ETHICS IN PRACTICE: Just Being a Shrewd Investor.

CASE STUDY
Sung Kook "Bill" Hwang is the founder and lead portfolio manager of Tiger Asia Partners (TAP) and Raymond Park is a trader for the firm. TAP is participating in private placements for both Bank of China and China Construction Bank stock, and the placement agents shared confidential information with Hwang and Park about both companies. In the days prior to the private placement, Hwang directed Park to make short sales in each stock. TAP earned $16.2 million by using the discounted private placement shares they received to cover the short sales. Park's actions were

A. acceptable because he was following the orders of his superior.
B. acceptable because he used a short position rather than trading in the bank stock itself.
C. acceptable if the placement agents did not require a confidentiality agreement covering information about the private placements.
D. unacceptable because the trade was based on material nonpublic information.
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ANALYSIS
This case relates to trading based on material nonpublic information (MNPI). CFA Standard II(A): Material Nonpublic Information prohibits members who have MNPI that could affect the value of an investment from acting or causing others to act on that information. Hwang and Park received MNPI about the bank stocks from the placement agents as part of the offering process. Park is not exempted from the requirements of the standards simply because his boss directs that he violate laws or ethical standards, so Answer A is not correct. Park should have advised Hwang that the actions he was being asked to take were unethical and likely illegal and refused the directive to trade. The prohibition on using MNPI goes beyond the direct buying and selling of individual securities and extends to any related derivatives (e.g., swaps or option contracts), mutual funds, other alternative investments, so Answer B is not correct. It would have been advisable for the private placement agents to ask Hwang and Park to sign a confidentiality agreement, establish a "fire wall" around the disclosure of that information, and agree not to trade on the information. But even absent such an agreement, Park is prohibited from trading on MNPI, therefore C is incorrect. Because the trading was based on MNPI, the trade was improper and Park's conduct is unacceptable — Answer D.

This case is based on an enforcement action by both the US SEC and the Securities and Futures Commission of Hong Kong.