

Sameer / Faris¹ is an entirely fictitious case meant to assist in the learning and application of CFA Institute Code of Ethics and Standards of Professional Conduct.

Sameer / Faris Case Scenario

Sameer Mustafa, CFA, is the head of the trading department at SWM, a boutique investment manager in the Gulf Co-operation Council (GCC) region. SWM is involved in four main lines of business:

1. Investment Banking: The Investment Banking group provides corporate finance advisory, equity and debt capital markets, M&A expertise, private placements, structured investments and other services.
2. Sales and Trading: Sales and Trading offers access primarily to all MENA and GCC securities markets.
3. Asset Management: Two divisions:
 - a. Portfolio Management: offer high net worth investors, as well as institutions, tailor-made solutions through Discretionary Portfolio Management (DPM).
 - b. Fund Management: the firm offers a number of open ended funds with a GCC focus.

The company offers Shariah compliant solutions in both their Portfolio Management and Funds.

4. MENA Real Estate: The MENA Real Estate Department offers investors various real estate investment opportunities across the MENA region and advisory services.

Markets for trading in securities and commodities have been licensed in the GCC countries by various Securities, Capital Market and Commodities Authorities who prescribe rules and regulations in such areas as the Supervision and Control of Trading in the GCC Financial Markets.

The Asset Management business has been growing strongly. The “DIFC Wealth & Asset Management Report 2017: Mapping Opportunities in the MEASA Region” states that Total Assets under Management (AuM) by GCC fund managers is expected to rise from US\$45.8bn in 2016 to US\$110.9bn in 2020.

Sameer has been with the company for five years and he earned the CFA charter while working for SWM. Sameer is an expatriate resident of the country where he is working and is extremely grateful to have the opportunity as the economic situation in his home country is not good. Sameer sends about 25% of his gross salary back home to support his parents and help his younger siblings complete their studies.

Six months ago, Faris was hired by the CEO of the company to start to work in the Trading department under the supervision of Sameer. Faris is the nephew of the CEO and Faris’s father is a Board Member for Air GCC, a publicly traded regional airline.

As part of his regular duties, Sameer was reviewing the last month’s trading activity for the Discretionary Portfolios. These clients include investors and also friends and family of the CEO and other employees who trust the judgment and performance of SWM.

¹ This case was written by Ted Stephenson, CFA, CPA, CMA, CFP, MBA, Executive Director, CFA Society Emirates

In general, on average, SWM has been able to outperform the benchmark indices. With markets in the region being classified as “Frontier” and “Emerging”, markets are not as informationally efficient as “Developed” markets and there are opportunities to add alpha. “Informational market efficiency is the state in which available information regarding an asset is quickly reflected in the market price of that asset. Informational market efficiency is a theoretical idea rather than a precise description of actual markets. No asset market is perfectly efficient. Actual markets should be viewed as exhibiting different degrees of market efficiency.”²

Last month, October, was a very good month for several of SWM’s clients. Faris had made some very profitable trades. In particular, Faris had bought many shares of Air GCC at the beginning of the month which he then sold at the end of the month for a large profit. The buy orders were executed at several different prices over the course of three days and allocations were then made to client’s accounts. It caught Sameer’s eye that the best trades and prices and therefore the largest profits were done first and allocated to accounts of Faris and his family members including the CEO company before other clients of who have discretionary accounts at the firm.

On October 15, Air ME announced that it was planning to acquire Air GCC. The airline industry has had series of consolidations in many different countries and regions. There is much academic research on the issue of how stock prices and trading volumes respond to merger announcements. Research has shown that the stock price of the company being acquired almost always rises after an announcement and indeed this was the case for Air GCC. After the merger announcement, Faris had bought more Air GCC stocks but these trades were allocated to clients with smaller accounts.

Based on his excellent performance for the month, Faris was named the employee of the month and received a gift from the CEO. This was a monthly event that was meant to encourage members of the staff and boost morale and performance.

Sameer congratulated Faris but he had some concerns. Sameer was near certain that Faris must have gained knowledge of the upcoming merger from his father. The regulators in the GCC have clear rules on insider trading. The SCA in THE UAE for example states under Article 8³ that:

- 1- A chairman, board members or any senior executive in a Company whose Shares are listed on the Market, shall not trade, by themselves or through others or on behalf of others, in Shares without first disclosing to the Market the purchase or sale transactions, and the number and price of Shares.
- 2- It shall not be permitted for a chairman, members of the board of directors of a Company, any of the employees who has access to insider information to trade – whether by themselves or through others– in the securities of the same company or its parent company, subsidiary, affiliate or allied company if any of those companies were listed on the Market, during a period of (15) days prior to disclosing the financial statements of the Company and until they are disclosed.

² Alternative Investments: A Primer for Investment Professionals, Donald R. Chambers, CAIA
Keith H. Black, CFA, CAIA, Nelson J. Lacey, CFA. © 2018 CAIA Association.

³ <https://www.sca.gov.ae/english/regulations/pages/default.aspx?id=31>

In Saudi Arabia, Insider Trading is considered to be one of the illegal practices to article No. (50) of the Capital Market Law issued pursuant to Royal Decree No. (M/30).⁴

Sameer noted that no trades were allocated to Faris's father account held at SWM. Clearly that would be against the law.

Sameer gently raised his concerns with his boss Aisha, the Vice President for the department. He said "Aisha, I have some concerns regarding our trades for Air GCC. We did a lot of buying at the beginning of the month. With the merger and acquisition announcement on the 15th the stock went up 30%. Faris's father is a Board Member for Air GCC."

Aisha responded "Sameer, I hear your concerns and I have three points to make:

- 1- We are in the business of making money for our clients. Information is power. We work hard to have a strong network to get information and then use our skill to get profitable results. If we do not get the results, then we will lose clients and not attract new clients.
- 2- I will check the trading volumes on the market for Air GCC at the beginning of the month. If there is lots of trading volume, our buy orders will hardly stand out and attract any attention from the Regulators.
- 3- Surely you know that many firms all trade based on information gained through their networks. That is why we monitor the trades of other firms and sometimes copy their buy or sell orders if we see heavy volumes. Last year we saw RAAM buying lots of Peninsula Cement and so we followed those trades and recommended buying Peninsula to our clients. I know that RAAM has done some advisory work for Peninsula Cement in the past. Our clients did very well on those trades."

Aisha concluded by saying "business is business Sameer. No one can prove that we broke the law, I do not think that we broke the law. I understand and appreciate your concerns but we need to be careful. Faris is the nephew of the CEO and was employee of the month!"

In November, SWM acted as co-lead on an Initial Public Offering (IPO) for a Real Estate Investment Trust (REIT). After several years of quiet IPO activity in the GCC, IPO activity is picking up since 2017 representing an improvement in market conditions and investor confidence in the GCC. As with many IPOs the price appreciated rapidly after the listing. Staff at SWM had the majority of the share allocation and this is viewed as an important benefit to salaries and bonuses.

Discussion Questions

1. Identify potential violations of CFA Institute Code of Ethics and Standard of Practice. Should Sameer or anyone else report any violation(s) to CFA Institute and/or regulatory authorities? Why or why not? How does the reporting process benefit the profession? The capital markets? What circumstances would support such disclosure?

⁴ <https://cma.org.sa/en/Awareness/Publications/booklets/English.pdf>

Teaching Note: Suggested Issues for Discussion on Question 1:

Students can discuss what constitutes material nonpublic information, what makes such information material, and whether Faris is engaging in illegal insider trading. If students conclude that Faris is not breaking the law, they can discuss whether Faris's actions affect the integrity of capital markets and the possible impact.

Some students might point out that even if Faris is engaging in insider trading it is unlikely that it could be proved and that he would be detected and/or convicted. This can lead to further discussion about whether it is appropriate or advisable to engage in behavior based on the premise that detection and/or conviction is unlikely. SWM should consider not only the legal issues associated with material nonpublic information, but also the risk and burden associated with an unwelcome and intrusive investigation and the possible reputational risk involved.

Students can discuss how they would handle a situation that Sameer is in and the Responsibilities of Supervisors. How to manage Faris whose actions may be in conflict with acceptable standards while Faris is related to the CEO. In such situations, Sameer faces difficult decisions that may have significant ramifications on his career. Sameer did raise his concerns with his supervisor Aisha. There is no mention of a compliance department. Very difficult to dissociate. The guidance from CFA Institute on Knowledge of the law states that there is “no requirement to report violations to governmental authorities”.

Students can discuss Fair Dealing and the trade allocation procedures regarding Air GCC and the IPO. These violations of CFA Institute Standards are clearer and it is an opportunity for Sameer to educate SWM on the recommended practices and procedures.

Students can discuss Diligence and Reasonable Basis regarding the Peninsula trades.

Reporting violations to CFA Institute and/or regulatory authorities allows those organizations to both enforce the law and uphold professional standards. Those who report violations contribute to the integrity of the capital markets. Fair, efficient, and open markets attract investors and capital, thus contributing to the effective functioning of the economy.