H. KENT BAKER AND E. THEODORE VEIT*

How Ethical Are Investment Professionals in Switzerland?

1. Introduction

Investment professionals live in a world of moral ambiguity in which conflicts of interest and temptation for unethical behavior abound, but the investing public expects them to have high ethical standards. Yet, a danger exists in viewing ethics as a precise list of commands about behavior because many ethical issues in the investment profession are not straightforward or simple.

This study investigates the ethical attitudes and practices of investment professionals in Switzerland and compares the results to those of similar respondents in North America (United States and Canada). Few empirical studies examine the ethical behavior of investment professionals because collecting data on unethical behavior at the individual level is difficult. People are often unwilling to admit their own violations of ethical standards. Yet, ethical abuses by investment professionals do occur as reported by the financial press. Abuses are not limited to those countries that get the most attention in the financial press such as North America, Japan, Italy, and the United Kingdom, because they occur in every capitalist country.

Because people may give untruthful answers to questions about their ethical conduct, the study asks security analysts and portfolio managers about the ethical behavior of investment professionals they know. The study seeks answers to five key questions.

- How do investment professionals view their own ethical behavior compared with other professionals?
- What are the past and expected future trends in ethical standards of investment professionals in Switzerland?
- Where should investment professionals receive training and education about ethical behavior?
- What violations of legal and ethical standards occur most frequently among investment professionals in Switzerland?
- What are the most important deterrents to unethical behavior by investment professionals?

2. Previous Research

Most accounts of the ethical behavior of investment professionals have focused on violations reported in the popular press. Few empirical studies

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examine ethical behavior in the securities industry, especially in Switzerland. Two studies report the results of surveys of investment professionals.

BAUMAN (1980) asked members of the Financial Analysts Federation (FAF) and the Institute of Chartered Financial Analysts (ICFA) what they would do in various hypothetical situations, all of which posed ethical dilemmas. The study wanted to learn if FAF/ICFA members know how to, and would comply with, the joint Standards of Professional Conduct espoused by those organizations. Those surveyed held various job titles including portfolio manager, supervisor of portfolio managers, and supervisor of securities research analysts. BAUMAN concluded that financial analysts are generally committed to professionalizing their practice, to maintaining high standards of conduct, and to protecting the public interest.

VEIT and MURPHY (1992) surveyed 910 North American investment analysts, who were members of the Association for Investment Management and Research (AIMR). Their goal was to learn the views of investment professionals about various ethical issues. These issues included ethical trends in the investment profession, the effectiveness of various sources of ethics training and education, the frequency of ethics violations among investment professionals, and the most important deterrents to unethical behavior. This study provides an initial effort at identifying the extent to which investment professionals commit various unethical acts.

3. Methodology

The current study centers on the same ethics questions asked by VEIT and MURPHY (1992). Therefore, this study can compare the responses and identify differences because both the Swiss and North American surveys ask the same questions of investment professionals.

A questionnaire was developed based on the one used by VEIT and MURPHY. Several investment professionals in Switzerland reviewed the questionnaire during the development stage and suggested changes to improve clarity. The final eight-page questionnaire contained 19 questions and a respondent profile.

The sample of investment professionals consisted of 151 analysts and portfolio managers who worked in Switzerland and were AIMR members during 1993. AIMR has a worldwide membership of more than 27,000. No other investment organization has more investment professionals associated with it. Because the survey included only AIMR members, generalizing the findings of this study to other Swiss investment professionals requires caution.

To increase the response rate, the President of the AIMR sent prospective participants a letter encouraging them to participate in the survey. The first mailing of the survey instrument took place in late June 1993. A second mailing was done three weeks later to nonrespondents. Of the 151 investment professionals surveyed, 128 respondents returned completed questionnaires, yielding a response rate of 84.8%. The response rate for individual questions varies slightly because not all 128 respondents answered each question. Although survey research often suffers from non-response bias, the unusually high response rate and the assurance of anonymity for respondents should reduce this potential bias. Chi-square tests are used to test for significant differences between the Swiss and North American responses.

4. Respondent Attributes

Understanding the characteristics of the survey respondents is important when interpreting participant responses. The key attributes of the sample respondents follow:

- 86.7% are male.
- 78.9% are between the ages of 26 and 35.
- 27.3% have less than five years experience in the investment business; 50.8% have from 5 to 9 years experience; and 21.9% have 10 or more years experience.

Table 1: Opinions about the Perceived Ethical Behavior of Various Professions

Profession	Country	n	Not Ethical (1)	Somewhat Ethical (2)	Moderately Ethical (3)	Highly Ethical (4)	Chi-Square	Mean	Rank
Commercial	SW	128	2.3%	24.2%	60.2%	13.3%	0.765	2.84[a]	1
bankers	NA	396	2.0	25.3	62.1	10.6		2.81	3
Engineers	SW	127	6.3	21.3	54.3	18.1	47.930**	2.84[a]	2
	NA	391	0.0	4.1	55.2	40.7		3.31	1
Investment	SW	126	1.6	31.0	57.9	9.5	3.132	2.75	3
professionals	NA	395	1.3	23.3	64.8	10.6		2.85	2
Corporate	SW	128	3.9	37.5	53.1	5.5	14.259**	2.60	4
managers	NA	395	1.5	23.0	69.6	5.8		2.80	4
Attorneys	SW	127	7.9	38.6	43.3	10.2	2.226	2.56	5
	NA	398	10.6	41.2	41.2	7.0		2.45	5
Politicians	SW	128	33.6	50.0	14.1	2.3	4.439	1.85	6
	NA	399	41.4	48.1	9.3	1.3		1.70	6

SW = Switzerland and NA = North America
The percentages may not add to 100 due to rounding.
[a]The mean for commercial bankers is slightly above that for engineers.
**Significant at the 0.01 level.

- 40.5% have a bachelor's degree as their highest earned academic degree; another 46.0% have masters' degrees.
- 25.0% hold the Chartered Financial Analyst (CFA) designation and another 74.2% are enrolled in the CFA program.
- 86.7% engage primarily in "buy-side" activities (managing portfolios), 11.7% engage primarily in "sell-side" activities (marketing securities), and the remaining 1.6% said "other".
- 26.6% of the respondents are employed by investment counseling and management firms, 25.0% by brokers or investment banks, 15.6% by commercial banks, 11.7% in investment counseling and management, and the remaining 21.1% in other areas.
- 15.6% of respondents are employed by firms with at least 10 analysts and portfolio managers, 7.8% by firms with 10 to 39 analysts and portfolio managers, and 76.6% by firms having more than 40 analysts and portfolio managers.

5. Survey Results

5.1 Perceptions about the Ethical Behavior of Various Professionals

The first question seeks to find out how investment professionals perceive the actual ethical behavior of most people in six professional groups. Table 1 shows that the respondents view commercial bankers and engineers as more ethical than investment professionals. Most respondents view investment professionals as "moderately ethical". This response could reflect a bias from respondents about the ethical behavior of their profession. Corporate managers and attorneys rank fourth and fifth, respectively, in terms of perceived ethical behavior, while politicians rank a distant sixth. About a third of the respondents view politicians are "not ethical".
Chi-square tests reveal several significant differences between the responses from the Swiss and North American surveys. The Swiss respondents perceive engineers and corporate managers as less

ethical than their North American counterparts. Both groups perceive the ethical behavior of investment professionals in a similar manner.

5.2 Past and Expected Future Ethical Standards

The second research question focuses on learning the respondents' views about perceived trends in ethical standards of investment professionals in Switzerland. As Table 2 shows, almost 80% of the respondents believe that the ethical standards of investment professionals in Switzerland have improved over the past ten years. More than 87% expect the ethical standards of investment professionals to improve over the next ten years. These responses suggest investment professionals in Switzerland are optimistic about the recent past and the future in terms of ethical behavior in their profession.

The chi-square tests show significant differences between the Swiss and North American survey participants involving changes in ethical standards over both the past ten years and the next ten years. The perceptions of the Swiss respondents about perceived trends in ethical standards of investment professions are much more positive than those reported by the North American analysts in the VEIT and MURPHY (1992) study. Perhaps these differences result from the different periods during which the surveys occurred. For example, the North American study took place shortly after several insider trading and takeover scandals became highly publicized.

5.3 Sources of Ethics Training and Education

The third question asks respondents for their opinion on how much of an investment professional's training and education about ethical behavior should come from various sources. As Table 3 shows, the Swiss respondents believe that the largest amount of an investment professional's ethics training and education should come from

Table 2: Perceived Trends in Ethical Standards of Investment Professionals

	Switzerland	North America	Chi-square
Over the past ten years ethical standards of investment professionals in your country have:	(n = 128)	(n = 395)	
Improved	79.7%	24.3%	
Deteriorated	1.6	34.9	
Remained unchanged	17.2	27.6	
No opinion	1.6	13.2	135.335**
Over the next ten years ethical standards of investment professionals in your country are likely to:	(n = 127)	(n = 373)	
Improve	87.4	63.0	
Deteriorate	0.8	5.4	
Remain unchanged	11.8	27.6	
No opinion	5.4	4.1	28.210**

The percentages may not add to 100 due to rounding.
**Significant at the 0.01 level.

Table 3: Opinions About Appropriate Sources of Ethical Training and Education

Source	Country	n	None (1)	Small Amount (2)	Moderate Amount (3)	Large Amount (4)	Chi-Square	Mean	Rank
Senior management (by example)	SW	128	0.0%	3.1%	17.2%	79.7%	27.973**	3.77	1
	NA	400	0.0	7.5	40.3	52.3		3.45	1
Employing firm (training programs)	SW	126	0.0	5.6	27.8	66.7	60.518**	3.61	2
	NA	398	2.8	19.1	49.2	28.9		3.04	3
Professional organizations	SW	127	0.0	11.0	27.6	61.4	65.690**	3.50	3
	NA	396	3.8	23.2	49.7	23.2		2.92	4
Home environment	SW	127	3.1	11.8	20.5	64.6	19.335**	3.46	4
	NA	399	1.3	8.0	41.4	49.4		3.39	2
School, college or university	SW	128	1.6	12.5	43.8	42.2	106.125**	3.27	5
	NA	399	4.5	44.4	44.1	7.0		2.54	5.5
Religious education	SW	127	32.3	31.5	17.3	18.9	16.163**	2.23	6
	NA	392	20.4	25.3	33.9	20.4		2.54	5.5

SW = Switzerland and NA = North America
The percentages may not add to 100 due to rounding.
**Significant at the 0.01 level.

senior management (by example). Almost 80% of the respondents report that a "large amount" of ethics training and education should come from this source. The importance that respondents place on senior management underscores the critical role that mangers play in setting organizational norms for ethical behavior. Knowing the norms and the consequences may reduce the chance of investment professionals acting unethically.

Based on mean responses, three other sources of ethics training and education cluster below senior management. These sources are the employing firm (training programs), professional organizations, and home environment. School, college, or university rank somewhat lower and religious education ranks a distant sixth.

Based on the chi-square results, respondents from the Swiss and North American surveys differ significantly in their views on all six sources. Compared with their North American counterparts, the Swiss respondents believe a significantly larger amount of an investment professional's ethics training and education should come from all these sources except religious education.

5.4 Frequency of Ethics Violations

The fourth question examines the extent to which ethical or legal violations occur in the investment profession. Certainly, social norms influence ethical judgments of investment professionals. The legal system also provides a set of encoded norms for members of the profession. Although prevalent social norms influence legislation, the development of these norms typically precedes legislation. Therefore, behavior of investment professionals can be unethical but still legal.

The survey asks respondents to indicate the frequency of ten types of unethical or illegal behavior in the investment profession *based on their personal experience or observation.* As Table 4 shows, the most frequently cited violation is failure to disclose conflicts of interest to clients.

About a quarter of the respondents report this violation occurs "often", and almost 28% report it occurs "sometimes". The second most commonly cited ethics violation involves front running or making personal trades before client trades.

At least 40% of the respondents report that five of the remaining eight violations occur "sometimes" or "often". In declining order of frequency, these violations are failure to use diligence and thoroughness in making recommendations, trading based on inside information, communicating inside information, plagiarizing another's work, and not dealing fairly with all clients when taking investment action.

The results of the chi-square tests show significant differences between the responses of the Swiss and North American investment professionals on six of the ten ethical or legal violations. Compared with their North American counterparts, the Swiss respondents perceive three of these violations as occurring more frequently – failure to disclose conflicts of interest to clients, front running, and plagiarizing another's work. By contrast, the North American respondents observe three violations occurring more frequently than the Swiss respondents. These violations are failure to use diligence and thoroughness in making recommendations, communicating inside information, and

Table 4: Perceived Frequency of Various Ethical or Legal Violations

Violation	Country	n	Never (1)	Seldom (2)	Sometimes (3)	Often (4)	Chi-Square	Mean	Rank
Failure to disclose conflicts of interest to clients[a]	SW	127	18.1%	29.1%	27.6%	25.2%	45.489**	2.60	1
	NA	390	23.6	44.9	26.4	5.1		2.13	9.5
Front running (making personal trades before client trades)	SW	127	16.5	25.2	40.9	17.3	22.109**	2.59	2
	NA	388	25.8	38.9	27.1	8.2		2.18	8
Failure to use diligence and thoroughness in making recommendations	SW	126	11.9	39.7	30.2	18.3	15.781**	2.55	3
	NA	391	7.4	26.1	48.8	17.6		2.77	1
Trading based on inside information	SW	127	15.0	34.6	41.7	8.7	2.664	2.44	4
	NA	394	17.0	35.0	35.3	12.7		2.44	4
Communicating inside information[a]	SW	127	15.7	36.2	41.7	6.3	7.874*	2.39	5
	NA	394	11.9	33.2	39.1	15.7		2.59	3
Plagiarizing another's work	SW	126	20.6	34.9	31.7	12.7	10.319*	2.37	6
	NA	392	17.3	45.7	31.6	5.4		2.25	6
Not dealing fairly with all clients when taking investment action	SW	127	20.5	37.0	29.9	12.6	1.069	2.35	7
	NA	391	18.7	38.9	32.5	10.0		2.34	5
Writing reports that support predetermined conclusions	SW	124	23.4	37.1	29.8	9.7	14.097**	2.26	8
	NA	388	11.9	32.5	39.9	15.7		2.60	2
Failure to disclose conflicts of interest to the professional's employer[a]	SW	126	19.8	44.4	27.0	8.7	2.662	2.25	9
	NA	390	23.6	44.9	26.4	5.1		2.13	9.5
Misrepresenting a firm's past or expected future performance	SW	125	25.6	38.4	32.0	4.0	2.594	2.14	10
	NA	390	19.5	43.3	31.8	5.4		2.23	7

SW = Switzerland and NA = North America
The percentages may not add to 100 due to rounding.
[a]These questions are combined in the VEIT and MURPHY (1992) survey.

**Significant at the 0.01 level.
*Significant at the 0.05 level.

Table 5: Importance of Various Deterrents to Unethical Behavior of Investment Professionals

Deterrent	Country	n	Not Important (1)	Slightly Important (2)	Moderately Important (3)	Highly Important (4)	Chi-Square	Mean	Rank
Concern about disciplinary action by the professional's employer	SW	128	0.8%	7.8%	39.8%	51.6%	–	3.42	1
	NA	–	–	–	–	–		–	–
Concern about government sanctions	SW	127	3.9	19.7	37.0	39.4	2.924	3.12	2.5
	NA	397	2.5	14.9	43.1	39.5		3.20	1
Concern about sanctions from self-regulatory organizations	SW	127	1.6	19.7	44.1	34.6	31.529**	3.12	2.5
	NA	398	12.6	34.7	33.4	19.3		2.60	4
Having a published code of ethics	SW	127	6.3	30.7	40.9	22.0	26.673**	2.79	4
	NA	396	21.0	40.2	25.8	13.1		2.31	5
Concern that family or friends will find out	SW	128	5.5	34.4	38.3	21.9	3.655	2.77	5
	NA	398	7.3	28.9	34.7	29.1		2.89	3
Moral or religious beliefs	SW	126	15.1	33.3	23.8	27.8	17.386**	2.64	6
	NA	398	9.0	20.4	25.4	45.2		3.07	2

SW = Switzerland and NA = North America
The percentages may not add to 100 due to rounding.
**Significant at the 0.01 level.

writing reports that support predetermined conclusions.

To gain a better understanding of unethical behavior committed by investment professionals, the survey asked the Swiss participants if they had seen any unethical behavior by employees of their firms during the past twelve months, and if so, what actions they took. About a third of the respondents reported seeing unethical behavior by employees (compared with 24% in the North American study). Of the Swiss respondents, only 11.4% made the activity known to their supervisor or other person in the chain of command (compared with 41.1% in the North American study). A total of 31.8% of the Swiss respondents discussed the unethical behavior with the person making the infraction (compared with 31.6% in the North American study) and another 27.3% took no action (compared with 35.8% in the North American study). Of the remaining Swiss respondents, 6.8% made the activity known to the compliance officer, 4.5% took "other" action, and 18.2% took no action.

They survey also asked respondents if someone in the firm where they worked had ever asked them to do anything they considered unethical. Almost 27% of the Swiss respondents said that someone had asked them to do something unethical (compared with 23% in the North American study). More than 79% of these respondents said the person making the unethical request was senior to them (compared with about 89% in the North American study). Despite this, 54.0% of the Swiss respondents think their firm's senior management seeks high ethical standards for all employees (compared with 86.6% in the North American study). Given the importance that investment professionals place on senior management as a source of ethical training, this result is among the most important findings of the study.

5.5 Deterrents to Unethical Behavior

The final survey question asks participants to identify the importance of six specific factors in deterring the unethical behavior of investment professionals. Table 5 shows the most highly ranked deterrent given by the Swiss respondents is the concern about disciplinary action by the professional's employer. Almost 52% of the respondents believe this deterrent is "highly important". Despite the importance respondents place on the concern about disciplinary action from their employer, only 28.9% of the firms employing the Swiss respondents have a compliance officer to help ensure the maintenance of legal and ethical standards. Two factors tied for the next most important deterrent – the concern about government sanctions and the concern about sanctions from self-regulatory organizations.

The fourth most important deterrent is having a published code of ethics. The questionnaire also contained several questions about the existence of a code of ethics applying to investment professionals in the respondents' firms. The results show that only 24.2% of the respondents' firms publish their own code of ethics separately from that of any professional organization. Of the firms endorsing a code of ethics, either their own or that of a professional organization, 36.6% require their professionals to read it. Most (63.0%) of these firms require investment professionals to read the code of ethics only when employment begins.

The final two deterrents are concern that family or friends will find out, and moral and religious beliefs. The exclusion of the deterrent, concern about sanctions by the professional's employer, from the North American study precludes conducting chi-square tests and lessens the ability to compare the rankings between the two studies.

Based on the chi-square tests, two deterrents – the concern about sanctions from self-regulatory organizations and having a published code of ethics – are significantly more important for investment professionals in Switzerland than for those in North America. In contrast, moral and religious beliefs are a more important deterrent to unethical behavior of investment professionals in North America than in Switzerland.

6. Summary and Conclusions

This study reports the results of a survey of the ethical attitudes and behavior of securities analysts and portfolio managers in Switzerland and compares the findings with a similar study of investment professionals in North America. The Swiss study provides six key findings.

- Most Swiss investment professionals view their ethical behavior as "moderately ethical".
- Most Swiss respondents believe that ethical standards among investment professionals in Switzerland have improved over the past ten years and are likely to improve more in the next decade.
- Swiss respondents believe that the two most important sources of an investment professional's training and education about ethical behavior should be senior management (by example) and the employing firm (training programs).
- Respondents perceive that the two most common ethical or legal violations in Switzerland are failure to disclose conflicts of interest to clients and front running.
- Swiss respondents believe that the most important deterrent to unethical behavior of investment professionals is the concern about disciplinary action by the professional's employer.
- Only 54% of the Swiss respondents think their firm's senior management seeks high ethical standards for all employees.

The evidence provided by this survey suggests that instances of unethical or illegal behavior by investment professionals are still common. The frequency of various ethical violations requires additional effort, especially by senior management and the employing firm. Besides providing ethical training and education, organizations employing investment professionals should establish and enforce appropriate disciplinary actions to deal with those violating ethical standards. Endorsing a code of ethics and having a compliance officer to maintain legal and ethical standards may also be important steps in encouraging ethical behavior among investment professionals.

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