

NEWS RELEASE

FOUNDATION FOR FIDUCIARY STUDIES

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FOR IMMEDIATE RELEASE

Guide to SEC Proposal for Required Code of Ethics

The challenge of integrating regulations and ethics

Pittsburgh, PA, January 16, 2004—The **Foundation for Fiduciary Studies (Foundation)** has prepared the following response to assist members of the press and other interested parties in understanding the issues associated with the SEC proposal to require investment advisers to have a code of ethics.

The SEC voted on January 14, 2004 to propose new rules (204A 1 and related rule amendments under the Investment Advisers Act of 1940) which would require registered investment advisers (“advisers”) to adopt and enforce a code of ethics. The SEC proposal was prompted by the number of breaches of ethical and fiduciary conduct by investment advisers.

The SEC holds investment advisers to a fiduciary status, and the new rules are intended to reinforce the fiduciary principles that govern the adviser. Each regulated investment advisory firm will be required to have a code of ethics that includes, as a minimum:

- **Standards of Business Conduct.** The requirement to establish standards of conduct that are expected of the adviser’s supervised persons and that reflect the adviser’s fiduciary duties. Supervised persons would have to acknowledge, in writing, receipt of a copy of the code of ethics.
- **Compliance with Federal Securities Laws.** The requirement for the adviser’s supervised persons to comply with applicable federal securities laws.

- **Safeguard Nonpublic Information.** The requirement to prevent disclosure of material nonpublic information about the adviser’s securities recommendations and clients’ securities holdings and transactions to persons without a “need to know.”
- **Personal Securities Reporting.** The requirement for certain supervised persons (“access persons”) to report their personal securities holdings and transactions, including transactions in mutual funds advised by the adviser or an affiliate.
- **Pre-Approval of Certain Transactions.** The requirement for “access persons” to pre-clear any personal investments in initial public offerings and limited (private) offerings.
- **Reporting of Code Violations.** The requirement for supervised persons to promptly report any violations of the adviser’s code of ethics to the firm’s compliance officer or to another designated person.

The Foundation endorses the SEC’s proposal, but cautions that the suggested additional language represents more regulations, and not necessarily a code of ethics. The proposed regulations **may not** fully protect the investor, for they still prompt the adviser to investigate what is permissible but not what is right.

The Foundation proposes that the SEC augment the proposed “Standard of Business Conduct” to include a requirement for training in ethical decision-making, such as Casuistic Decision-Making (CDM). CDM already is widely used in religion and medicine, and is defined as the application of principles and ethics to aid in investigating and judging “right” from “wrong.” As it pertains to the investment industry, it would be the application of generally accepted fiduciary practices to help clarify legal, ethical, and moral decisions made by investment advisers.

As we’ve seen in the mutual fund scandals, there will be advisers who will hide behind the **letter** of the law in order to escape the higher demands of the **spirit**. Less ethical advisers and, in some cases, entire investment advisory firms have found ways to camouflage their self-centered interests behind a systematized scheme of codified conduct.

A well-defined code of ethics should be based on fiduciary practices to serve as the working guide for investigating and distinguishing “right” from “wrong.” However, ethical behavior cannot be simply a checklist of rules and regulations—it also must be a state of mind and an attitude. Ethical behavior requires more critical intelligence, more factual information, and a greater commitment to doing what’s right.

Investors are not going to let Wall Street return to business as usual. Investors are going to require evidence that investment advisers are meeting a higher standard of care than what is required by regulations alone.

*About the **Foundation for Fiduciary Studies (Foundation):** The **Foundation** was established in 2000 for the purpose of defining the practices that detail a prudent process for investment fiduciaries. The*

Foundation is part of the trilogy of organizations focused solely on the subject of investment fiduciary responsibility that make up the unincorporated entity, **Fiduciary 360** (www.fi360.com). The other associated organizations include the **Center for Fiduciary Studies**, which is associated with the **University of Pittsburgh Joseph M. Katz Graduate School of Business**; and **Fiduciary Analytics**, which develops Web-based tools based on the fiduciary practices for investment decision-makers.

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