

December 31, 2004

CFA Institute
CFA Centre for Financial Market Integrity
Re: Guidance Statement on Portfolio Recordkeeping Requirements
Re: Guidance Statement on the Use of Leverage and Derivatives
Re: Guidance Statement on Wrap Fee/SMA Performance
P.O. Box 3668
Charlottesville, Virginia 22903

To Whom It May Concern:

Please find our comments to the Guidance Statements on Recordkeeping, Leverage and Wrap Performance attached. Please feel free to call if you have any questions or would like to further discuss any particular items.

Thank you for this opportunity to comment to your organization.

Sincerely,

Melvin W. Ashland, CPA, PFS
Partner

Tobin S. Cochran
Partner

Kimberly A. Cash, CPA
Partner

Timothy S. Simons, CFA, CFP
Partner

Attachment

Portfolio Recordkeeping Requirements:

Comments Requested

1. Yes, we support the principles established in this Guidance Statement.
2. No, the list included in the Guidance Statement appears quite thorough.
3. Yes, we believe that each firm should be able to decide internally what records are essential to support their compliance with the GIPS standards.
4. Yes, January 1, 2006 is a reasonable date to apply this guidance.

1) While we agree that the second guiding principle should not attempt to be an exhaustive list, we recommend that such records allowing for recalculation of account-level returns be required to be third party documents whenever third party documents can be obtained at the time the records are generated.

2) The last bullet item under the fifth principle should require that firms have a demonstrated system in place to prepare compliant presentations and supporting information in a reasonable period, upon request. Firms should be able to focus their time and resources on products that they show to external users. Restricted, small market value, and individual portfolio composites that will never be used or viewed by people other than regulators and internal personnel should not need to have fully compliant presentation prepared. Requiring firms to create and maintain presentations for all of them, regardless of whether or not any prospective client is interested in them, will create an unnecessary time burden, particularly when such presentations are not requested by the investing public, institutional or retail.

3) The eighth principle provides a list of recommended items to be maintained. The second bullet item is recommended if used to determine account composite assignment. Since the fourth principle requires maintenance of records to support why an account was assigned to a specific composite, we recommend moving this bullet item from a recommendation under the eighth principle to a requirement under the fourth principle.

4) We recommend that the fourth bullet item of the eighth principle be a requirement rather than a recommendation.

5) Item nine of page five: Why should verification reduce the record keeping requirements? We recommend removing this caveat, as it may encourage firms to destroy records once they have been verified. The SEC would still expect the adviser to maintain the necessary records, regardless of verification, and it becomes a verifier independence issue if the verifier plays a recordkeeping role.

6) We especially appreciated the Application's example #1, which highlighted that firms must maintain sufficient records to support the performance record and that this might include a combination of the types of records listed in the guidance statement, but not necessarily all of them. It would be superfluous to require the adviser to maintain all of the records described,



particularly since many include redundant information that may be satisfied by another of the documents.

Leverage and Derivatives:

Comments Requested

1. Yes, we support the principles established in this Guidance Statement.
2. No, the list included in the Guidance Statement appears quite thorough.
3. Yes, we believe that each firm should be able to decide internally what risk measures are appropriate to present for their specific strategy.
4. Yes, January 1, 2006 is a reasonable date to apply this guidance.

This guidance statement does not seem to require anything except for the establishment and maintenance of a leverage policy. Besides that, it describes various recommended (not required) risk measures that a firm utilizing leverage should be presenting. The statement appears to provide some good guidance on how these risk measures should be calculated, while not putting any additional unnecessary requirements on advisers.

We would appreciate some clarification from the IPC in regards to composites that do not contain leverage in their style, but for one reason or another, an account in the composite could be levered and still remain in the composite. An example would be an account that decides to leverage 5% of its account value in margin. The holdings and return on the account may still be very similar to the rest of the accounts in the composite, so should it come out or not? If not, does the firm need to disclose it is using leverage, albeit client initiated, in the composite if the returns have been calculated using an all cash methodology? If restating leveraged returns to cash is not an applied method, would it be appropriate for a firm to leave accounts in and disclose that they allow leverage in the composite up to some percent but that leverage is not part of the strategy?



Wrap Fee:

Comments Requested

1. Somewhat. We support CFA Institute's effort to develop guidance for the calculation and presentation of SMA/wrap fee portfolios. We are concerned that the calculated results that end up presented are often beyond the control of the managers participating in SMA programs, so a concerted effort with MMI or the SEC would be more effective. We applaud CFA Institute's decision to make the recordkeeping guidance only required on a go-forward basis.
2. Yes, eventually. Retroactively these requirements would have been very difficult for many firms to achieve, but on an ongoing basis they should be attainable.
3. Somewhat. It is not current industry practice in the U.S., as sponsors request gross institutional performance and managers claiming compliance give sponsors what they ask for in addition to the performance that receives the double hit.
4. January 1, 2006 may be a bit aggressive. We would recommend January 1, 2008 be the required date of compliance with this guidance, giving the MMI, separately managed account sponsors, portfolio accounting vendors, as well as managers, two more years to change their process. Imposing these standards on the managers without support from the rest of the industry would not be as effective.
5. No, we believe that CFA Institute is taking the appropriate steps to clarify the GIPS standards in terms of SMA/wrap portfolios if buy-in from MMI is obtained, so that application of this methodology is actually practised.

This guidance statement is very similar to the original guidance statement that received very negative responses.

1) Page 3 paragraph 2 refers to the glossary in the GIPS Fees Provisions for definitions. We believe that this would read better if the definitions were footnoted here.

2) Disclosure Requirement 4.A.16 requires firms to disclose the Fee Schedule appropriate to the presentation. If the portion of the wrap fee that is between the sponsor and the end user client is not provided to the investment manager, does showing net performance after deduction of actual fees and disclosing a management fee schedule and that a sponsor fee schedule is available from the sponsor suffice? This is a key area where the CFA Institute needs MMI or regulatory support before it can make this a requirement of investment managers.

3) The guidance statement would require firms that place reliance on performance calculated by the sponsor to obtain an agreement with the sponsor to secure the underlying records. Sponsors have been hesitant to make such blanket agreements in the past. Unless sponsors can be persuaded to acquiesce to this requirement, many advisers could be faced with an impractical choice (see comments in 2 above). Firms don't want to define their firm for AIMR-PPS or GIPS purposes to exclude wrap accounts (this is not even viable for firms who either specialize in wrap or whose marketing efforts are presently focused on wrap), and firms do not want to stop claiming compliance altogether.



4) 4.A.18-20: In a bundled fee arrangement advisers are sometimes able to distinguish among the various fees in the “Bundled Arrangement”. In other cases they are not. Since the disclosure is contingent on the sponsor’s cooperation, we recommend that the requirement include the phrase “to the best of their knowledge”.

5) Page 6, 4.A.18 could provide more explanation as to the various types of fees that are required to be disclosed.

6) Page 8, Paragraph 3 states that a firm “must be sure” that the performance provided by wrap sponsors be in compliance with the standards. We recommend that this be revised to say that a firm gain “reasonable assurance”.

7) We believe that support from the SEC should be obtained via a no action letter before a guidance statement allows exemption for managers to maintain books and records prior to 1/1/06; otherwise, the Standard’s requirement that managers follow their country’s regulatory advice would override this guidance. We also recommend this section be revised to state that obtaining the sponsor returns will be sufficient, as opposed to not having any recordkeeping requirements at all prior to 1/1/06.

8) Performance Presentation (Page 11): “Investment management firms must group SMA portfolios in a composite according to the same investment style or strategy, regardless of the SMA sponsor”. We agree with making this a requirement for theoretical reasons. However, prospective sponsors currently ask for institutional performance, and managers provide the sponsors what the sponsors ask for. A composite mixture of sponsors would include a mixture of wrap fees, which can have a wide spread depending on the sponsor, and this renders a net-of-all fee composite less meaningful to a prospective sponsor, so a supplemental pure gross return would be a good recommendation in order to make this more palatable for the sponsors.

9) The second Application (p. 14) discusses the fee between the manager and wrap sponsor and the fee between the sponsor and the end user client. In many cases, wrap sponsors do not provide investment managers with the fee that is between the sponsor and the end user. Requiring the investment manager to include disclosure of this fee is problematic without there being a way to require the sponsor to disclose this fee to the investment manager. We recommend that in such cases, provision be made for the investment manager to present performance net of the all fees, with specific disclosure of only the fees they charge and a general disclosure that wrap sponsor fees are available upon request from each wrap sponsor.

