



BADGLEY,
PHELPS AND
BELL
INVESTMENT COUNSEL

August 10, 2004

CFA Institute
Professional Standards & Advocacy Department
Reference: "Gold" GIPS® Standards
P.O. Box 3668
Charlottesville, Virginia 22903

Dear Members of the Investment Performance Council,

We appreciate this opportunity to offer our thoughts on the proposed Gold GIPS and we thank you for the work you have invested in drafting this proposal. We will be happy to answer any questions and provide additional information on the following comments. We hope our comments prove useful in your efforts to finalize the Gold GIPS.

General Comments

1. Do you support AIMR's effort to revise and expand the GIPS standards?

Absolutely – we strongly support the mission of the standards and believe that periodic review and revision are the keys to keeping the standards relevant and robust.

2. Do you agree with the evolution process for the GIPS standards as outlined above?

We do agree with the evolution of the GIPS, though we harbor some concerns that practices, systems, and markets around the globe remain divergent enough at this time that a single global standard (with no regional variances) may not yet be possible. In addressing needs for some markets, the present draft of the Gold GIPS presents great challenges for other markets. Our specific comments below should help clarify this opinion.

3. Is the language of the standards straightforward and comprehensible? If not, how can it be improved?

Generally speaking, the language used in the standards is clear. Where we believe clarification is necessary we have indicated as much in our comments.

4. What modifications, if any, should be made to this proposal?

Modification suggestions are included with our comments.

5. Do you agree with the numbering and format of the proposed revised GIPS standards?

The general organization and numbering system utilized are logical and useful.

6. Should AIMR consider any other methods for meeting the objectives of evolving the GIPS standards?

All suggestions we have to make at this time are included below.

Specific Comments

1. Is the new requirement that mandates firms to provide a compliant presentation to all prospective clients too onerous a burden for firms claiming compliance with the GIPS standards?

While we appreciate the desire to prevent managers from selectively claiming compliance, we believe a more pressing concern is the potential for managers to use their claims of compliance and their composite presentations inappropriately. To the greatest extent possible, performance presentations should be relevant to the prospect’s investment needs and objectives. We do not want the standards to encourage managers to present irrelevant performance simply to meet a requirement. This could lead to an inappropriate generalizing of a manager’s abilities, implying that the manager has equal facility in managing all types of investments.

An additional concern we have with this new requirement is that it is not realistic under a host of common circumstances. In the US marketplace, it is very common for a manager to have no direct contact with prospective clients. Wrap, or Separately Managed Accounts (SMA), and other types of third-party-sponsored programs are intentionally designed to keep the manager from directly meeting the individual investor. Clearly, then, the manager has no control over whether or not a compliant presentation is made.

Given the complex and diverse nature of private wealth management, another common scenario is clients whose needs fall outside a manager’s predominant management style. In addition to traditional investment management services, many firms also provide investment counseling for clients with unique investment circumstances and preferences. Often these clients hire an investment counselor for advice on the existing assets they own, with no intention of allowing the manager to transition the portfolio to the manager’s typical style. The accounts bear no resemblance to the manager’s other client portfolios, are non-discretionary, and will never be included in a composite. In these cases, the manager has no appropriate composite to show the prospect, and the use of any of the manager’s existing composites could be misleading, or at the very least confusing.

Finally, as we discuss below, we support the new recommendation that firms should not market a composite to a prospective client with assets less than the composite’s minimum asset criterion for inclusion. If a prospect is known to fall below the asset minimum for all potentially relevant composites maintained by the manager, the new requirement places the manager in a double bind. He or she would be obligated to show performance but would have no allowable performance to show. Smaller prospects are another common component of the private client side of the business. Often, managers accept smaller accounts as an accommodation where a broader client relationship exists. For example, a manager might maintain small portfolios for the adult children of an existing client whose portfolio well exceeds the manager’s minimums.

Given the above, we recommend that requirement FC.A.3 be reworded as follows (here and below, suggested changes are italicized and underlined for easy identification):

FC.A.3 The firm *should attempt to* provide a compliant presentation to all prospective clients. *In doing so, firms should take care to present composite performance relevant to the prospective client’s investment needs and objectives.* (As long as a prospective client has received a compliant

presentation *for a particular investment product* within the previous 12 months, the firm can present the prospect with interim performance information *for that product.*)

2. Is the new requirement that mandates firms to provide a list and description of composites to any prospective client that makes such a request too onerous a burden for firms claiming compliance with the GIPS standards?

No, this requirement is perfectly appropriate and well within reason.

3. Do you agree with the new recommendation that states the firm should not market a composite to a prospective client with assets less than the composite’s minimum asset level?

Yes, we agree with this new recommendation. It is consistent with our belief that prospective clients should receive composite presentations relevant to their investment needs and objectives. At the same time, we must acknowledge the reality of marketing. It is not always possible to know exactly how much capital a prospective client has to invest prior to presenting performance, particularly in a setting where a manager is presenting information to a group of prospects simultaneously (including advertisements). This is why we strongly agree that this language is best left as a recommendation, rather than a requirement. We suggest that the last sentence of 4.A.5 be moved to the recommendation section of the “Presentation and Reporting” portion of the standards (5.B).

4. Do you agree with the new requirement that mandates firms to be prepared to provide a compliant presentation for any composite on the firm’s list of composites to a prospective client that makes such a request?

Yes, this requirement is reasonable. Firms should already be maintaining presentations for all composites. The standards have always been careful not to distinguish between marketed and non-marketed composites.

5. Do you agree with the new requirement that requires firms to calculate composite performance by asset-weighting the member portfolio returns at least monthly (beginning 2005)?

While this requirement presents no challenge for our firm, we understand that some firms are still calculating composite results on a quarterly basis. In all likelihood, market demands will cause these managers to update their calculation methods to a monthly basis in due time. We suggest making this requirement a recommendation in this version of the Gold GIPS, allowing managers time to adapt their practices, and also suggest that the subject be revisited during the next review and revision cycle for Gold GIPS.

6. Do you agree that the effective date should be moved from 2005 to 2010 for the requirement that stipulates a carve-out return be managed separately with its own cash balance?

We are very pleased that the IPC has recognized the great importance of this issue by moving the effective date from 2005 to 2010. We know that some of our fellow commentators believe this deadline extension “weakened” the standards; however, our opinion is exactly the opposite. We believe the IPC, by keeping an open ear to all marketplaces and practices, has indeed strengthened the GIPS as a working, broadly applicable, truly global standard. In fact, we strenuously encourage the

IPC to drop altogether the requirement that carve-outs be managed with their own cash balances and to permanently allow the use of properly defined carve-outs and cash allocation.

We have commented extensively on the legitimate use of carve-outs and cash allocation in the past, and we offer a summary of our position here. Please contact us with any questions on this important subject.

As we understand it, the primary objection to carve-outs is the potential for their inadvertent misuse. While we certainly agree that managers should properly apply the standards, we do not understand why this single provision of the standards warrants special concern. Any misapplication of the standards undermines the integrity of the resulting performance presentation and negates the manager’s claim of compliance. We find no basis for the opinion that the misuse of carve-outs constitutes a particularly egregious breach of the standards. Further, the “Guidance Statement on the Treatment of Carve-Outs” provided thorough clarification on the proper definition and application of carve-outs, such that carve-outs should now be clearly understood by all managers claiming compliance with the standards.

For managers whose client base is largely composed of private clients with multi-asset-class (balanced) portfolios, carve-outs offer a host of valuable advantages. Briefly, they enable managers to group all like-managed assets into a smaller number of larger, more widely-representative composites that include a higher percentage of the firm’s total assets-under-management than would be included if the carve-outs were not used. Because changes in portfolio-level asset weightings do not typically affect the individual asset class segments’ eligibility for inclusion in composites, carve-outs also lend greater stability to composite membership. In sum, the use of carve-outs strengthens the composites of managers with large private wealth practices, providing prospective clients with more meaningful information upon which to evaluate the managers’ past performance.

Because of these advantages, private wealth managers have long used properly defined carve-outs and cash allocation. Indeed, it is our understanding that the use of carve-outs is widespread in Japan and Canada, in addition to the US. In all the time carve-outs have been in use and for all the firms who have employed them, pre-defined and consistently applied cash allocation has never been shown to result in materially inaccurate or misleading performance results.

On the contrary, cash allocation offers the most practical solution for handling cash for carve-outs, particularly in comparison to the options offered in the carve-out guidance statement, which are unfortunately cost-prohibitive and impractical in many respects. For example, even if a manager is able to account for cash in multiple sub-balances or buckets, custodians only recognize one cash balance per account (or possibly two, if principal and income cash are tracked separately – a practice that further complicates the question at hand). The resulting reconciliation of multiple-balances-to-one would be a labor-intensive manual process, eliminating the use and efficiency of auto-reconciliation systems.

The amount of additional back-office work resulting from the elimination of cash allocation – whether firms opted to implement a cash allocation alternative or chose to eliminate the use of carve-outs in their composites – is staggering and translates into tremendous costs for firms facing this proposition, including the addition of personnel. For some firms these costs would be so burdensome, the cost of compliance so prohibitive, they would end up being priced out of compliance.

Our other primary concern with the offered cash allocation alternatives is the highly questionable practice of altering the structure and manipulating the accounting of current client portfolios for marketing purposes (i.e. to suit the manager’s composite needs). Suggested practices of this dubious nature provide a far greater threat to the integrity of the standards than the unintended misapplication of one provision or another by a limited number of firms – something that can never be entirely eradicated. In fact, by advocating that firms change their accounting practices for current client portfolios solely for the purpose of calculating composite returns, the credibility of the standards may very well be undermined in the eyes of government and other regulators. Given these serious concerns and the long track record of legitimate cash allocation use, we do not see how the elimination of cash allocation can be justified.

Our specific recommendations for adapting the carve-out related provisions are as follows:

3.A.7 – Eliminate the last sentence which alters this provision beginning in 2010.

“Carve-out segments excluding cash must not be used to represent a discretionary portfolio and, as such, must not be included in composite returns. When a single asset-class is carved out of a multiple asset portfolio and the returns are presented as part of a single asset composite, cash must be allocated to the carve-out returns. ~~Beginning 1 January 2010, carve-out returns must not be included in single asset class composite returns unless the carve out is actually managed separately with its own cash balanced.~~”

3.B.3 – Eliminate this recommendation altogether.

4.A.15 – Eliminate the introductory clause in the first sentence so the disclosure requirement stands indefinitely.

~~“For periods prior to 1 January 2010, when a single asset class is carved out of a multiple asset portfolio and the returns are presented as part of a single asset composite, the firm must disclose the policy used to allocate cash to the carve-out returns.”~~

5.A.6 – Our specific comments on this carve-out related provision are detailed below under our response to question 8.

7. Is it reasonable for the GIPS standards to require firms beginning 2010 to value portfolios on the date of any external cash flow?

We strongly oppose this provision for two reasons. First, we assert this will not provide any material improvement in the accuracy of portfolio returns beyond what is already achieved by recalculation for significant cash flows. Through the years, we have conducted this exercise on a number of occasions, calculating performance on a daily basis for an equity portfolio. In every case, the resulting performance was nearly identical to the performance run monthly with recalculations for any significant cash flows (greater than 10% of the portfolio value). Imagine how miniscule the impact would be for bonds, an asset class with far more limited price fluctuations.

Second, implementation of this provision would essentially require all securities to be priced daily – a very costly proposition, particularly for certain types of fixed income securities. With no material gain in the accuracy of performance returns, we cannot see any justification for imposing this dramatic expenditure increase on managers, some of whom may well find daily pricing cost-prohibitive.

We strongly encourage the IPC to drop requirement 1.A.3 entirely.

8. Should the GIPS standards require firms to retroactively disclose the following when carve-outs segments are used?
 - a. a list of the underlying composites from which the carve-out was drawn, and
 - b. the percentage of the composite that is composed of carve-outs.

We agree that firms who utilize carve-outs should be prepared to disclose this data on a historical basis for annual periods; however, we are very sensitive to the ever-increasing volume of required disclosures. Of course, disclosure is of paramount importance in achieving the full goal of the standards, but the reality is that prospects rarely read the disclosures. The increasing length of the disclosures only further discourages prospects from delving in for a careful read. In this case, we believe disclosing this information for the most recent period enables prospects to better understand what is meant by the term “carve-outs.” At the same time, we believe this same data for every annual period does not add value – particularly in the case of 5.A.6 (a), which is likely to be the same for every time period – and only contributes to the imposing effect of the disclosures.

Given the above, we recommend 5.A.6 be altered as indicated:

5.A.6 If a composite is formed using single asset carve-outs from multiple asset class composites the presentation must include the following:

- (a) a list of the underlying composites from which the carve-out was drawn, and
- (b) the percentage of the composite that is composed of carve-outs.

As of 1 January 2006, ~~the firms must also include a statement making this same~~ disclose this information for each annual period (retroactively and going forward) *available by request*.

Additional Comments

In addition to our answers to the specific questions asked in the “Invitation to Comment,” we offer the following comments on other provisions in the proposed Gold GIPS.

FC.A.5 – We suggest a slight amendment to the language of this provision in acknowledgement of the complex joint marketing efforts undertaken by some firms where they have no control over the actual presentation materials shown to the prospective clients and may never meet the prospective clients in person (Wrap or SMA programs are one example).

FC.A.5 When the firm jointly markets with other firms, the firm claiming compliance must *make every reasonable effort to* be sure that it is clearly defined and separate relative to any other firms being marketed and that it is clear which firm is claiming compliance.

FC.A. 6 – We strongly disagree with the introduction of non-fee-paying assets into the definition of total firm assets. Non-billable assets were not previously included in the GIPS total-firm-assets definition, and to our knowledge, the inclusion of non-billable assets in a firm’s AUM is against industry standard. We believe it is inappropriate to ask managers to begin to calculate their total firm assets in a different and non-standard manner. Historical consistency is an important part of maintaining data integrity. If this new definition is implemented, firms face a significant disruption in the consistency of their historical data. And of course, it is not advisable for firms to restate total firm asset figures retroactively.

At the same time, we do realize some firms manage sizeable portfolios for non-fee-paying clients and wish to include the portfolios in composites, with proper disclosure. Where this is the case, we believe it makes sense for the firms to include all non-fee-paying assets in their total firm asset figures as well.

Since the exclusion of non-fee-paying assets from composites is the “standard” composite construction approach under GIPS, and since the burden of disclosure falls to those firms who choose to include non-fee-paying portfolios in their composites, we believe the burden of any necessary disclosure regarding the existence of non-fee-paying assets in the firm’s total asset figure should likewise fall to the firms that include these assets. However, we are not convinced any additional disclosure is necessary. The consistent treatment of non-fee-paying assets that we advocate – i.e. excluding them from both composites and AUM figures, or including them in both – is a very logical approach. In reading a composite presentation, prospective clients are highly likely to assume this sort of consistency. As a result, the disclosure requirement for non-fee-paying assets included in composites probably provides enough information for prospects to understand that the firm includes non-fee-paying assets generally in its calculations, including total firm asset figures. Lastly, any disclosure regarding the total firm asset figure is likely to be confusing since this figure is no longer directly disclosed, except voluntarily.

We recommend FC.A.6 be reworded as indicated:

FC.A.6 Total firm assets are equal to the market value of all discretionary and non-discretionary assets under management within the defined firm. *For firms that include non-fee-paying portfolios in their composites*, this includes both fee-paying and non-fee-paying assets.

FC.A.9 – We have one minor modification to suggest for this provision. Remove the word “all” from the sentence. This single word may result in excessive written policies that amount to nothing more than statements of the obvious. While we do not advocate introducing “grey areas” into the standards, we believe managers are capable of discerning which GIPS requirements warrant written policies and which do not. If a manager is in doubt, he or she need only look as far as the “Required Verification Procedures” section of the standards for clear guidance on which written policies are necessary, at a minimum.

1.A.6 – We began using accrual accounting for dividends at the beginning of 2003 and must report the practice is of no positive value. It does not result in any material difference in the performance of portfolios, as the only real effect of the practice is to move the timing of these small cash flows. However, accrual accounting for dividends does create extra work for our back office – in part by causing retroactive changes to cash positions for prior month-ends – and also creates confusion for our clients, since their custodian statements do not match our portfolio appraisals.

Though we have already adopted this provision, we highly recommend that requirement 1.A.6 be dropped from the standards.

1.A.7 and **1.A.8** – In large part these provisions seem to be statements of the obvious, which we would normally suggest removing in the interest of keeping the standards as succinct as possible. However, the 2006 implementation dates and allowance for non-calendar fiscal year reporting suggest there are firms who are not presently using consistent, calendar-based valuation dates or calendar-year reporting schedules. We find this very surprising, particularly for firms claiming compliance with the standards, as these practices seem counter to the intention of the standards. Since one of the primary purposes of the standards is to ensure comparability of investment performance among firms, we would strongly advocate that all firms use a calendar year reporting schedule and calendar-based (monthly and annual) valuation dates.

We recommend the following changes:

1.A.7 For periods beginning 1 January 2006, composites must have consistent beginning and ending annual valuation dates. ~~Unless the composite is reported on a non-calendar fiscal year, the~~ These beginning and ending valuation dates must be at calendar year-end (or on the last business day of the year).

1.A.8 For periods beginning 1 January 2006, the firm must value portfolios as of the calendar month-end (or on the last business day of the month).

2.A.2 – While we strongly advocate that firms use the most accurate calculation methodologies possible, we also recognize the many obstacles and limitations firms face with regard to implementing new calculation methods. (In addition, we recognize that composite definition and membership criteria have far more impact on performance than the calculation method used, assuming it is consistently applied.) As indicated above, our experience with calculating performance on a daily basis has never yielded any material difference in the resulting performance versus returns calculated on a monthly basis with recalculations for large cash flows. Beyond this, requiring a performance calculation that adjusts for daily-weighted cash flows may make it impossible for some firms to continue to be in compliance with the standards. As previously mentioned, daily pricing of securities may prove cost-prohibitive for some firms, and wrap managers who rely on the performance calculations of the program sponsors have no way to control the performance calculations used. Further, this requirement will discourage additional firms from coming into compliance with the standards in the future (post-1 January 2005). Most firms, at least in the US, are not calculating performance to adjust for daily-weighted cash flows, and the task of doing so on a retroactive basis would be onerous indeed.

In light of these concerns and the lack of material impact to performance, we recommend the last two sentences of the requirement be moved to a recommendation status. In addition, we support the inclusion of a return calculation disclosure requirement.

2.A.2 Time-weighted rates of return that adjust for cash flows must be used. Periodic returns must be geometrically linked. ~~Approximated time weighted rates of return that adjust for daily-weighted cash flows must be used for periods beginning 1 January 2005. The firm must use a "true" Time Weighted Rate of Return calculation method for periods beginning 1 January 2010.~~

Suggested addition: 2.B.4 Firms are strongly encouraged to use the most accurate calculation methodology possible. Approximated Time-Weighted Rate of Return calculations that adjust for

significant or daily-weighted cash flows are superior in accuracy to mid-month convention calculations. True Time-Weighted Rate of Return calculations are ideal.

Suggested addition: 4.A.31 Unless a firm is using a true Time-Weighted Rate of Return calculation, the firm must disclose a brief description of the calculation methodology used.

2.A.9 – This requirement, as worded, will not be possible for managers of Wrap or SMA assets to implement for a host of reasons. To begin, it is often difficult or impossible to ascertain the bundled fee being charged to end clients by wrap program sponsors. Commonly, managers have no access to the actual portfolio-level fees charged by the sponsors. Managers might be able to obtain a copy of the sponsor’s standard fee schedule, in which case the manager would be able to determine a reasonably appropriate model fee (though it is important to remember that managers’ wrap-fee composites often include portfolios from multiple programs which would be subject to varied fee schedules). However, managers are never privy to the exact composition of a sponsor’s bundled fee, so it is impossible for managers to determine the actual trading expenses or even the portion of the bundled fee that includes trading expenses. In most cases, managers have no choice but to utilize a model fee.

We must also note that the proposal to reduce gross-of-fee returns by the entire bundled fee is illogical, as the resulting figure would not be “gross-of-fees” in any sense of the term. While it would invariably result in managers understating performance, it would be misleading to show such a return and label it as gross-of-fees. Even with disclosure, such a practice would only cause confusion for prospective clients.

Recognizing that the above described problems do not plague the use of bundled fees in some markets, we recommend the provision be changed as indicated:

- 2.A.9 If the actual direct Trading Expenses cannot be identified and segregated from a Bundled Fee:
- (a) ~~When calculating Gross-Of-Fee returns, returns must be reduced by the entire Bundled Fee, or the portion of the Bundled Fee that includes the direct Trading Expenses. For Gross-of-Fee returns, managers have three options. They must reduce the returns by the portion of the Bundled Fee that includes the direct trading expenses(estimated Trading Expenses are not permitted) or by the entire bundled fee reduced by the actual Investment Management Fee, or they may choose to show the pure Gross-of-Fee return as supplemental to Net-of-Fee returns.~~
 - (b) When calculating Net-Of-Fees returns, returns must be reduced by the entire Bundled Fee, or the portion of the Bundled Fee that includes the direct Trading Expenses and the Investment Management Fee. Estimated Trading Expenses and Investment Management Fees are not permitted. Where the exact Bundled Fee is not known, managers must reduce returns by a model fee equal to the highest known bundled fee charged among all the portfolios included in the composite being shown.

As indicated in our comments on 4.A.20, we believe any model fee used to reduce the returns should be disclosed.

2.A.11 – We offer a slight revision on this provision in order to allow firms to maintain either firm-wide or composite-specific policies with regard to performance adjustments for external cash flows.

2.A.11 Performance adjustments for external cash flows must be treated in a consistent manner with the firm’s documented policies, either firm-wide or composite-specific policy.

3.A.5 – We agree with and greatly appreciate the expansion of this provision to acknowledge that a composite redefinition might necessitate the movement of portfolios from one composite to another.

4.A.10 – We would appreciate any clarification the IPC can offer on this provision. Specifically, we are curious about the term “managed against a benchmark” and wonder if this is directed to passive managers or “indexers.” For active managers who simply provide a benchmark as a measure of the broad market, this requirement would be unreasonably onerous.

4.A.17 – Prior guidance on this matter, though not finalized, stipulated that the dollar value of non-wrap portfolios be disclosed, rather than the percentage of the composite assets that are bundled fee portfolios. We ask the IPC to consider keeping the requirement consistent with prior guidance as follows:

~~4.A.17 If a composite contains portfolios with Bundled Fees, the firm must disclose for each annual period shown the percentage of composite assets that are Bundled Fee portfolios. When a firm includes portfolios as a part of a wrap fee composite that do not meet the wrap fee definition, the firm must disclose for each year presented the dollar amount of the non-wrap fee portfolios represented.~~

4.A.18 – This requirement is simply not feasible for managers of Wrap or SMA assets. As described above, managers are not privy to the exact fee arrangements between the wrap program sponsor and the end clients. Managers have no way of knowing how the bundled fee is structured or what is included. Further, this information is not something wrap program sponsors have any interest in or incentive to disclose to managers. We also find this requirement redundant, given the addition to the standards of requirement 4.A.20, a more broadly applicable provision. The wording of 4.A.20 should allow managers of wrap assets to provide a non-specific disclosure indicating that the bundled fee includes charges for services provided by the wrap program sponsor that go beyond the investment management fee and direct trading expenses. Again, wrap asset managers cannot be any more specific than this. We recommend the IPC eliminate requirement 4.A.18 entirely.

4.A.19 and **4.A.20** – In both of these provisions we suggest replacing “included” with the word “deducted” for greater clarity. In addition, we believe it is important for managers who utilize a model fee for the calculation of net-of-fee returns to disclose that fee.

We recommend the following:

4.A. 19 When presenting Gross-Of-Fee returns, the firm must disclose if any other fees are deducted ~~included~~ in addition to the direct Trading Expenses.

4.A. 20 When presenting Net-Of-Fee returns, the firm must disclose if any other fees are deducted ~~included~~ in addition to the Investment Management Fee and direct Trading Expenses. Firms that utilize a model fee for the calculation of Net-Of-Fee returns must disclose that a model fee is used, how the model fee was selected, and the amount of the fee.

4.A.21 – As mentioned above, we are seriously concerned about the escalating volume of required disclosures. More is not always better, and in the case of disclosure, excessive length serves only to put off would-be readers. Nevertheless, if this requirement provided important information we would heartily support its inclusion. However, we do not see the value in adding this text. If a prospective client is inclined to read the disclosures, the prospect clearly has enough interest in the details of calculation to ask

any questions he or she might have – and we cannot imagine a manager anywhere who would refuse to answer the questions of an interested prospective client. Given this, we recommend that requirement 4.A.21 be eliminated entirely.

4.A.24 – We believe this is a strong and logical addition to the standards, as it is important to make clear to prospects the nature of the investment mandate being presented. We firmly support the inclusion of this new provision.

4.A.28 – While we appreciate the “full disclosure” intent of this provision, we do not view discontinued composites as being of any importance to prospective clients who might request a list of the firm’s composites. Further, the inclusion of discontinued composites on the list is a likely source of confusion for prospects who ask for composite presentations only to find none exists because the composite is no longer maintained. We think a firm’s list of composites is far more valuable if it reflects only those composites which are currently maintained. We recommend that 4.A.28 be eliminated from the standards.

4.A.30 – We have never seen the positive value of this particular disclosure. In fact, it only causes confusion since a composite’s creation date is very often years after the start date of the performance track record. What is important for prospects to know, in terms of reading a performance presentation, is the effective dates of compliance, which are already included in the disclosures. While this has long been a part of the standards, we recommend that the requirement be dropped.

5.B.5 – We would like to encourage the IPC to consider adding a recommendation that appears in guidance provided in the interpretations database. In an answer posted September 19, 2001, it was recommended that managers who change a benchmark should continue to present the old benchmark. Our specific recommendation is as follows:

Suggested addition: 5.B.5 If the firm changes the benchmark that is used for a given composite in the performance presentation, the firm is encouraged to continue to present the old benchmark.

Verification & Performance Examination

While we believe strongly in the great value of verification, we oppose making verification mandatory for several reasons. To begin, verification is very expensive. The standards are intended to level the playing field for all firms but mandatory verification would make compliance with the standards cost-prohibitive for some managers. Unfortunately, this might be particularly true for managers whose client base is largely private. Since individual prospective clients are not as likely as institutional prospects (and their consultants) to have heard of the GIPS or AIMR-PPS[®] standards, managers faced with the prospect of paying for verification may determine compliance is not worth the expense, as the lack of compliance will not harm them significantly in their marketing efforts. If verification is left as a recommendation, private wealth managers are left with the option of maintaining compliance with the standards as a means of ensuring the integrity of their performance returns. This can only benefit private clients.

Next, mandatory verification would increase the demand for verifiers. Unfortunately, there are not enough qualified verification professionals available to meet this demand (which throws open the door for non-qualified practitioners).

Lastly, there continues to be great misunderstanding as to the meaning of verification, particularly among consultants. Mandatory verification would only further solidify this confusion, allowing consultants and others to persist in their belief that verification provides assurance as to the integrity of specific composite returns.

Given the above concerns, we believe the most broadly beneficial approach to verification is to maintain it as a recommendation.

Finally, we recommend the inclusion of the performance examination guidelines in the Gold GIPS, though not as a requirement or even a recommendation. We understand that the focus of the CFA Institute has been on raising awareness and acceptance of verification, with some effort to deemphasize performance examinations. However, some markets have come to expect this level of independent auditing and the guidance is critical to making sure the work is done consistently.

Special Note

We believe it is important to note a special circumstance that has greatly hindered the ability of our colleagues in the US to provide comment letters on Gold GIPS. US firms are presently extremely busy working to comply with rigorous new SEC mandates, many of which were released within days of the Gold GIPS draft. US firms must have comprehensive new compliance programs in place by October 5th of this year, and compliance professionals at most firms are working greatly extended hours to be ready by this deadline. As a result, these professionals have not been left any time to focus on the Gold GIPS draft. This is especially true for small and mid-sized firms with minimal staff resources. Unfortunately, these are the same firms likely to be most adversely impacted by some of the proposals contained in this draft of the Gold GIPS, a perfect example being the proposed 2010 elimination of cash allocation for carve-outs. We are not suggesting that all would-be commentators would necessarily agree with our pro-cash-allocation position; however, we have spoken with numerous firms who utilize carve-outs and zealously support the continued acceptance of cash allocation but who have not been able to comment on the matter. It is important to understand, generally, that the absence of US comment letters is not necessarily a tacit endorsement of everything contained in the current draft of the Gold GIPS, nor is it a sign of indifference. Again, the tremendous demands being placed on compliance professionals by the new SEC requirements are largely responsible for the dearth of US comment letters.

In conclusion, we would like to thank you once again for your work in drafting the Gold GIPS. We will be happy to answer any questions or to provide additional information on the topics covered above.

Sincerely,

/s/ Rebecca S. Spooner

Rebecca S. Spooner
(rebeccas@badgley.com)