manager examine the provider or the model, meaning its process, its assumptions and its record, or just rely on a pitch?
- In the middle: was a quantitative strategy tested properly, including stress scenarios and not just a back test?
- And on the right: does the analysis actually support the action and the client's objectives?
- If the answer to any box is no, the basis is not reasonable and adequate.
- Note one thing the Standard does not say.
- A good basis does not guarantee a good outcome, and a loss on its own is not a breach.
- A weak basis is.

23 Standard V(B): telling clients the truth

- Explain the process in outline, plus its risks and limits
- Tell clients promptly about material change
- Material change: leverage added, key manager lost
- Separate fact from opinion, and show assumptions

IN THE LESSON

- Now five B, communication.
- Clients are entitled to know how their money is managed, so the manager explains the investment process in outline: what is analysed and how decisions are made.
- The manager also tells clients the significant risks and limitations of that process.
- If something material changes, such as adding leverage or losing a key manager, clients must hear about it promptly, not at the next annual report.
- And the manager must separate fact from opinion.
- A past return is a fact.
- An expected return is an opinion, and should be labelled as such with its assumptions.
- A back test is a fact about a simulation, and not a promise.
- Mixing the two misleads clients.

24 How leverage changes the numbers

R(lev) = w × R − (w − 1) × b
σ(lev) = w × σ

Leverage	Assets held per unit of capital
Unlevered return	Return of the fund unlevered
Borrowing rate	Cost of borrowing
Unlevered volatility	Risk of the fund unlevered

IN THE LESSON

- Case seven needs one formula.
- When a manager adds leverage, borrowing money to hold more than the fund's own capital, two things change.
- The return becomes the leverage multiple times the unlevered return, minus the extra borrowing times the borrowing rate.
- So with leverage above one, the fund holds more than its capital and borrows the extra.
- The volatility, the risk, becomes the leverage multiple times the unlevered volatility, assuming the borrowing rate is fixed.
- Higher expected return and higher risk arrive together, which is why this is a material change that clients must be told about.

25 Case 7: the change nobody told Brightwater about

Brightwater 80m; leverage 1.5×; borrowing 3%

Amount borrowed	0.5 × 80m	**40m**
Levered return	1.5 × 6 − 0.5 × 3	**7.5%**
Levered volatility	1.5 × 10%	**15%**
Interest cost a year	3% × 40m	**1.2m**
Duty to the trust	prompt notice	**V(B)**

IN THE LESSON

- Case seven.
- The Brightwater Trust mandate has eighty million and has been unlevered, with a return of six per cent and volatility of ten per cent.
- Marlowe Quay now decides to hold one and a half times capital, borrowing at three per cent.
- That means borrowing forty million.
- The new expected return is one and a half times six, less half times three, which is seven and a half per cent.
- The volatility becomes fifteen per cent.
- The interest bill is one point two million a year.
- The fund's risk is half as high again, yet the trust has heard nothing.
- That is a material change to the process, so five B requires prompt notice, with its risks.

26 Fact or opinion?

Five lines from a client report

Returned 7.5% last year	**fact**
We expect 8% next year	opinion
Back test earned 9% a year	fact; label hypothetical
Interest rates will fall	opinion
Fees 0.80% plus 0.25% costs	fact; show all costs

IN THE LESSON

- A neat way to test five B is to sort statements into fact and opinion.
- Ines gives her team five lines from a client report.
- The fund returned seven and a half per cent last year: fact.
- We expect eight per cent next year: opinion, and it needs its assumptions shown.
- The back test returned nine per cent a year: a fact about a simulation, which must be labelled as hypothetical, and is not a promise.
- Interest rates will fall: opinion.
- Fees are eight tenths of a per cent plus a quarter of a per cent in costs: fact, and the costs must be shown as well as the fee.
- Mixing these up, with opinion dressed as fact, is how five B is breached.

27 Standard V(C): records belong to the firm

- Keep the research, model output, minutes and client papers
- Records are the firm's property, not the manager's
- Retention: local rules, else at least seven years
- Stored centrally, not in a personal inbox

IN THE LESSON

- Last, five C, records.
- A decision has two lives: the moment it is made, and the later day when a client, a regulator or a court asks why.
- The records that support the decision, such as the research, the model output, the committee minutes and the client communications, must be kept.
- They belong to the firm, not to the manager who produced them.
- That is why Dana's copying of model portfolios was a loyalty breach too.
- How long?
- As long as local rules require; where there are none, the Standards suggest keeping them for at least seven years.
- Where local rules set a period, that period governs.
- Records stored in a personal inbox do not count.

28 Procedures that make a reasonable basis routine

Controls for five A

Due diligence checklist	**same questions every time**
Repeat the checklist	periodically
Independent model validation	someone other than builder
Back and stress tests	documented before launch
Committee minutes	why it was adopted

IN THE LESSON

- Now the procedures.
- A reasonable basis is easy to claim afterwards, so firms make it routine.
- First, a written due diligence checklist for sub advisers, data vendors and third party research, with the same questions each time, repeated periodically because a provider that was sound three years ago may not be today.
- Second, independent validation of models, meaning someone other than the builder checks them, with back tests and stress tests documented before deployment.
- Third, investment committee minutes recording why each strategy was adopted.
- These three show that Marlowe Quay asked the questions before the money moved, and that the answers are on file.

29 Procedures for clients and records

Controls for five B and five C

Client documents	fees, costs, process, risks
Change management	prompt notice to clients
Projections	labelled opinion, assumptions
Retention policy	local rules, else 7 years
Central storage	the firm's property

IN THE LESSON

- For communication, the firm needs standard client documents that set out fees and all costs, the investment process and its main risks.
- It needs a change management procedure that triggers prompt notice to clients whenever the process, the key staff or the risk profile changes.
- Projections should be labelled as opinion, with their assumptions shown.
- For records, it needs a retention policy that follows local rules or keeps files for at least seven years where none exist, held centrally, because the records are the firm's property and not the manager's.
- Here are the five controls in one grid, which pairs with the earlier one.
- Together they make a complete set.

30 Case 8: fees, costs and the file

50m mandate; fee 0.80%; other costs 0.25%

Headline fee	0.80% × 50m	**400,000**
Other costs borne by fund	0.25% × 50m	**125,000**
All-in cost	1.05% × 50m	**525,000**
Approved in	committee minutes	**2027**
Keep until at least	2027 + 7 years	**2034**

IN THE LESSON

- Case eight shows two of those controls.
- Marlowe Quay's brochure for a fifty million mandate shows only the headline fee of eight tenths of a per cent, four hundred thousand a year.
- But the fund also bears other costs of a quarter of a per cent, one hundred and twenty five thousand.
- The all in cost is one point zero five per cent, five hundred and twenty five thousand.
- A client who sees only the first number has been told less than the truth, so the standard document must show all costs.
- Then the file.
- The committee approved the mandate in twenty twenty seven, so the minutes and tests must be kept in the central archive until at least twenty thirty four.
- Keeping them that long is simply good housekeeping.

31 From adoption to archive

Adopt

Checklist → Validated model → Minutes

Run

Client papers → Change notice → Central records

IN THE LESSON

- Let us put the controls on one picture.
- The top row is what happens when a strategy is adopted: the checklist puts the same questions to every provider, an independent person validates the model with its tests on file, and the committee minutes record why.
- The bottom row is what happens while it runs: client documents show fees, costs and risks, a change notice goes out promptly when something material changes, and the records are kept centrally.
- Notice how this covers all three parts of Standard five in order, five A on the top row, five B and five C below.
- A firm that can point to each box has made good conduct routine, and that is what the exam rewards.

32 Mistakes to avoid on Standard V

- 1. Letting an outside provider carry your duty
- 2. Treating a passed back test as enough
- 3. Waiting to report a material change
- 4. Treating records as the manager's own (keep 7 years)

IN THE LESSON

- Four mistakes cost marks.
- One.
- Thinking that hiring an outside sub adviser or buying outside research moves the duty to them.
- The manager still has to examine the provider's process, assumptions and record.
- Two.
- Thinking a quantitative model that passed its back test is ready.
- It needs stress tests beyond its data.
- Three.
- Thinking leverage or a key departure can wait for the next annual report.
- Material changes need prompt notice.
- Four.
- Thinking the records belong to the manager who made them.
- They belong to the firm, and the retention period is local rules or at least seven years.

33 Recap: both Standards in five lines

- IV(A): loyal until the last day; records stay behind
- IV(B) and IV(C): written consent; prevent, detect, act
- V(A): examine providers; stress test beyond the data
- V(B): tell clients; fact apart from opinion
- V(C): records are the firm's, kept at least 7 years

IN THE LESSON

- Let us pull the lesson together.
- First, under four A a manager owes the employer loyalty until employment ends: planning in personal time is fine, copying records or soliciting clients is not, and after leaving only memory and public sources may be used, subject to valid agreements.
- Second, four B needs written consent from all parties for client bonuses, and four C makes supervisors prevent, detect and act, with a system that is written, sized, communicated, followed and reviewed.
- Third, five A requires examined providers and stress tested models.
- Fourth, five B requires honest process disclosure, prompt notice and fact kept apart from opinion.
- Fifth, five C requires records kept as firm property.

34 Try three quick questions

1. Fund 50m; bonus 20% of return above 5%; fund earns 7%. Bonus, and what is needed?
   Answer: 2% × 50m = 1.0m; 20% = 200,000. Written consent from employer and client first.
2. Worst month −5%, leverage 2×, limit 12%. Stress of twice the worst: pass?
   Answer: −5% × 2 × 2 = −20%. That breaks the 12% limit, so no.
3. Decision made in 2028, no local rule. Keep records until at least?
   Answer: 2028 + 7 = 2035.

IN THE LESSON

- Now try three quick questions yourself.
- Pause after each one.
- Question one.
- A client of a fifty million fund offers the manager twenty per cent of any return above a five per cent benchmark, and the fund earns seven.
- What is the bonus, and what must the manager have first?
- Two points of excess on fifty million is one million, and twenty per cent of that is two hundred thousand.
- She needs written consent from her employer and the client before accepting.
- Question two.
- A strategy's worst month is minus five per cent, leverage is two times, and the clients' limit is twelve per cent.
- Does a stress of twice the worst month pass?
- Five per cent, times two for leverage, times two for the stress, is twenty, which breaks the limit, so no.
- Question three.
- A decision is made in twenty twenty eight, with no local rule.
- What is the earliest date to destroy the records?
- Seven years on is twenty thirty five, so the file stays put until then.