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# Adviser Code of Ethics

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# Background

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- As fiduciaries, advisers generally owe clients a duty of undivided loyalty
- SEC has become concerned that advisers have lost sight of this duty
- Existing SEC rules lacked a thematic approach
- The SEC's new rule is designed to prevent fraud by more thematically reinforcing principles to govern the conduct of advisory firms and their personnel

# Code - Required Provisions

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- Codes must contain minimum provisions
  - But advisers can tailor their codes to best fit the structure, size and nature of their business
- Standards of business conduct for supervised persons
  - Reflect the fiduciary obligations of the adviser and its supervised persons
  - “Set out ideals for ethical conduct premised on fundamental principles of openness, integrity, honesty & trust”
  - Require compliance with federal securities laws
  - Require all “access persons” to report, and the CCO or delegate to review, personal securities trades and holdings

# Access Person Concept

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- Access person is any “supervised person” who
  - Has access to nonpublic information about any client’s purchase or sale of securities
  - Has access to nonpublic information about the portfolio holdings of any affiliated mutual funds
  - Is involved in making securities recommendations to clients
  - Has access to such recommendations that are nonpublic
- If providing investment advice is the adviser’s primary business, all directors, officers and partners are presumed access persons

# Holdings Reports

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- Access persons are required to report current securities holdings
  - Within 10 days of becoming an access person
  - At least annually thereafter
- Reports must reflect holdings as of a date not more than 45 days before the date
  - The person become an access person (initial report) or
  - The report is submitted (annual report)
- An access person can satisfy holdings report requirements by confirming in writing the accuracy of previously provided confirms & statements If
  - He or she previously provided them for all trades
  - The adviser kept them

# Content of Holdings Report

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- Title and type of security
- Exchange ticker symbol or CUSIP
- Number of shares and principal amount
- The name of the broker-dealer or bank with which the account is maintained
- The date the report is submitted

# Transaction Reports

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- Access persons are required to submit quarterly reports of transactions
  - Involving a “reportable security”
  - In which the access person had, or as a result of a transaction acquired, any direct or indirect beneficial ownership
- Transaction reports must be submitted no later than 30 days after the close of the calendar quarter
- Access persons with no personal securities transactions during the quarter are not required to submit a report confirming the absence of transactions

# Content of Transaction Reports

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- Date of each transaction
- Title of security
- Exchange ticker symbol or CUSIP
- Number of shares and principal amount (interest rate and maturity date, if applicable)
- Nature of transaction (i.e., purchase or sale)
- Price at which transaction was effected
- The name of the broker-dealer or bank through which the transaction was effected
- The date the report is submitted

# Reportable Securities

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- Reportable securities includes all securities except
  - Direct U.S. government obligations
  - Certain bank instruments and short-term debt instruments, including repurchase agreements
  - Shares issued by money market funds
  - Shares issued by other types of mutual funds
    - Unless the adviser or a control affiliate acts as the investment adviser or principal underwriter for the fund
  - Interests in variable insurance contracts funded by insurance company separate accounts that invest exclusively in unaffiliated mutual funds
- Transactions and holdings of affiliated mutual funds, closed-end funds, and offshore funds are not exempt from reporting

# Reporting Exceptions

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- Access persons are not required to submit any report:
  - For securities held in accounts over which the person had no direct or indirect influence or control
  - For transactions effected pursuant to an automatic investment plan
  - That duplicates information in trade confirmations or account statements the adviser holds in its records
    - If the adviser has receives them no later than 30 days after the close of the calendar quarter when the transaction takes place

# Beneficial Ownership

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- An access person must submit holdings and transaction reports for reportable securities in which he has, or acquires, direct or indirect beneficial ownership
- An access person is presumed to be a beneficial owner of securities held by his immediate family members sharing the same household

# Pre-Clearance Procedures

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- Access persons must obtain approval before directly or indirectly acquiring beneficial ownership in an
  - IPO
  - Private placement

# Reporting Violations

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- Supervised persons are required to report violations of the code to the CCO
- Advisers should foster an environment that encourages and protects supervised persons who report violations

# Informing Employees

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- An adviser is required to provide each supervised person with a copy of the code (and any amendments)
- Supervised persons are required to provide written acknowledgment of receipt (which may be electronic)
- SEC expects advisers to provide training on the principles and procedures of their codes

# Review & Enforcement

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- Advisers are required to maintain and enforce their codes
- Enforcement includes reviewing access persons' reports
  - Assess whether the access person followed procedures
  - Compare personal trading to any restricted lists
  - Assess whether the access person is trading for his own account in the same securities he trades for clients (and if so whether clients are receiving terms as favorable)
  - Periodically analyze the access person's trading patterns for possible abuse, including market timing
  - Investigate any substantial disparities between the performance the access person achieves for his own account and that he achieves for clients
  - Investigate any substantial disparities between the percentage of profitable trades when the access person trades for his own account and the percentage when he places trades for clients

# Recordkeeping

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- Advisers are required to keep
  - Copies of their codes
  - Records of violations and actions taken
  - Copies of supervised persons' written acknowledgment of receipt
  - Certain records about access persons:
    - Names
    - Holdings and transaction reports
    - Records of decisions approving acquisition of securities in IPOs and private placements

# Form ADV Disclosure

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- Advisers are required to
  - Describe their codes to clients
  - Furnish a copy to clients on request
- Advisers that materially deviate from policies and procedures disclosed in Form ADV could run afoul of anti-fraud provisions

# SEC Recommendations

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- Pre-clear personal securities trades by access persons
- Restricted lists of securities the adviser is analyzing or recommending for client transactions (or about which the firm has inside information)
- Blackout periods when client securities trades are being placed or recommendations are being made
- Reminders that investment opportunities must be offered first to clients and procedures to implement this principle
- Restrictions on short-swing trading
- Requirements to trade only through certain brokers
- Requirements to provide the adviser with confirms and account statements

# SEC Recommendations

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- Procedures for assigning new securities analyses to employees whose personal holdings do not present apparent conflicts
- Limits on acceptance of gifts
- Limits on accepting outside directorships of public companies
- Detailed identification of who is considered an access person
- Procedures for the firm and compliance personnel to periodically review the code and any reports made pursuant to it
- Discussion of specific penalties for violating the code of ethics
- Ensuring that employees receive adequate training about the principles, provisions and procedures of the code

# Action Items

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- By February 1, 2005, each adviser must
  - Adopt or revise its code and be prepared to maintain and enforce it
  - Identify all “access persons”
  - Provide a copy of the code to each “supervised person” and have received his or her acknowledgment
  - Have received an initial holdings report from each access person
  - Arrange for the submission of quarterly transaction reports by access persons
  - Update Form ADV

# Sources of Information

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- New Rule 204A-1
- Amended Rules 204-2 & 17j-1
- SEC Adopting Release
- ICAA Best Practices for Investment Adviser Codes of Ethics



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