Ethical Decision Making

CFA Society of Milwaukee

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Ethics

- Effective
- Thinking about:
  - Honesty
  - Integrity
  - Character
- Suitability
Goal of Ethics Training

- To encourage you to become more conscious about your thoughts and behaviors, to increase the likelihood that you will notice and act upon ethical issues before they become destructive.
- To recognize that ethical dilemmas are a normal and predictable part of most jobs.
- To discuss approaches for dealing with ethical issues.
Code of Ethics

Ethics

Reasonable Care
Respect
Independent Judgment
Diligence
Competence
Professionalism
Integrity
Ethical Decision Making
Standards of Professional Conduct

- Professionalism
- Conflicts of Interest
- Duties to Clients
- Candidate & Member Responsibilities
- Duties to Employers
- Investment Recommendations
- Market Integrity
- Ethical Decision Making

Duties
- Ethics
- Ethics
- Ethics
- Ethics
- Ethics
Capital Markets Depend on Trust

Investors must have confidence in:

- Corporate leaders
- Accountants & Auditors
- Security analysts
- Asset managers
- Ratings agencies
- Consultants
- Financial institutions
Investment Management: A Business of Confidence

Between…

- Client and advisor
- Client and consultant
- Analyst and advisor
- Issuer and investors
- Issuer and analyst
- Investors and institutions
- more…
The Situational vs. Dispositional

Situational influences have more to do with unethical behavior than a person's character.

Under the right conditions good people can be induced, seduced, and initiated to act unethically.

Philip Zimbardo, Professor Emeritus, Stanford University
Unethical People vs. Unethical Actions

“The unethical actions of infamous wrongdoers who have recently populated the crime sections of the financial papers do not prove they are evil people. Instead they illustrate that the circumstances in which we find ourselves often (not always) have more to do with the decisions we make and actions we take than do our basic character traits.”

Robert A. Prentice, Ed & Molly Smith Centennial Professor of Business Law, McCombs School of Business, University of Texas, Austin
Factors Leading to Unethical Behavior

- Obedience to Authority
- Conformity Bias
- Self-serving Bias
- “Incrementalism”
- Groupthink
- Overconfidence
- Over-optimism
Your boss, who hired you and has mentored you for the past three years is being “let go.” A week before he is scheduled to leave, he places a stack of files on your desk and asks you to copy them, because he will need them in his job search. The files contain research reports that he wrote, marketing presentations containing his performance record, and spread sheets that he created. What should you do?

A. Copy the files.
B. Refuse to copy the files.
C. Speak to your boss’ supervisor.
D. Only copy certain files.
Law versus Ethics

Law: a clearly defined set of enforceable rules that applies to everyone. It represents a minimum level of expected conduct that everyone must observe.

Ethics: address situations not covered by the law (relations with competitors, interpersonal relations at work) and also contributes to the creation of laws.

“Honesty is the best policy. O.K.! Now, what’s the second-best policy?”
Fundamental Ethical Principles

• Client interests come first
• Maintain independence and objectivity
• Avoid/manage conflicts of interest
• Full and fair disclosure
• Preservation of confidentiality
• Fair dealing
• Reasonable care & prudent judgment
Rationalizations for Unethical Behavior

- Everybody else does it, so it must be okay.
- That is the way they do it at Firm X, so it must be okay.
- If we do not do it, someone else will.
- This is the way it has always been done.
- It doesn’t really hurt anyone.
- It's not a big deal.
- It's not my responsibility
- I want to be a team player, I want to be loyal.
Responses to Rationalizations

■ If it is standard practice, why is there a policy against it?
■ It may not hurt anyone now, but if everyone takes that approach it will matter.
■ It may not be a big deal to you, but it may be very important to others.
■ If a colleague requests your loyalty at the expense of your integrity, ask yourself whether the colleague is being loyal to you.
Key Points to Remember

- Client interests come first
- Functioning capital markets depend on trust
- Good ethics is fundamental to market integrity
- Clients demand ethical conduct from managers – not just good performance
- Employers demand ethical conduct from employees – not just good performance
A Framework for Ethical Decision Making

• What are the important facts?
• To whom is a duty owed?
• What are the issues?
• What are the ethical principles involved?
• Are there any conflicts of interest?
• How are the conflicts managed?
Resolving Ethical Dilemmas

1. Acknowledge that there is an ethical issue.
2. Determine who is faced with and owns the problem.
3. Gather the relevant data
4. Test the wrong vs. right parameters
5. Test for right vs. right paradigm
6. Apply the resolution principles
7. Investigate 3\textsuperscript{rd} way options - compromise
8. Make a decision.
9. Reflect on what you learn from the decision.
“I want employees to ask themselves whether they are willing to have any contemplated act appear the next day on the front page of their local paper – to be read by their spouses, children and friends-with the reporting done by an informed and critical reporter.”

Warren Buffett, Interim Chairman of the Board, Salomon Brothers