

Wednesday, November 30, 2022

THE BUSINESS TIMES

INSIGHTS FROM CFA SOCIETY SINGAPORE

Fund performance presentations – standards and potentially unethical practice

**By CFA Society Singapore
 Advocacy Team**

THE Christmas lights along Singapore's shopping belt have been turned on. Year-end is fast approaching. Most investors would want to take stock of their investments in 2022. Thereafter, some investors may make investment decisions for the year ahead. They may pour more funds into risk assets, liquidate certain investments, or stand pat with others.

Portfolio managers know the importance of the year-end period. In presenting performance reports to current and potential investors, managers must not engineer performance presentations. They must present credible performance information, and avoid misstating performance or misleading investors.

Investors may ask how much confidence they can have in managers to do what is right when presenting performance data.

CFA Institute is the global association of investment professionals that sets standards for professional excellence and credentials. Its Performance Presentation Standard requires managers and professionals to provide credible performance information to clients and prospective clients. This standard encourages full disclosure of investment performance data.

The standard covers any practice that would lead to misrepresentation of a manager's performance record, whether the practice involves presentation or measurement of performance.

This standard prohibits misrepresentations of past or reasonably expected performance. A manager must give a fair and complete presentation of performance information whenever communicating data on the performance history of individual accounts, composites or groups of accounts, or composites of an analyst's or firm's perform-

ance results.

The manager should also not state or imply that clients will obtain or benefit from a rate of return that was generated in the past. Whenever a manager provides performance information for which they are claiming responsibility – such as for pooled funds – the history must be accurate.

If the presentation is brief, the manager must make available to clients and prospects – on request – the detailed information supporting that communication. Best practice dictates that brief presentations include a reference to the limited nature of the information provided.

Ethics in action: Harmless allocation of expenses?

Here is a hypothetical base to illustrate the principles, written by Anna Sembos, a CFA charterholder. The desired ethical behaviour is based on the CFA Institute Code of

Ethics and Standards of Professional Conduct.

Huang SK, CFA, is a portfolio manager at an alternative asset management firm, Nonthaburi Capital. At the direction of her boss, she makes a one-time allocation of the expenses incurred by the Private Credit Opportunities fund to the Private Credit Special Situations fund. Her boss wants to temporarily boost the end-of-year results of the Private Credit Opportunities fund, which has been underperforming.

Boosting the performance of the Private Credit Opportunities fund would help to attract investors to the Private Credit Opportunities II fund. The consolidated performance results of Nonthaburi Capital are not affected by the reallocation of expenses between these two funds.

This case relates to CFA Institute Standard Performance Presentation Standard, which states that

charterholders must make reasonable efforts to ensure that the investment performance results communicated to their clients are fair, accurate, and complete.

Huang's actions are inappropriate because re-allocation of expenses between the two funds is a misrepresentation and not a fair, accurate, and complete presentation of the funds' performance, even though the consolidated results of Nonthaburi Capital are not affected.

Developing and maintaining clear and accurate communication with clients regarding the performance of their investments is critical because it allows clients to make well-informed decisions about their investment portfolios, including whether to withdraw their money from underperforming funds or to invest in follow-on funds. Any misrepresentation of performance, however temporary, affects investors' assessment of

their investments and subsequently their investment decisions.

In this case, Huang made the allocation of expenses at the direction of her boss, who had determined that the temporary boost of the Private Credit Opportunities fund's end-of-year results would benefit Nonthaburi Capital. But the interests of an investment professional's employer are secondary to protecting the interests of clients. In asking Huang to make the reallocation of expenses between the two funds, her employer is acting contrary to Huang's clients' interests. Following the direction of a supervisor does not excuse unethical behaviour or actions contrary to a client's best interests.

The writers are CFA charterholders who volunteer with the Singapore chapter on advocacy issues with a view towards promoting financial literacy among retail investors and improving overall standards and integrity in the industry.