

2008 FINANCIAL MARKET INTEGRITY INDEX

SWITZERLAND

CFA Charterholders and Professional Integrity

With offices in Charlottesville, VA, New York, Hong Kong, and London, CFA Institute is the not-for-profit, professional association of 98,000 financial analysts, portfolio managers, and other investment professionals in 128 countries, of whom 84,000 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute Centre for Financial Market Integrity is the research, policy, and advocacy arm of CFA Institute.

The CFA designation is widely recognized as the designation of professional excellence within the global investment community. CFA charterholders must pass three rigorous examinations that test their understanding of a number of financial disciplines, including ethics and professional standards, and must complete several years of qualifying financial work experience to earn the charter. To retain the designation, CFA charterholders also must annually renew their pledge to adhere to the CFA Institute Code of Ethics and Standards of Professional Conduct.

In 2002, when CFA Institute and the United Kingdom Society of Investment Professionals partnered, UKSIP members were adopted into CFA Institute and holders of the corresponding FSIP and ASIP designations were accepted into CFA Institute membership based on the comparable level of rigor needed to obtain these designations. Although all CFA Institute members adhere to an ethical standard, only CFA, FSIP, and ASIP designees also have displayed a level of mastery in investment principles. Therefore, this research does not include responses from all CFA Institute members but, rather, only from those who are active members with CFA, FSIP, or ASIP designations; all will be referred to collectively as “charterholders” throughout this report.

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Introduction

Value of the FMI Index

The Financial Market Integrity Index (the FMI Index) was developed by the CFA Institute Centre for Financial Market Integrity (the CFA Institute Centre) to gauge the perceptions investment professionals have about the state of ethics and integrity in six major financial services markets. Specifically, the index measures the level of integrity that investment practitioners experience in their respective markets—Canada, Hong Kong, Japan,

The FMI Index is distinguished from other market surveys and is proprietary in that it capitalizes on our exclusive access to seek the opinion and perspective of the CFA Institute membership (see inside cover for details). CFA charterholders are investment professionals who have earned the CFA designation and are required to adhere to a stringent code of ethics. The informed opinion of this particular respondent group offers valuable

The Financial Market Integrity Index was developed to gauge the perceptions investment professionals have about the state of ethics and integrity in financial services markets.

Switzerland, the United Kingdom, or the United States—and the practitioners' beliefs in the effectiveness of regulation and investor protections to promote such integrity. This pragmatic input from working investment professionals will help raise awareness of leading issues in the capital markets and will inform the work of the Centre in conducting regulatory outreach and developing enhanced professional standards.

insight into the current state of ethical practices and standards in select global markets and will help to inform regulators and other financial industry thought leaders concerning potential areas for improving the investment profession.

The CFA Institute Centre provides this report on the findings of the survey (the Report) to advance the cause of ethics and integrity in financial markets

*The CFA Institute Centre
provides this report to advance
the cause of ethics and integrity
in financial markets.*

through the views and opinions of trained investment professionals so as to:

- Inform investors and regulators of the perceived ethics and integrity of practitioners and the effectiveness of regulatory systems in the market;
- Encourage investors to consider whether they are likely to be treated fairly and ethically if they invest in the market;
- Help assess whether a particular country or market has specific integrity issues that need to be addressed by regulators; and
- Inform practitioners in the market about how others perceive their actions and honesty, in general, and to stimulate remedial actions on their part where appropriate.

Each FMI Index Report measures the sentiments expressed by a cross section of survey respondents concerning ethical standards and investor protections of a particular market. The ratings discussed in this Report represent the opinions of a distinct group of professionals, charterholders, responding to a series of questions about their experiences with practitioners, regulations, and investor protections in Switzerland. This survey was specifically designed to gather the perceptions of only the Swiss market. Because respondent populations differ significantly between markets, we believe it will be more valid and informative to assess each country's report independently of the others, rather than trying to make cross-country comparisons.

About the FMI Index Methodology

The FMI Index is constructed to give equal weight to two dimensions of evaluation: (1) the ethics of market participants and (2) the effectiveness of market systems in ensuring market integrity.

The CFA Institute Centre, in consultation with Harris Interactive, developed the FMI Index to specifically reflect the perspectives and opinions of investment professionals identified as being committed to the highest level of professional ethics. CFA charterholders and holders of the ASIP and FSIP designations were asked to evaluate and rate a number of financial “market participants,” including sell-side analysts, hedge fund managers, board

members, and others, and “market systems,” such as market regulation and investor protections, including corporate governance, shareowner rights, and transparency. The questions relate to how market participants and market systems contribute to financial market integrity. Respondents were asked to answer a number of questions that rate on a five-point scale the ethical behaviour of these market participants and systems.¹

FMI Index Questions and Rating Scales

Please rate the overall ethical behaviour exhibited by the following groups in Switzerland.



For each of the following, please rate the overall effectiveness of market systems for ensuring market integrity in Switzerland.



Figure 1

The ethical behaviour of market participants and the effectiveness of market systems were the two dimensions of evaluation that produced the final FMI rating.

More than 2,000 professionals in six countries who hold the CFA, FSIP, or ASIP designations participated in the research by taking the survey either online or by scripted telephone interview between 2 April and 8 May 2008.

To provide the most statistically reliable opinions, this Report will use in-market ratings when referring to an index rating or score, unless otherwise noted.²

Out-of-market ratings will be used for discussion and comparisons only where noted because these results are statistically less significant as a result of smaller sample sizes.

The FMI Index is constructed to give equal weight to two dimensions of evaluation: (1) the ethics of market

participants and (2) the effectiveness of market systems in ensuring market integrity. Data gathered during phone interviews were transformed so that they could be integrated with online responses. This is an opinion-based survey, and CFA Institute makes no representations concerning accuracy or otherwise warrants use of the FMI Index for any purpose by readers.

For more comprehensive information regarding the overall FMI Index methodology, please refer to the separate report available on the Centre's website at www.cfainstitute.org/centre.

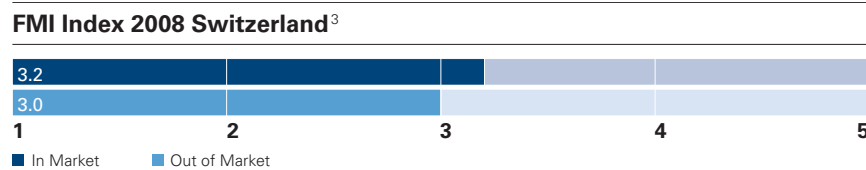
¹ One question dealing with severity of unethical behaviour or ethical lapses was an exception and listed a score of 1 as not severe at all and 5 as extremely severe. This question did not figure in the final calculations of the FMI rating.

² In this Report, in-market ratings are those from respondents inside Switzerland and out-of-market ratings are those given by respondents outside Switzerland.

Executive Summary

Figure 2

Respondents inside Switzerland gave the Swiss market a higher overall FMI rating (3.2) than did those outside Switzerland (3.0).



The overall FMI Index rating for the Swiss market came in just above the mid-range at a score of 3.2 on a five-point scale.⁴ This rating suggests that respondents see room for improvement in the state of ethics and integrity in the Swiss market. The global credit crisis that began in the United States in 2007 and spread around the world has had a detrimental effect on a number of global banking institutions, and large Swiss banks have not been immune. Such financial market turmoil likely weighed on the minds of respondents as they expressed their views on the ethical behaviour of their peers and on the regulatory and investor protections currently in place in the Swiss market when completing this survey. Although the overall ratings for most Swiss market participants and systems remain above a mid-range 3.0 rating, we would expect to see higher ratings for such a sophisticated financial market. We will have to see if

the market's ratings rise in the future or if respondents remain somewhat sceptical about the ethical behaviour of financial professionals and the effectiveness of market systems in Switzerland.

Based on respondent comments collected in the survey, transparency appears to be an area of primary concern. Issues such as conflicts of interest and regulation in the Swiss market also prompted comments from respondents. Financial advisers were the group of market participants that respondents most singled out for comment.

Meanwhile, based solely on the ethical behaviour of financial professionals and the regulatory and investor protections currently in place, respondents inside Switzerland were twice as likely to invest in the market as were those outside the Swiss market.

Conclusions

- The overall mid-range ranking of 3.2 that respondents assigned to market integrity signals that there is some perceived room for improvement both in the ethical behaviour of financial professionals and the effectiveness of market systems.
- Respondents generally rated the components of ethical behaviour of financial professionals slightly higher than they rated the components of the effectiveness of regulatory and investor protections.
- Based on ethics and integrity alone, 84 percent of in-market respondents were either likely or very likely to recommend investing in the Swiss markets, whereas those outside Switzerland were less favourable, at 45 percent.
- Respondents provided open-ended comments in addition to their survey rankings that indicate transparency, in general, and the ethical behaviour of financial advisers, in particular, are top areas of concern.

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³ A market's overall rating is composed of the 10 factors that make up the financial professionals rating and the 7 factors that make up the market systems rating. The final, overall rating for this market was created by taking the average rating or score from two sets of questions. The first question set contained 10 equally weighted components from a set of questions pertaining to investment professionals (i.e., market participants). The second question set contained 7 equally weighted components of questions pertaining to the effectiveness of capital market systems in ensuring market integrity. These two sets of questions were averaged as a set, and then each set carried equal weighting in the final determination of the FMI Index rating for this market.

⁴ Final rating is based on in-market ratings.

Key Findings

Ethical Behaviour of Individuals

The first group of FMI Index questions asked respondents their opinions concerning the ethical behaviour exhibited by various financial professionals—also referred to as “market participants”—in the market over the past year. The “all financial professionals” category received a rating above the mid-range, at 3.4. This rating is not simply an average of the nine

ratings linked to the ethical behaviour of specific professions but was asked separately as a control question. (The *average* rating of the nine professions is 3.3.)

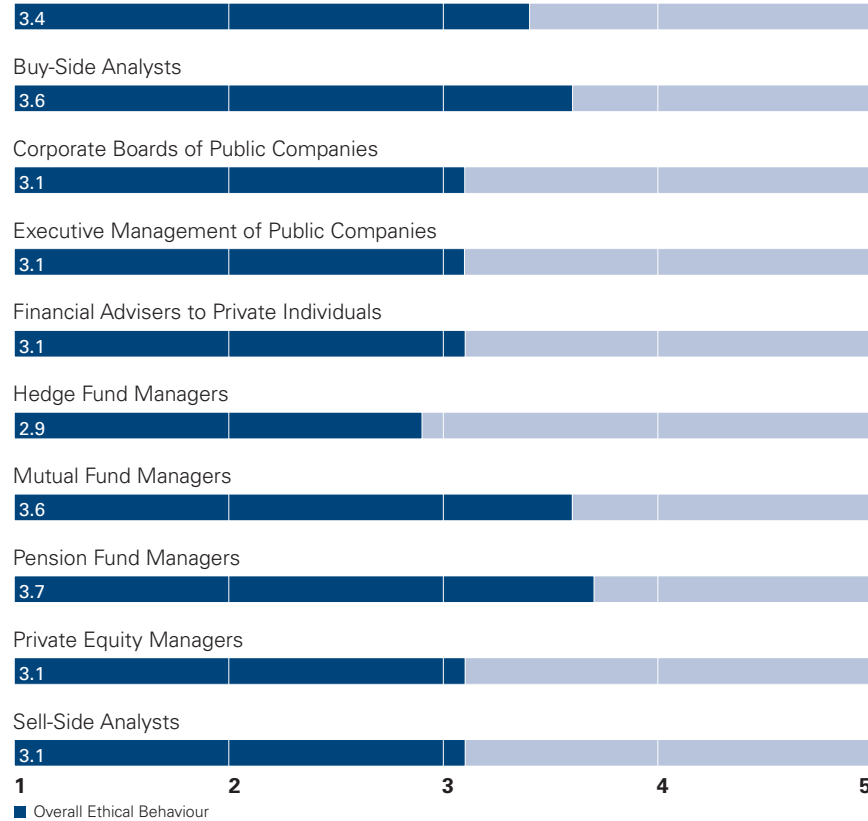
Of the nine professions listed in **Figure 3**, the ethical behaviour of hedge fund managers rated lowest at 2.9. They were also the only group

Figure 3

Respondents were asked to rate the ethical behaviour of financial professionals as a whole, as well as the ethical behaviour of specific financial professionals.

Ethical Behaviour of Individual Market Participants

All Financial Professionals



of all financial professionals in Switzerland to receive a rating below the mid-range of 3.0.

Respondents rated pension fund managers, mutual fund managers, and buy-side analysts more highly than the control question of “all financial professionals.” Financial advisers, private equity managers, corporate boards, executive management, and

sell-side analysts all rated just above the mid-range with a rating of 3.1.

In Switzerland, a high proportion of charterholders are buy-side professionals; 51 percent of those who answered this survey in Switzerland identified themselves as buy-side professionals.⁵ It is, therefore, important to note that buy-side respondents rated the buy-side analysts at 3.6, the

“

I guess most relevant in Switzerland is the integrity in the wealth management industry; I think, therefore, ethical training should be increased with financial advisers.

— Survey Respondent

”

⁵Please see demographic data at the end of this Report for more details about this survey.

Ethical Behaviour of Individuals

(continued)

same rating given by the rest of those rating the behaviour of these buy-side professionals. Sell-side analysts also rated the buy side at 3.6. Only about 14 percent of the Swiss respondents identified themselves as sell-side analysts.

Sell-side professionals gave sell-side analysts a rating of 3.3, yet their buy-side counterparts rated the sell-side analysts only 2.9.

When given the opportunity to provide open-ended comments on issues or

behaviours that they thought need to be addressed, respondents most often noted challenges related to advisers and conflicts of interest.

The topics of conflicts of interest and whether or not financial professionals always put their clients' interests first were not specific issues addressed in the survey questions, so it is quite interesting that respondents cited these issues more than any other as primary ethical concerns without prompting by the survey.

“
Financial advisers may mislead customers with advice that generates more/easier fees for the bank than adequate return for the investor.

— Survey Respondent

”

“
*Universal banking system
(asset management, investment
banking, custody business are
frequently parts of the same
company) creates potential
conflicts of interest.*

— Survey Respondent

”

Effectiveness of Regulatory and Investor Protections

The second group of FMI Index questions asked respondents their opinions concerning the effectiveness of regulatory and investor protections in the market (referred to as market systems) over the past year (see **Figure 4**). In the control question seeking ratings of “all capital market systems,” this group of investor protections received a rating of 3.3. This control question rating differed little from the *average* rating of 3.1 earned by the group, so

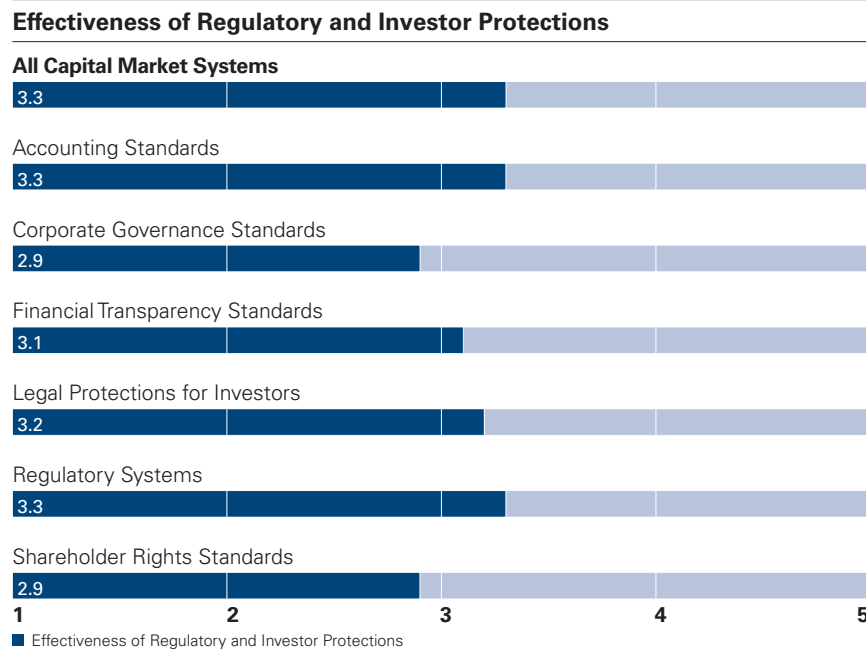
in this instance, the control question does a suitable job of aggregating the ratings of the other market systems.

Shareholder rights and corporate governance standards were the only investor protections that rated under a mid-level rating of 3.0.

Transparency was the market system that garnered the most comments from respondents. Given the leg-

Figure 4

Respondents were asked to rate the overall effectiveness of capital market systems as a whole, as well as the effectiveness of specific systems and standards.



“
Issues about retrocessions (‘referral arrangements’) going to private accounts or not disclosed by banks, e.g. one bank changed general contracts saying that all retrocessions are going to the bank and not to the clients; before that, it was done so without saying so.

— Survey Respondent

endary discretion of the Swiss in financial spheres, it is not surprising that transparency received the most attention. The comments concerning transparency did not focus on one area, however. Respondents showed concern over such topics as referral arrangements, a lack of general disclosure in the financial markets as a whole in Switzerland, transparency of fees, and transparency of conflicts of interests.

Respondents also were asked two subquestions about capital market systems that were distinct from the final financial market integrity rating of 3.2 for Switzerland. These questions were designed to further illuminate some of the reasoning behind the individual scores given to the various market system components. The first subquestion asked about the effectiveness of capital market regulation policies themselves. Specifically, we sought respondents’ perceptions on

Effectiveness of Regulatory and Investor Protections

(continued)

whether the regulations and investor protections available in the market represent industry standard or best practice and if implemented correctly, whether those market systems would offer a solid framework for investor rights. Respondents rated these regulations and policies as “good” by assigning an average rating of 3.1 out of 5.0.

The second subquestion focused on the effectiveness of implementation or enforcement of such regulations and policies. Respondents showed the same confidence in effective enforcement of existing regulations and policies as they did in the adequacy and level of regulation and policies. Respondents rated the enforcement process in Switzerland 3.1 out of 5.0 as well.

“
The ethical issue that investors have to face is fees. What I mean by this is that there may be a combination of private clients, banks, etc. where they charge certain fees without the investors knowing about it. There is a lack of transparency in the market, which needs to be addressed.

— Survey Respondent

”

Willingness to Invest in Switzerland

To test the connection between confidence in market participants and systems and the willingness to invest in Switzerland, we asked respondents about their willingness to recommend investing in the Swiss market based *solely* on the ethical behaviour of financial professionals and the effectiveness of capital market systems. The results demonstrated in **Figure 5** allow us to compare respondents' willingness to invest against the ratings they assigned

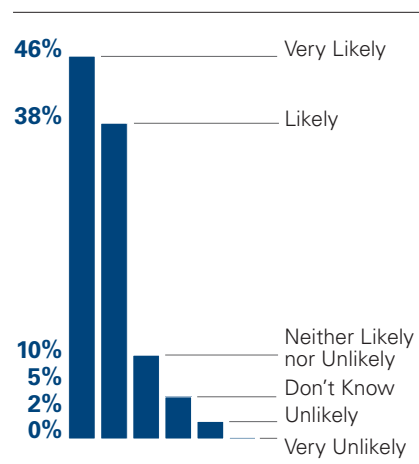
to the integrity of the market participants and systems in Switzerland.

Approximately 84 percent of Swiss respondents said they were either likely or very likely to make such a recommendation, and just about 2 percent of this group said they were unlikely to invest based on the same criteria. Although respondents within Switzerland proved confident in their market's integrity, far fewer of the respondents outside Switzerland said they were likely or very likely to invest in the market, signalling a potential cautiousness among investors outside Switzerland.

Somewhat surprisingly, only about 45 percent of those respondents outside the Swiss market (61 respondents total) were likely or very likely to make such a recommendation. It is unclear why there is such a disconnect between those inside and outside the market, but Switzerland's legendary lack of transparency may have something to do with such a difference. There may indeed be a large gap in the perceived image of Switzerland between those outside the market and

Figure 5

Likelihood of in-market respondents to recommend investing in Switzerland based solely on the ethical behaviour of market participants and the effectiveness of capital market systems.



Based Solely on Ethical Behaviour and Capital Market Systems, Would You Recommend Investing in Switzerland?

*May not add to 100% because of rounding.

those who operate in the market and perform due diligence or make investments in the Swiss market every day.

In assessing the integrity of market participants and systems, respondents outside Switzerland rated both participants and systems comparably to how the Swiss rated themselves (see next section). This finding suggests that the relative unwillingness of out-of-market respondents to recommend investing in Switzerland—despite the instruction to base their response solely on the integrity of market participants and systems—may be coming from some other area not addressed in this survey.

Perhaps the results reflect a diversification issue because the Swiss market is highly concentrated in a few industries, predominantly financials and to a lesser extent pharmaceuticals. A lack of willingness to invest may also reflect a desire to seek more diversified investment options or to avoid the troubled financial sector. Future surveys will further illuminate the reasons behind this disparity if it persists over time.

Other Key Survey Considerations

In-Market vs. Out-of-Market Perceptions

For purposes of this FMI Index, charter holders from five other markets we surveyed (Canada, Hong Kong, Japan, the United Kingdom, and the United States) were given the opportunity to rate and comment on both their own and the Swiss market. (Survey respondents were given the option to skip questions pertaining to any market about which they did not think they were knowledgeable.)

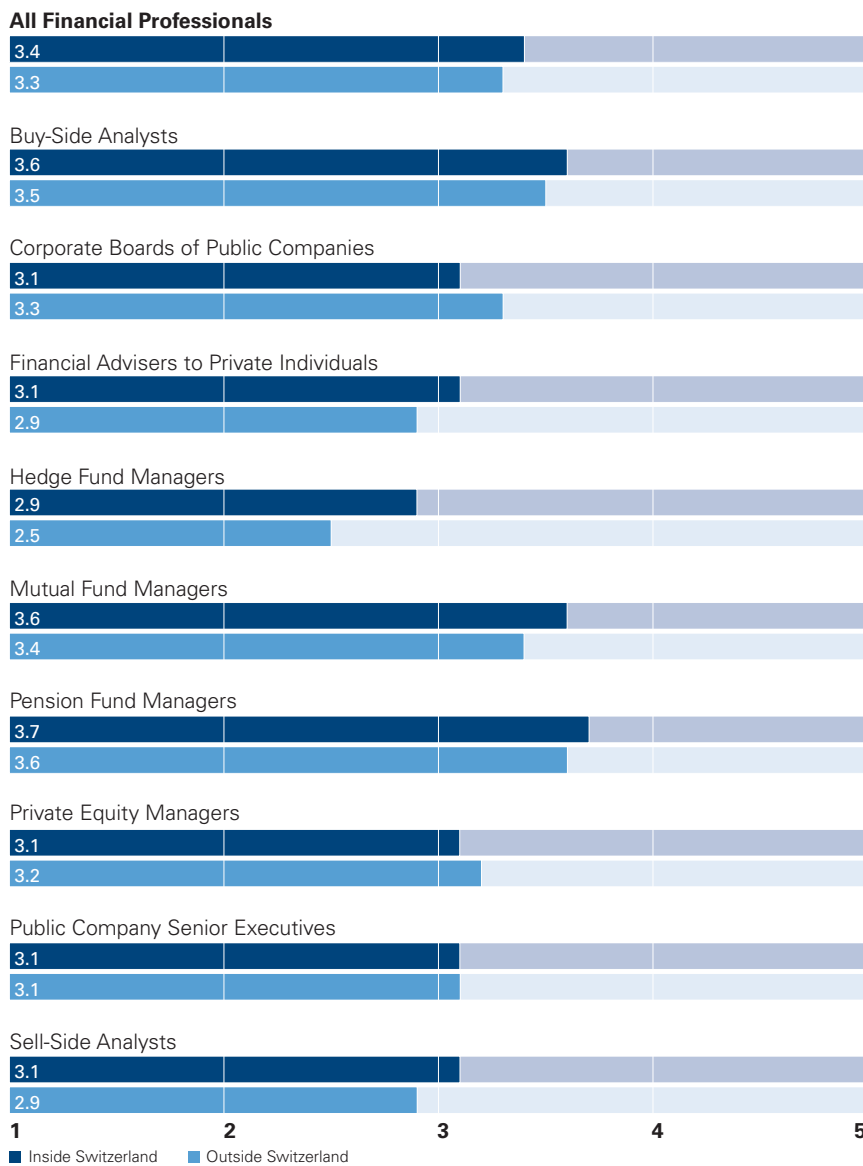
Survey respondents in Switzerland tended to rate both the integrity of individuals and the effectiveness of regulatory and investor protections

slightly higher than did those outside the Swiss market.

Figure 6 demonstrates that respondents in Switzerland consistently rated the ethical behaviour of financial professionals in Switzerland higher than did those outside the market. None of the differences between inside and outside ratings were judged to be particularly significant with just one year's data, except for the opinion of both groups concerning the ethical behaviour of hedge fund managers. Both groups rated hedge fund managers below a mid-range rating of 3.0.

Ethical Behaviour of Individual Market Participants

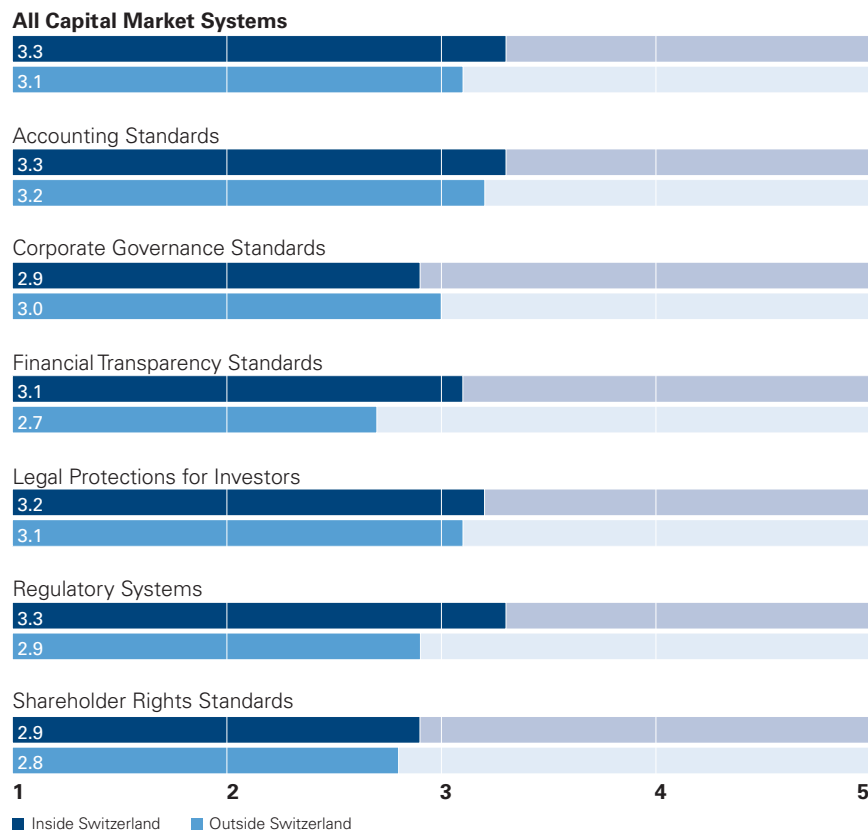
Figure 6



In-Market vs. Out-of-Market Perceptions

(continued)

Figure 7 Effectiveness of Regulatory and Investor Protections



Respondents from outside Switzerland consistently rated each individual market system slightly lower than did in-market respondents (see **Figure 7**). Based on our assessment, the only ratings that approach a meaningful difference between in-market and out-of-market ratings are the ratings concerning regulatory systems and transparency standards. We are interested to see if these relationships persist into the future, because it may be that Switzerland will continue to rate low in transparency from an outsider's perspective as a result of the country's reputation for financial discretion.

Comments of Survey Respondents

Respondents were given opportunities in connection with several of the survey questions to provide written comments about their thoughts and concerns. In particular, additional comments were solicited in the survey section concerning individual market participants and again after questions concerning market systems. At the

“no answer” or “nothing to add” types of remarks were excluded.

The various responses were examined and then categorized based on the main concern of each comment (e.g., corporate governance, transparency, fraud). The key areas of comment and the topics raised most often are

Figure 8

Survey respondents commented most about conflicts of interest/client interests, transparency, and advisers.

Issues Raised Most Frequently

Advisers	30 comments
Conflicts of Interest/Client Interest	21 comments
Transparency	14 comments

completion of the survey, respondents also were asked what additional or specific issues investors should be concerned about and for any other comments.

Nearly 200 substantive comments were received; those responding with

highlighted in **Figure 8**. In instances where an individual raised more than one concern, we identified the primary concern for this Report and noted any secondary or tertiary concerns, although these do not appear in Figure 8.

Conflicts of Interest

The most prominent and consistent commentary from respondents addressed conflicts of interest or putting a professional or personal interest ahead of clients' interests.

These concerns about conflicts were not concentrated on any one group of market participants or capital market regulations or systems. Rather, they reflect a broad concern among respondents that conflicts of interest need to be addressed more thoroughly in the Swiss market. One interesting comment we received multiple times concerned the issue of retrocessions or an undisclosed inducement. Eight respondents specifically addressed

retrocessions in their commentary; this specific issue did not come up with such frequency in any other market.

An analysis of this issue should include the recognition that sources of revenue for financial advisers in Switzerland are spread across diverse options (including volume-driven rebates). This system is unlike major Anglo-Saxon markets, where profits are usually more concentrated at the product level (while keeping overall banking fees relatively low). That being said, it appears that respondents see the need for more transparency about retrocessions in the Swiss market.

“
I would watch out for hidden fees and retrocessions deals that may make products/ services very expensive, thereby providing you with a lower return.

— Survey Respondent

”

Comments of Survey Respondents

(continued)

Transparency

We received 14 comments concerning transparency in the Swiss market. The concerns about transparency were not generally focused on any particular market regulation or group of market participants. However, the tenor of

these comments reflected especially on the disclosures expected of investment advisers; the topics of conflicts of interest and fee disclosure were the issues cited most often.

“

They should be sure that they get a balanced perspective from the persons who are selling to them or advising them.

— Survey Respondent

”

Financial Advisers

Although financial advisers as a group received a rating above the mid-point rating of 3.0, a number of respondents addressed concerns either about advisers directly or in connection with issues clearly linked to advisers, such as conflicts of interest and fee transparency.

“
I think the main problem is on a day-to-day basis, when the advisers look at what they can sell in order to make a transaction.

— Survey Respondent

”

Demographics

The following figures indicate some of the key demographic information about the respondent base (please see complete methodology report at www.cfainstitute.org/centre for further details). It is interesting to note that

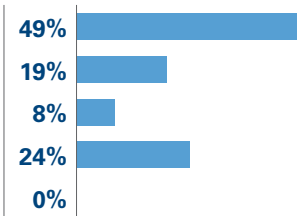
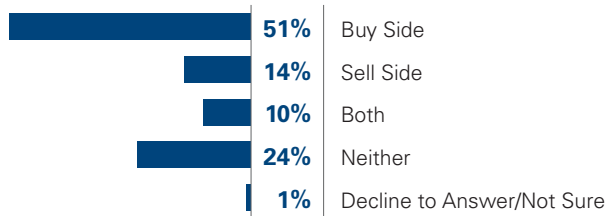
of the overall group of respondents, a large number indicated that they were working or employed in some capacity other than one of the practitioner categories identified in the survey.

Respondent Profiles for Swiss Market

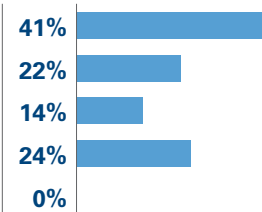
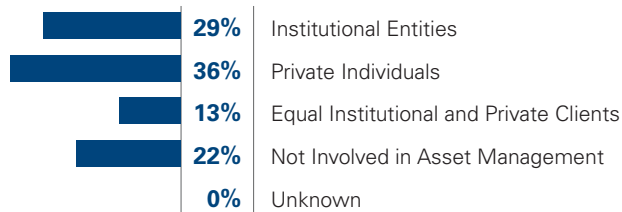
In Market (242 respondents)

Out of Market (61 respondents)

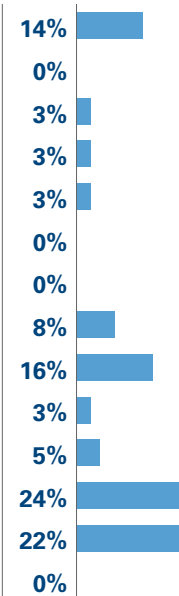
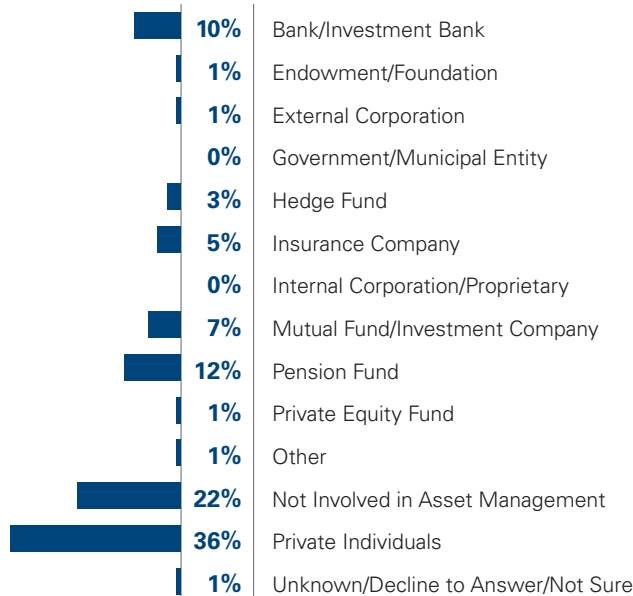
Buy/Sell Side



Client Asset Base



Institutional Asset Client Type

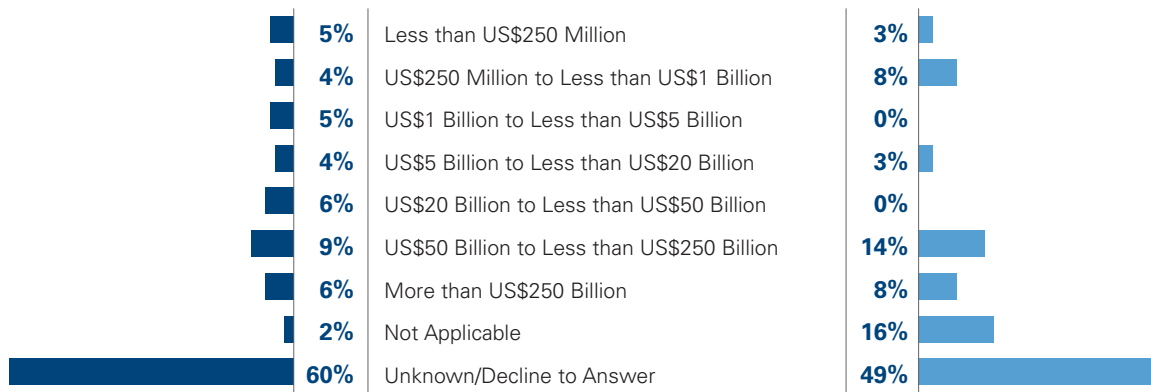


Respondent Profiles for Swiss Market (continued)

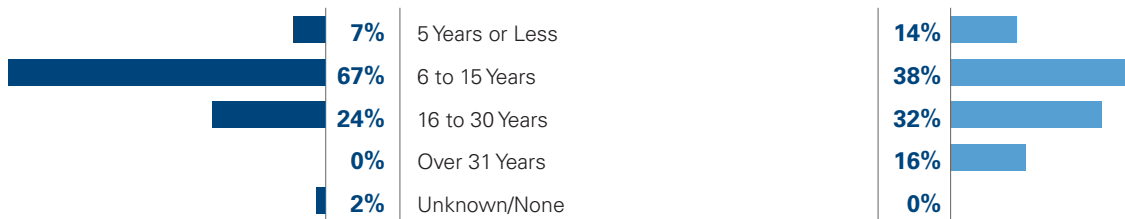
In Market (242 respondents)

Out of Market (61 respondents)

Assets Under Management



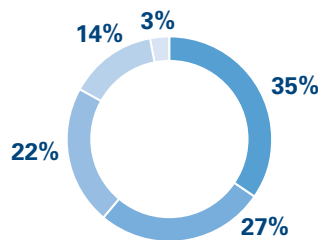
Years in the Investment Industry



Overview of Out-of-Market Respondents

Market

- 35% United Kingdom
- 27% Canada
- 22% United States
- 14% Hong Kong
- 3% Japan



*May not add to 100% because of rounding.

CFA Institute Centre for Financial Market Integrity

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