

INVESTMENT ADVISER ASSOCIATION

June 29, 2009

Via Electronic Filing

Jonathan A. Boersma
Executive Director
Global Investment Performance Standards
CFA Institute
Centre for Financial Market Integrity
Reference: Global Investment Performance Standards
P.O. Box 3668
Charlottesville, VA 22903

Re: Exposure Draft of the 2010 Global Investment Performance Standards

Dear Mr. Boersma:

The Investment Adviser Association¹ appreciates the opportunity to comment on the significant proposed revisions to the Global Investment Performance Standards (GIPS Proposal).² If the revisions to GIPS are adopted, investment managers that claim compliance with GIPS would be required to adhere to the revised standards beginning January 1, 2011.

The IAA appreciates the review of the current standards by the GIPS Executive Committee of the CFA Institute. We believe many of the changes will achieve the CFA Institute's goals of eliminating GIPS provisions that are no longer necessary or relevant and maintaining GIPS' global relevance. We are concerned, however, that in an attempt to add new provisions to promote best practices in the performance presentation area, the CFA Institute may be implementing requirements only tangentially relevant to performance calculation and presentation and stepping into areas more appropriate for a regulator. We

¹ The Investment Adviser Association (IAA) is a not-for-profit association that represents the interests of SEC-registered investment adviser firms. The Association's membership consists of investment advisory firms that manage assets for a wide variety of institutional and individual clients, including pension plans, trusts, investment companies, endowments, foundations, and corporations. For more information, please visit our web site: www.investmentadviser.org.

² See GIPS 2010 Exposure Draft, available at, http://www.gipsstandards.org/news/releases/2009/pdf/gips_2010_exposure_draft_track_changes.pdf.

provide our general comments first and then discuss the specifics of the revisions in more detail below.

CFA Institute Should Avoid Adopting GIPS Provisions that Have Broader Implications for Investment Managers than Performance Calculation and Presentation

The IAA understands that many aspects of an investment manager's business may have relevance to the composition of a managed portfolio, which in turn may have some relationship to the calculation and presentation of performance of the portfolio. In the GIPS Proposal, however, we are concerned that two proposed revisions go well beyond performance into areas best left to regulators of investment managers. We respectfully request that these provisions be removed from the standards that are ultimately adopted or be reduced in scope so as to bear exclusively on performance calculation and presentation.

Risk Disclosure

The GIPS Proposal would amend section 4.A.20 of GIPS to require firms, in disclosing the composite description, to provide sufficient information to allow a prospective client to understand the key characteristics of the composite strategy, including risks. We fully support disclosure of material risks and providing clients with complete information. As fiduciaries, investment managers generally describe the material risks associated with particular investment strategies. A GIPS compliant presentation, however, may not be the appropriate forum in which to make such disclosures. A GIPS compliant presentation also is not typically tailored for a particular type of client and as such the "risk disclosure" may be too generic to be meaningful to a specific client.

Moreover, the disclosure regarding risks of a particular strategy goes beyond information necessary for clients to understand performance information and enters into regulatory territory more appropriately considered by regulators of investment managers, such as the U.S. Securities and Exchange Commission (SEC).³ We do not believe that GIPS should be used to "regulate" investment managers indirectly by imposing requirements not directly relevant to the accuracy of performance information. This approach is especially important in that GIPS is intended as "best practices" and not a regulatory requirement.

In addition, although we understand that some firms do provide risk disclosure to clients in GIPS compliant marketing materials, these disclosures are often in a different location than the area where performance information is provided. We request that section 4.A.20 be amended to eliminate any language relating to "key characteristics" and "risks."⁴

³ See e.g., *Amendments to Form ADV*, Rel. Nos. IA-2711, 34-57419; File No. S7-10-00, 73 Fed. Reg. 13598 (Mar. 14, 2008) at 13963 (discussing current SEC expectations regarding risk disclosure and proposing to include such disclosure under certain circumstances in Form ADV).

⁴ We note that corresponding changes should be made in other sections of the GIPS Proposal that propose to include disclosure about "risk." For example, the definition of "composite description" also includes information "to allow a prospective client to understand the key characteristics of the composite strategy, including risk." We believe this new proposed language should be removed.

An investment manager may decide voluntarily to include this type of disclosure in marketing materials, but the manager should not be required to include it as part of GIPS compliance.⁵

For similar reasons, we believe that section 4.A.5 should be amended to eliminate a requirement to disclose a “description of the frequency of use and characteristics of the instruments [*e.g.*, leverage, derivatives and short positions] sufficient to identify risks.”⁶ These disclosures again are intended to ensure a full and fair disclosure of an investment manager’s investment strategy rather than to promote the full and fair disclosure of an investment manager’s investment performance. We believe only the latter and not the former goal should be incorporated into GIPS; the broader goals should be left to the appropriate regulators.

Fair Value

Although valuing a portfolio appropriately is critical to the determination of performance, the GIPS Proposal should not require GIPS compliant firms to use fair value, as defined and applied under US GAAP, FAS 157, Fair Value Measurements.⁷ The guidance from which the GIPS Proposal is drawn is far from settled or definitive. We believe it is premature to incorporate the fair value standards as part of GIPS. As recently as April 2009, the Financial Accounting Standards Board (FASB) adopted new staff positions on FAS 157, Fair Value Measurements.⁸ Therefore, we urge extreme caution in attempting to codify FASB and IASB fair value guidance in GIPS at this time.

Moreover, as part of their compliance programs, SEC-registered advisers generally have adopted policies and procedures to value client holdings.⁹ These valuation policies and procedures are tailored for an adviser’s business and are drafted to be appropriate for the types of instruments in which the advisers would typically invest for their clients. For these reasons, the IAA urges the CFA Institute to not adopt the requirement for firms to fair value their portfolios under FAS 157. Instead, we suggest that GIPS require firms to disclose to clients their valuation policy upon request¹⁰ and recommend that firms consider fair value in

⁵ Despite our concerns, if the CFA Institute decides to adopt the risk disclosure provision, we request that the CFA Institute provide a sample risk disclosure.

⁶ Appendix C of the GIPS Proposal includes a similar disclosure requirement for advertising. We believe section B. 9 of Appendix C also should be amended to eliminate language about risks.

⁷ Appendix D – GIPS Valuation Principles of the GIPS Proposal would require firms claiming compliance with GIPS to fair value their portfolios.

⁸ In addition, President Obama’s financial regulatory reform proposal suggests that the SEC, the FASB, and the International Accounting Standards Board (IASB) review fair value accounting rules with the “goal of identifying changes that could provide users of financial reports with both fair value information and greater transparency regarding the cash flows management expects to receive by holding investments.” *Financial Regulatory Reform A New Foundation: Rebuilding Financial Supervision and Regulation* (June 17, 2009) at 11.

⁹ Rule 206(4)-7 of the Investment Advisers Act.

¹⁰ Similarly, we do not believe that firms should be required to disclose all “significant events that would help a prospective client interpret the performance record” in current section 4.A.19. We understand this current

their valuation policies. Clients who are interested in how their investment managers will value their holdings would be able to receive this information.

If the CFA Institute determines, however, to go further than our suggestions discussed above, we urge that GIPS only recommend firms to fair value their portfolios under FAS 157 and request several changes to the fair value provisions. First, section 4.B.2. of the GIPS Proposal recommends that firms disclose the key assumptions used to value investments. As noted above, discretionary investment managers generally have valuation policies and clients may request to see a copy of the policy. It is unclear whether clients would be interested in reviewing assumptions used to value investments, and we question the utility of disclosure of such information in a GIPS presentation. Instead, GIPS could recommend firms to disclose to clients that a firm's valuation policy is available upon request.

Second, the Introduction to Appendix D states that while some firms "may utilize external third parties to value investments, the FIRM retains its responsibility for compliance with the GIPS standards, including the GIPS Valuation Principles." We seek clarification that as long as appropriate due diligence is conducted on third parties, a firm would not be responsible for non-compliance by the third party that is beyond the control of the firm.

Third, even if the CFA Institute decides to recommend fair value generally, the current provision for private equity investments should be retained. The current standard provides investment managers with flexibility by requiring firms to justify why fair value was not applicable for private equity investments.¹¹ We believe that private equity investments will present difficulties in assigning a fair value especially in the early period after initial investment, and we request that GIPS retain the flexibility provided to investment managers.

IAA Suggests Modifications to Certain Proposed Revisions

In addition to our comments discussed above, we recommend a number of changes to specific provisions in the GIPS Proposal. We believe adopting the modifications suggested below would ensure that GIPS continues to be a global leader in performance standards without unduly imposing burdensome requirements on firms seeking compliance with the standards.

Claim of Compliance

Section 0.A.7 of the GIPS Proposal would require firms to make a statement about compliance depending on whether the firm is currently verified, has been verified but is not

requirement to be related to valuation; we believe, however, that it would be more helpful for clients to request disclosure of the valuation policy rather than a description of the significant events. If this requirement is intended as a general disclosure requirement, it is not clear what exactly should be disclosed. Investment managers have a duty to provide disclosure that would not make marketing materials misleading and generally have policies or procedures for identifying material events that must be disclosed. The proposed GIPS requirement does not enhance these current investor protection requirements.

¹¹ Appendix D – Private Equity Valuation Principles.

currently verified, or has not been verified. We have concerns with respect to the last two situations.

First, firms that have not been verified should not be required to disclose that they have not been verified. Under the GIPS Proposal, verification continues to be voluntary (which we support), and we do not believe a statement of non-compliance with a recommended practice is necessary. We are concerned that GIPS indirectly is attempting to turn a recommendation into a requirement by requiring advisers to make a statement that may have negative connotations. We request that the proposal to require firms to state that they are not verified be removed.

Second, firms that are not currently verified but have been verified in the past would be required to indicate the periods for which they were verified and to state that the firm is “not currently independently verified.” Because the year of the last verification is provided, we question the need for the additional statement that a firm is not currently verified. We request that the statement of not being currently verified be removed.

Finally, the GIPS Proposal would consider a verification to be current if the verification report covers a period ending not more than 24 months ago. If the CFA Institute does not remove the statement of not being currently verified as requested above, we suggest that a verification be considered current if a report covers a period ending not more than 36 months ago. Verification involves a significant process and can be quite costly. We question whether the benefits of obtaining a verification report more frequently, which is voluntary, would outweigh the costs. A verification report conducted every 36 months would provide adequate comfort that a firm is complying with GIPS. Moreover, clients and prospective clients will see the year of the last verification and can judge for themselves whether the verification is adequate based on the date disclosed.

Wrap Fee Accounts

In section 0.A.11, firms are required to make every reasonable effort to provide a compliant presentation to all prospective clients. For wrap accounts, we seek confirmation that if firms provide a compliant presentation to the wrap sponsors, this requirement would be deemed satisfied. In wrap account situations, investment managers typically do not have direct contact with the ultimate clients and the responsibility for providing material information rests with the wrap fee sponsors.

Firm Fundamental Responsibilities

In section 0.B.2, the GIPS Proposal would recommend that firms provide each existing client a compliant presentation for the composite in which the client’s portfolio is included on an annual basis. Although the recommendation itself is reasonable (and many firms already do so on a regular basis), we do not believe that it would be necessary to include such a recommendation in GIPS. After an individual or institution becomes an advisory client, the firms regularly provide reports to their clients. Moreover, clients and investment managers typically discuss the types of information that clients are interested in receiving

from their advisers. In addition, this type of recommendation does not further standardization of calculation and presentation of performance information.

Input Data

Section 1.A.1 of the GIPS Proposal would require all data and information to support “all items included in a compliant presentation” to be captured and maintained. Previously only items necessary to support the “performance presentation and to perform the REQUIRED calculations” were required to be captured and maintained. We are concerned that this change would require firms to capture and maintain supporting materials for all supplementary information that firms include voluntarily. We believe this proposal would impose a burden on firms that include information that is not required but is provided because it could be helpful to clients and prospective clients. This unnecessary requirement may discourage firms from providing supplementary information voluntarily.

Calculation Methodology

Section 2.A.2. of the GIPS Proposal would require firms to revalue portfolios in a composite for “large cash flows.” We understand that, although revaluation would be required only at the time of “large cash flows,” in practice and for operational efficiency, some firms may need to revalue daily because they may have to review hundreds of portfolios to determine whether there were large cash flows. For portfolios with fixed-income securities, this daily revaluation may be extremely costly because outside pricing services may charge a fee per bond valuation. Moreover, in times of high market volatility, a pre-determined “large cash flow” threshold may not accurately reflect the appropriate level of cash flow that should trigger a revaluation of a portfolio. For these reasons, we request that this requirement be eliminated from the GIPS Proposal.

If the GIPS Proposal is not amended to eliminate this requirement, we seek clarification of section 2.A.2, which uses the terms “external cash flows” and “large cash flows.” We recommend that the section refer consistently to “large cash flows” because that term is defined as the level at which a firm determines that a client directed *external* cash flow may distort performance if the portfolio is not revalued.

Non-fee Paying Portfolios

We support the goal of the proposed change in section 3.A.1 to require non-fee paying discretionary portfolios to be included in at least one composite – to prevent cherrypicking of non-fee paying portfolios. We request, however, that the language be revised slightly to require inclusion only of “portfolios in strategies that are offered to clients” in a composite. A firm may be investing its own assets in strategies that are specific to the firm’s particular needs and are not in strategies that are intended to be offered to outside clients. We do not believe that it would be helpful to include this type of portfolio in a composite. Similarly, this revised language also would relieve advisers of including portfolios that are managed as an accommodation or courtesy to specific clients and not generally offered to clients. Including

only non-fee paying portfolios that are intended to be offered to outside clients would make the composites more relevant and helpful to clients.

Composite Asset Minimum

In section 3.A.9, the GIPS Proposal would prohibit firms from presenting a composite to a prospective client known to have a portfolio with assets less than the composite's minimum asset level. We are concerned about this requirement because an investment manager may not know the amount of assets that a prospective client has or wants to invest with the investment manager until the prospective client becomes a client. Moreover, some firms that have a general minimum asset requirement may decide to waive the requirement under certain circumstances.

In addition, a composite that is the most relevant to a prospective client should be permitted even if the minimum asset level is higher than the client's portfolio assets so long as appropriate disclosure is provided to the client. Any potentially misleading information can be eliminated by requiring investment managers to disclose that performance may differ because of the minimum investment requirement.

Disclosures

The GIPS Proposal would amend section 4.A.7 to require firms to disclose if benchmark returns are net of withholding tax. We understand some index vendors are not public about how they handle withholding taxes or how material the treatment of withholding taxes is to their indices. Therefore, we request that this provision be revised into a recommendation rather than a requirement.

In Section 4.A.21, the GIPS Proposal would require the "nature" of a firm redefinition to be disclosed. We request that the term "nature" be replaced with "description" in the section. A description of a firm redefinition would more clearly indicate the information that should be disclosed for this proposed requirement.

Time Period for Disclosure

The GIPS Proposal requests comment on how long disclosures should be required to be included in a compliant presentation. We believe GIPS should provide investment managers with the discretion to determine how long the required disclosures should be included. This flexibility would permit investment managers to ensure that they include disclosures until they believe the presentation would not be misleading without those disclosures.

If the CFA Institute determines not to provide investment managers with such discretion, we recommend that disclosures be retained for one year. The disclosures subject to this period would include when (1) there is a change to the minimum asset level below which portfolios are not included in a composite (4.A.3); (2) there are significant events that would help prospective clients interpret the performance record (if this requirement is not

removed) (4.A.19); (3) there is a redefinition of a “firm” (4.A.21); (4) there is a composite name change (4.A.23); and (5) there is a change in the benchmark (5.A.6b).

Standard Deviation

We also request that investment managers be provided with discretion to determine whether the standard deviation disclosure should be provided (rather than being required to disclose standard deviation as currently proposed in 4.A.29). We are concerned that standard deviation may not be the appropriate measure for all strategies. Standard deviation may have limited value depending on the style of a specific strategy.

Recommended Disclosures – Benchmark

In section 4.B.3, the GIPS Proposal recommends that firms disclose the description of the benchmark and the material differences between the benchmark and composite strategy. Because firms are generally required to use an appropriate benchmark for a composite strategy, we are unclear about the information that should be disclosed regarding the “material” differences between the benchmark and composite strategy. Because firms may not be sure what information should be disclosed, this recommendation could lead to disclosure that is not meaningful.

Presentation of Supplemental Performance Information

Current section 5.A.2 states that firms may link non-GIPS compliant returns but that only compliant returns can be presented for periods after January 1, 2000. We request that firms that become newly compliant with GIPS be permitted to include non-compliant performance prior to the minimum five-period for which compliant performance must be shown. We seek guidance permitting newly compliant firms to show non-compliant performance as supplemental information as long as proper disclosure is provided.

Proprietary Assets

Section 5.A.8 of the GIPS Proposal would require firms presenting a composite containing any proprietary assets to disclose the percentage of composite assets represented by proprietary assets. Funds often include seed money, which remain in the fund until a critical number of shareholders or assets under management are reached. Because many funds may have small amounts of proprietary assets, it would be operationally burdensome to have to recalculate constantly the percentage of assets that have to be disclosed. For funds, we request that GIPS include a minimum threshold for disclosing proprietary assets.

Update of Compliant Presentations

Under section 5.B.6, the GIPS Proposal recommends that firms update the compliant presentations quarterly. Although a recommendation to update performance presentations quarterly may be appropriate, it would be difficult to update all of the other materials that are

part of a compliant presentation. We suggest that GIPS recommend that firms update the performance presentations quarterly and other materials at least annually.

Section 6 – Real Estate

The GIPS Proposal would add various new requirements and recommendations in section 6 for closed-end real estate funds. We believe that these provisions were intended for managers of closed-end real estate funds because they would have the requisite information necessary to comply with these requirements. Firms that merely invest in, but do not manage, closed-end real estate funds would not have access to the information required to be able to comply with these new provisions. We, therefore, seek confirmation that these provisions would not apply to firms that invest in closed-end real estate funds through, for example, private equity. Firms that invest in closed-end real estate funds through private equity would be required to comply with section 7 (Private Equity), which is discussed below.

Section 7 – Private Equity

Section 7.A.19 requires firms to disclose any period of non-compliance and meet the disclosure requirement for non-compliant performance. We seek clarification that the non-compliant performance would be for periods earlier than the minimum five year period.

In section 7.A.20, the GIPS Proposal would require reporting of SI-IRRs for the first partial year of performance. We request that this proposed requirement be removed from GIPS. It is difficult to calculate meaningful performance figures in the early stages of private equity investments. Private equity investments need time to convert committed capital to real investments that are able to generate a return. Therefore, we believe that performance during the drawdown period is not particularly meaningful.

In section 7.A.22, the GIPS Proposal would eliminate the requirement to report total invested capital for each period and impose a new requirement in section 7.A.23 to report the amount realized from the liquidation of investments. We recommend retaining the invested capital requirement because this figure is important.

Section 7.A.25 would require firms to use the same time period for the annualized SI-IRR for the benchmark as the vintage year of the composite. Previously, this requirement was imposed “if” a benchmark was shown. If no benchmark is shown, firms were required to explain why no benchmark was disclosed. The new proposed standard, however, does not appear to provide any flexibility for firm not to show a benchmark even if none is available. We note that section 5.A.6a states that if a firm determines no appropriate benchmark for a composite exists, the firm must disclose why no benchmark is presented. We understand that this general section would apply to private equity as well. We seek confirmation that GIPS will permit firms the flexibility to not show a benchmark if none is available.

Definition of Prospective Client

In Appendix E, the GIPS Proposal includes a definition for a “prospective client.” The IAA is concerned that the proposed definition may be too expansive. Inclusion of anyone who has “expressed interest” in a strategy may include competitors, journalists, commentators, and data vendors. We do not believe that the GIPS Proposal was intended to capture these types of persons. Therefore, we request that the definition be amended to reach those that have expressed interest in “investing” or “committing funds” in one of the firm’s strategies.

IAA Recommends Additional Changes to GIPS

In addition to the proposed revisions included in the GIPS Proposal, we discuss several areas where further guidance may be helpful to firms.

Hedge Fund and Master-Feeder Structures

Unlike for private equity and wrap-fee structures, GIPS currently does not provide any particular guidance for special issues that arise for creating composites of hedge funds or master-feeder structures. The IAA recommends that the CFA Institute consider providing some guidance in this area.

Complete List and Description of Firm’s Composite

Although we generally support the requirement for firms to provide a complete list and description of a firm’s composites, we believe additional guidance is necessary for firms that also advise mutual funds for which the GIPS compliant presentation is not being used to sell shares. Specifically, in the United States, a fund must provide a prospectus (full or summary) when using written materials to sell fund shares. Because these firms are not permitted to market these funds through a GIPS presentation and the number of funds may be numerous, we request that additional guidance be provided on the presentation of these funds when they are not part of a composite for a strategy being marketed.

Calculation Methodologies

Generally, the Calculation Methodology presented in the GIPS Proposal is workable in the context of a typical mandate to manage a portion or all of a client’s portfolio. The calculation methodology, however, does not fit well for a mandate that involves an investment manager providing overlay or only specific hedging strategies (*e.g.*, mandate to manage currency hedging) for a portfolio. We believe that the calculation methodology should include provisions to accommodate these types of investment strategies.

Time Period to Comply for Mergers and Acquisitions

Under current Section 5.A.4c, in the event of a merger or acquisition, firms have one year to bring non-compliant assets into compliance. We recommend this provision be

changed to permit firms 36 months to come into compliance with GIPS. In many circumstances, the integration of portfolio management processes may take more than a year, and we believe the pace of integration should be dictated by strategic considerations, not compliance with GIPS.

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We appreciate the opportunity to provide our views on these issues and would be pleased to provide any additional information. Please contact the undersigned or Karen L. Barr, General Counsel, at (202) 293-4222 with any questions regarding these matters.

Respectfully submitted,

/s/ Jennifer S. Choi

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