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Jonathan J. Stokes  
Associate, Standard Setting  
Association for Investment Management and Research (AIMR)  
P.O. Box 3668  
Charlottesville, Virginia 22903

Via E-Mail: [ethics@aimr.org](mailto:ethics@aimr.org)

Dear Mr. Stokes:

On behalf of the North American Securities Administrators Association (NASAA),<sup>1</sup> I am pleased to offer comments on the proposed changes to AIMR's *Code of Ethics and Standards of Professional Responsibility*.

NASAA commends AIMR for its attention to ethics issues. According to the Invitation to Comment, the proposed changes fall in the following areas:

- Reorganize the structure of the Code and Standards to improve clarity and understandability,
- Make substantive revisions to explicitly address current industry issues and promote best practices on a global basis,
- Revise standards to enhance global relevance, and
- Revise the text to make translations easier and to clarify language for a global audience.

Given NASAA's international membership and the growing globalization of finance, we particularly commend AIMR for efforts to make the standards relevant beyond the borders of the United States.

Many of AIMR's Chartered Financial Analyst (CFA) charterholders are investment adviser representatives or otherwise licensed by NASAA members. It is therefore important that your *Code of Ethics and Professional Responsibility* be consistent with existing regulatory requirements.

NASAA's Model Rule on Unethical Business Practices of Investment Advisers ("NASAA Model Rule") was first approved in 1985 and ratified, with amendments, by the NASAA membership on April 27, 1997. It has been adopted in some form by more than 40 states. A link to the Model Rule on Unethical Practices of Investment Advisers also may be found on our web site at [http://www.nasaa.org/nasaa/scripts/fu\\_display\\_list.asp?ptid=82](http://www.nasaa.org/nasaa/scripts/fu_display_list.asp?ptid=82).

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<sup>1</sup> The oldest international organization devoted to investor protection, the North American Securities Administrators Association, Inc., was organized in 1919. Its membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, Mexico and Puerto Rico. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

You specifically solicit comment on a number of questions. NASAA's responses to those questions regarding which it has an opinion (with the questions paraphrased from the original in some instances) follow.

### General Comments

*1. Do you support AIMR's effort to redraft the Code of Ethics and Standards of Professional Conduct in the manner proposed?*

Yes. Updating and clarifying the obligations of those in the financial services industry is of critical importance, especially in the areas where AIMR proposes enhancing its guidance: misrepresentation, manipulation, records retention, suitability, fiduciary duty, and non-public information. It is important that this be done in a way that leaves no ambiguity as to responsibilities.

*2. Is the language of the Standards straightforward and comprehensible?*

The language used generally is fine.

*3. What modifications, if any, should be made to this proposal?*

While there are separate discussions of a charterholder's obligations to a client and obligations to an employer, there is little material about the interplay of possibly conflicting responsibilities. The Standards should make clear that any doubt should be resolved in favor of the client.

*4. Are there other issues that should be addressed?*

It is difficult to write standards of general applicability that address all fact scenarios. However, recent publicity regarding abuses suggest that certain practices that are widely-acknowledged to be ethical violations should be expressly listed as prohibited practices. Another area that should be addressed is engaging in personal transactions such as loans with clients.

*5. Do any of the changes go too far?*

NASAA supports the broadest possible application of ethical standards.

### Specific Comments

*1. Are the new statement of principles recommended for the Codes of Ethics regarding subordinating personal interests and promoting market integrity appropriate? Should other broad principles be included?*

The principles are appropriate, but AIMR might consider being more specific in terms of "promoting market integrity." Possible areas that could be addressed are abuse of discretion, excessive trading, unauthorized trading, misrepresentation of qualifications, unreasonable fees, and guaranteeing results.

*2. Is the requirement under "Knowledge of the Law" to dissociate from unethical activity too onerous?*

No. Firms and individuals should not only understand and comply with all applicable laws and rules, but should have an affirmative duty to seek legal guidance if unclear regarding their responsibilities.

*3. Is the Independence and Objectivity standard overly broad?*

NASAA's view is that investment advisers have an affirmative responsibility to make compensation disclosures to clients. Furthermore, NASAA believes this is an ongoing

responsibility throughout the relationship with a client. Thus, Paragraph 11 of the NASAA Model Rule declares the following to be an unethical business practice for an investment adviser:

Failing to disclose to clients in writing before any advice is rendered any material conflict of interest relating to the adviser or any of its employees which could reasonably be expected to impair the rendering of unbiased and objective advice including:

- (a) Compensation arrangements connected with advisory services to clients which are in addition to compensation from such clients for such services; and
- (b) Charging a client an advisory fee for rendering advice when a commission for executing securities transactions pursuant to such advice will be received by the adviser or its employees.

Some difficulty could occur for an adviser if the “client” is the firm, as in the recent analyst conflicts-of-interest inquiry. The proposal should make clear that independence and loyalty also extends to investors, even when the investors are not clients in the normal sense.

4. *Do you agree with broadening of the misrepresentation standard?*

Yes.

5. *Is the misconduct standard overly broad?*

No; the proposal is correct in noting that *any* dishonesty, fraud, or deceit is improper.

6. *Is it appropriate to impose a duty to act with reasonable judgment and exercise reasonable care in all matters relating to clients?*

Yes; while we had some initial concerns regarding the removal of the term “fiduciary” from the standard because this is such a central concept, we note that references have been added elsewhere.

7. *Should AIMR require a written investment policy statement for clients?*

NASAA supports such written statements. Written statements and discussions with clients protect clients by providing clear information on which to base expectations. They are good business practice for AIMR members and industry in general.

8. *Should AIMR require some discussion with clients regarding risk and return?*

Discussion with every client is advisable. No matter what the client’s level of sophistication, risk and return should always be discussed in view of expectations.

9. *Is the language on Investment Guarantees sufficiently clear?*

The language in question is clear. It is similar to Paragraph 9 of the NASAA Model Rule, which prohibits guaranteeing a client a specific result from advice.

10. *Is it appropriate for AIMR to impose a general duty of loyalty to employers?*

As noted previously, NASAA is concerned about how an individual’s duty of loyalty to an employer will be resolved if there is a conflict with responsibilities to a client. It should be made clear that the client’s interests are primary.

*11. Is it necessary to require members and candidates to comply with an employer's policies and procedures?*

Compliance with lawful employer policies and procedures clearly should be a condition of continuing employment.

*12. Is the language on disclosure of conflicts sufficiently clear?*

The interests of clients should be given prominence, not the interest of employers. Otherwise, the provision is similar to Paragraph 11 of the NASAA Model Rule, discussed above.

*13. Should the provision on fee disclosure be expanded?*

The provision should be made consistent with the level of disclosure required on Parts I and II of Form ADV. Broad disclosure of all possible fees benefits both the client and the AIMR charterholder by eliminating confusion or misunderstanding.

*14. Should the provision on material nonpublic information be expanded, or is it sufficient?*

Under Paragraph 17 of the NASAA Model Rule, an adviser must “establish, maintain, and enforce written policies and procedures reasonably designed to prevent the misuse of material nonpublic information.” AIMR might want to consider adding requirements for written protections to this provision, especially given recent statutory enactments such as Sarbanes-Oxley that bear on misuse of information.

*15. Does the provision on market manipulation limit legitimate practices, and should an “intent” requirement be added?*

NASAA supports broad prohibitions on market manipulation and any conduct that would otherwise tend to work a fraud or deceit on the marketplace. We support the language as stated.

Thank you for consideration of these concerns. We understand that these proposed changes to AIMR's *Code of Ethics and Standards of Professional Conduct* may be further revised. As you proceed, NASAA would welcome the opportunity to continue working with you to accomplish shared objectives.

If you have any questions about these comments, feel free to contact me, Patricia Struck of Wisconsin, Chair of NASAA's Investment Adviser Section, or Mark Davis at the NASAA Corporate Office.

Sincerely,



Ralph A. Lambiase  
NASAA President  
Director, Connecticut Division of Securities