CFA INSTITUTE

ETHICS IN PRACTICE:

Doing Too Much to Make Investments a Success?

CASE STUDY

Corrales manages a hedge fund that seeks out investment opportunities in developing markets. Using assets of the fund's investors, the fund hires local companies to serve as "sub-advisers" to explore and obtain promising investment opportunities and navigate local laws and regulation. The sub-advisers often have very limited experience as financial consultants or advisers but do have close relationships and connections with local high-ranking government officials. The payments made by Corrales, through the sub-advisers, often cover substantial "deal fees" and other expenses that facilitate governmental support of each investment. Corrales does not require the local business partners to provide details of their activities or what specific expenses are covered by the fees. Corrales reports these expenditures to fund investors as operating expenses necessary to the success of the investment. Over several years, the hedge fund is very successful producing an 18% annual rate of return for its investors. Did Corrales actions violate the CFA Institute Code of Ethics and Standards of Professional Conduct?

A. Yes.

B. No because it is acceptable to hire sub-advisers and business consultants to assist in procuring investment opportunities and managing specialized assets.

C. No because the payments to the sub-advisers represent legitimate expenses to ensure the success of investments and protect the interest of investors.

D. No, as long as the sub-advisers provide more detail about the nature and purpose of the payments and this information is disclosed to the hedge fund investors.