



June 26, 2009

**CFA Institute  
Centre for Financial Market Integrity  
Reference: Global Investment Performance Standards  
PO Box 3668  
Charlottesville, Virginia 22903**

**Dear Mr. Boersma:**

ClearBridge Advisors ("CBA") welcomes the opportunity to comment on the Exposure Draft of the 2010 Global Investment Performance Standards. We submit our comments with the common goal of supporting GIPS and advancing the development and practical application of the standards.

Our comments include the following:

**FUNDAMENTALS OF COMPLIANCE**

**1. Requirement 0.A.7:** Once a FIRM has met all applicable REQUIREMENTS of the GIPS standards, the FIRM MUST use one of the following compliance statements to indicate that the FIRM is in compliance with the GIPS standards. The compliance statement MUST remain in a single paragraph.

For FIRMS that are currently verified:

"[Insert name of FIRM] claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. [Insert name of FIRM] has been independently verified for the periods [insert dates]. A copy of the VERIFICATION REPORT(S) is/are available upon request. "

For FIRMS that have been verified, but are not currently verified:

"[Insert name of FIRM] claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. [Insert name of FIRM] has been independently verified for the periods [insert dates]. The FIRM is not currently independently verified.

For purposes of this provision, a VERIFICATION is considered current if the VERIFICATION REPORT covers a period ending not more than 24 months ago.

For FIRMS that have not been verified:

"[Insert name of FIRM] claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. [Insert name of FIRM] has not been independently verified."

**CBA Comment:** We support the concept of verification remaining a recommendation, and not a requirement of GIPS. We also support that a firm be required to disclose whether or not it has been verified. However, we believe the current requirement is more complicated than necessary. We

believe that the change could be accomplished with two compliance statements: one for firms that are verified and one for firms that are not verified.

We do not support the need for creating the concept of a “current verification” and defining it as a verification that has occurred within the past 24 months. As the compliance statement for a firm that has been verified does include the date of the verification, this will provide enough information for a potential client to decide if it is current in a way that is meaningful to it. Using 24 months as a limit seems a bit arbitrary. Some prospective clients may think 24 months is too short a time period, while others may think it is too long to provide meaningful assistance. We believe having a second statement for firms that have not been currently verified is unnecessary.

## **2. Requirement 0.A.11: Regarding Wrap-fee/SMA**

**CBA Comment:** This provision requires a firm to make every possible effort to get a complaint presentation to every prospective client, at least once a year. Regarding the Wrap fee/SMA business, we ask for clarification that delivering the compliant presentation to the wrap sponsor satisfies this requirement.

### **INPUT DATA**

**3. Requirement 1.A.2:** For periods beginning on or after 1 January 2011, PORTFOLIOS MUST be valued at FAIR VALUE in accordance with the GIPS Valuation Principles in Appendix D.

**CBA Comment:** We do not support a requirement for FAIR VALUATION. While we agree, conceptually, with this change, currently a firm is allowed to exclude from firm assets those assets which are based on cost or book values rather than market values. While accounting standards throughout the world are moving toward fair valuation, there are many firms that are not subject to SEC requirements. While we agree with the general idea of using fair value, we think it may be premature to require all firms throughout the world to use fair value at this time.

### **CALCULATION METHODOLOGY**

**4. Requirement 2.A.2:** TIME-WEIGHTED RATES OF RETURN that adjust for EXTERNAL CASH FLOWS MUST be used. Periodic returns MUST be geometrically LINKED. EXTERNAL CASH FLOWS MUST be treated in a consistent manner with the FIRM’S documented, COMPOSITE specific policy. FIRMS MUST define LARGE CASH FLOW for each COMPOSITE to determine when the PORTFOLIOS in that COMPOSITE are to be revalued for calculating performance.

**CBA Comment:** We support the proposed change.

### **COMPOSITE CONSTRUCTION**

**5. Requirement 3.A.6:** For periods beginning on or after 1 January 2010, CARVEOUTS MUST NOT be included in COMPOSITES unless the CARVEOUT is actually managed with its own cash balance.

**CBA Comment:** We support the redefinition of the CARVEOUT to ensure it represents a separate mandate managed in a particular style. We believe those in the industry who were stripping securities from a mandate, and calling it a CARVEOUT, were not acting in the spirit of the GIPS standards.

However, we strongly disagree with the removal of CARVEOUTS with cash allocation for purposes of COMPOSITE construction. It is unfortunate that the CARVEOUT with cash allocation has

received so much unwarranted negative attention. This practice has existed very long time in the US market place among firms with traditional balanced portfolios. Firms and verifiers alike have significant data which demonstrates that an unbiased cash allocation can be achieved and the results have shown immaterial differences between an equity segment plus allocated cash and a stand alone equity portfolio with cash. For firms with balanced mandates, we believe the use of CARVEOUTS (with a standardized, repeatable, documented cash allocation method) is a functional, cost effective, objective way of achieving single style portfolio returns for compositing. The new requirement forces both the manager and the client to force balanced accounts into sub-accounting structures. This restructuring of the portfolio may lead to increased costs to the client, without offering any measurable benefit. We respectfully suggest the Executive Committee reconsider this decision. In our opinion, the requirement that the CARVEOUT MUST represent a separate mandate managed in the style effectively solves the problem of potentially abusive CARVEOUTS (*i.e.*, stripping securities and calling it a mandate).

**6. Requirement 3.A.9:** FIRMS MUST NOT present a COMPOSITE to a PROSPECTIVE CLIENT known to have a PORTFOLIO with assets less than the COMPOSITE'S minimum asset level.

**CBA Comment:** We do not support raising this item from a recommendation to a requirement. More times than not, a Firm may not know the full assets involved in a new client situation until further into the discussions.

#### DISCLOSURES

**7. Requirement 4.A. 5:** FIRMS MUST disclose the presence, use, and extent of leverage, derivatives and/or short positions, if material, including a description of the frequency of use and characteristics of the instruments sufficient to identify risks.

**CBA Comment:** We support the proposed change.

**8. Requirement 4.A.16:** When presenting NET-OF-FEES RETURNS, FIRMS MUST disclose:

- a) If any other fees are deducted in addition to the INVESTMENT MANAGEMENT FEE and direct TRADING EXPENSES.
- b) If model or actual INVESTMENT MANAGEMENT FEES are used.
- c) If returns are net of PERFORMANCE BASED FEES.

**CBA Comment:** We support the proposed change and ask for further guidance on the appropriate handling of performance based fees within the composite net-of-fee return calculation.

**9. Requirement 4.A.20:** FIRMS MUST disclose the COMPOSITE DESCRIPTION which must include sufficient information to allow a PROSPECTIVE CLIENT to understand the key characteristics of the COMPOSITE strategy, including risks.

**CBA Comment:** We do not support this change which would include risk disclosure within the composite description. While we support full disclosure to prospective and existing clients, we do not believe the GIPS composite description or compliant presentation is the place for such information. We also believe that risk disclosure requirements properly belong with the appropriate regulators.

**10. Requirement 4.A.27:** If the FIRM has adopted a SIGNIFICANT CASH FLOW policy for a specific COMPOSITE, then the FIRM must disclose how the FIRM defines a SIGNIFICANT CASH FLOW for that COMPOSITE, and for which period(s).

**CBA Comment:** We view this as the same as the existing requirement from the Significant Cash Flow Guidance Statement. We support the simplification of this disclosure.

**11. Requirement 4.A.28:** FIRMS MUST disclose, for a minimum of 12 months, any change to the COMPLIANT PRESENTATION due to a correction of a material error.

**CBA Comment:** We support the proposed change and believe clarification on the minimum time frame such disclosures should remain. We request similar handling on other disclosure requirements in terms of minimum time periods for disclosure.

**12. Please find our response to the question posed in this section:**

- o Should firms be allowed to remove certain disclosures after a defined period of time?
  
- o If so, which disclosures would be eligible for removal and after what period of time?

**CBA Comment:** At present, in the absence of guidance which speaks to how long certain disclosures should remain in place, “firms” are hesitant to remove any – which leads to unnecessarily long disclosures. We support a minimum of 1 year for disclosures and removal of disclosures after 3 years. Firms should/could determine some disclosure should remain longer, as applicable.

**13. Requirement 4.A.29:** FIRMS MUST disclose the 3 year annualized EX-POST STANDARD DEVIATION (using a minimum of monthly periods) for the COMPOSITE and for the BENCHMARK as of the most recent annual period presented. The PERIODICITY of the COMPOSITE MUST be identical to the PERIODICITY of the BENCHMARK when calculating EXPOST STANDARD DEVIATION.

**CBA Comment:** While conceptually we support the change, it is unlikely that this risk measure will provide meaningful information for all managers, for all composites, in all markets. We recommend more latitude be given to the manager to present a different measure when warranted, with disclosure.

## **PRESENTATION AND REPORTING**

**14. Requirement 5.A.4:**

- a) Performance track records of a past firm or affiliation MUST be LINKED to or used to represent the historical record of a new FIRM if, on a COMPOSITE-specific basis:
  - i. Substantially all the investment decision makers are employed by the new FIRM (e.g., research department, portfolio managers, and other relevant staff),
  - ii. The decision-making process remains substantially intact and independent within the new FIRM, and
  - iii. The new FIRM has records that document and support the reported performance.
- b) The new FIRM MUST disclose that the performance results from the past firm or affiliation are LINKED to the performance record of the new FIRM,
- c) If a FIRM acquires another firm or affiliation the FIRM has 1 year to bring any non-compliant assets into compliance.

**CBA Comment:** We support the proposed change.

**15. Requirement 5.A.8:** For periods beginning on or after 1 January 2011, if a COMPOSITE contains any PROPRIETARY ASSETS, the FIRM MUST present, as of the end of each annual period, the percentage of the COMPOSITE assets represented by the PROPRIETARY ASSETS.

**CBA Comment:** We do not support the proposed change as it results in an addition to the table of data to present information that may be meaningless to the potential client. Any account that is discretionary and managed in the strategy should be considered an equal contributor to the return.

**16. Recommendation 5.B.6:** FIRMS SHOULD update COMPLIANT PRESENTATIONS quarterly.

**CBA Comment:** We do not support this recommendation. Significant resources go into the process of creating, reviewing, publishing, distributing and monitoring the annual compliant presentation. The interests of existing and potential clients would be best served for firms to spend their resources on GIPS oversight, procedures, error correction and the goal of producing error-free annual presentations.

#### **WRAP FEE/SEPARATELY MANAGED ACCOUNTS (SMA)**

**17. Provision 8.A.6** allows a firm to create sponsor-specific composites, versus style-specific composites.

**Please find our response to the question posed in this section:**

- Is it appropriate and/or necessary to include this provision (8.A.6), which addresses presenting performance to existing clients, in the GIPS standards?
  
- Should firms be allowed to present a ‘sponsor-specific composite’ as opposed to a ‘style-specific composite’?

**CBA Comment:** We support the continuance of this provision, and to allow for sponsor specific composites. This practice has been in place since the adoption of the Wrap-fee/SMA Guidance Statement and is widely used in this market. The sponsor is the client and the prospective client when considering wrap-fee/SMA. The ability to create sponsor specific composites has encouraged and enabled wrap managers to comply with the Standards and to address their clients’ needs. We would not support any change to the current provision.

#### **APPENDIX E – GIPS GLOSSARY**

**18. Definition of PROSPECTIVE CLIENT** Any person or entity that qualifies to invest in a COMPOSITE strategy (e.g., has assets above the COMPOSITE minimum asset level) and has expressed interest in one of the FIRM’S strategies. Existing clients may also qualify as PROSPECTIVE CLIENTS for any strategy that is different from their current investment mandate. Investment consultants are included as PROSPECTIVE CLIENTS if they represent investors that qualify as PROSPECTIVE CLIENTS.

**CBA Comment:** We do not support this definition as written as we believe it is much too broad. We see this definition issue as a very serious issue, as it is at the core of GIPS Provision 0.A.11 – which requires a firm to make every reasonable effort to provide a compliant presentation to all prospective clients.

Two examples that demonstrate how the proposed definition meaningfully alters two business sectors:

- a) Wrap-fee/SMA – Most wrap-fee/SMA end clients are contractually clients of the SMA Sponsor. The sponsor is the client and prospective client for the compliant firm. It is critical that the standards continue to support the acknowledgement of this client arrangement as set forth in the original SMA/wrap fee Guidance Statement. It is our concern, that as written – the requirement to deliver a compliant presentation to the end clients of the SMA Sponsor, exists. This is a significant issue, as many SMA sponsors contractually forbid the manager from reporting directly to the end client.
  
- b) Pooled Unitized Products: In our view, investors in mutual funds and other pooled unitized products cannot trigger this requirement. It is our concern, that as written – the requirement to deliver a compliant presentation to the investors in mutual funds and pooled unitized vehicles, exists. This is a significant issue that must be clarified.

We believe it may prove to be difficult to construct a single, simple definition of “prospective client” for the Glossary that would serve all client types, in all business sectors, in all markets world wide. To that end, we advocate removal of the definition from the Glossary and in its place we would suggest a requirement that a firm provide a written definition of “Prospective Client” in its GIPS Policy manual.

#### **19. DEFINITION OF PURE GROSS RETURN – NEW ADD**

**CBA Comment:** We support the addition of a definition of Pure Gross Return to be added to the Glossary.

Thank you for the opportunity to comment.

Sincerely,



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