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23 July 2004

### **Invitation to comment – Revising the GIPS Standards (“Gold GIPS”)**

We would like to thank the CFA Institute for this opportunity to provide comments on the proposed content of the next version of GIPS and to commend you and the IPC for the continuing good work that you are doing in the development of this important standard.

The following comments have been produced in discussions across a number of KPMG offices, primarily in Europe and have also drawn from discussions with a number of our clients. However, we recognise that there are some local market differences which cannot be fully reflected in a single document and accept that some offices may also make comments individually.

### **General Comments**

#### **1) Do you support AIMR’s effort to revise and expand the GIPS standards?**

Yes.

One of the key objectives of GIPS is “To promote fair, global competition among investment firms for all markets without creating barriers to entry for new firms.” and this remains essential to the creation of a genuine global market for such services. However, the trend towards a growing number of country specific versions of GIPS is worrying in that it serves to undermine this objective, and in some cases can appear to be creating barriers to free trade.

There is an obvious solution which is to adopt a single version of GIPS in all countries (with translation where required to meet local demand but no country specific changes) and then to deal with local regulatory requirements by way of country specific guidance.



Whilst it is obviously difficult to persuade some countries to give up their traditional requirements there are moves that the IPC could take to facilitate convergence over a reasonable, and clearly defined, timetable:-

- Introduce language to establish a base line as the date after which compliant performance must be presented (subject to the usual qualification where a firm inception date is later). If this date were to be set at 1/1/2000 then, as all data after this date is already required to be presented in compliance, by 1/1/2010 the single most problematic difference would be removed. This is the difference between the GIPS requirement for 5 years history and the AIMR-PPS requirement for 10 years. This suggestion is based upon an assumption that removing the AIMR-PPS specific requirement for 10 years of history would not be acceptable to the US and Canadian Country Sponsor.
- Retain the current wording which requires mandatory verification after 1/1/2010 with a firm commitment to this date to remove the only difference between GIPS and the UK and South African versions.

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

In principle we agree with this process, subject to the following comments.

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

Whilst accepting that it will always be difficult to service all markets in a single language document we are generally happy with the language used by the standards. We have provided some specific suggestions where further clarification could be useful in some markets.

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

See detailed comments below.

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

Yes.

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

No – subject to detailed comments set out 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?**

Our understanding of this requirement is that its objective is to prevent firms from picking and choosing when they do, or do not, claim compliance with GIPS. This is a good objective, but the approach which has been taken could force firms into a difficult position of having to decide which composite to choose when asked to pitch for a mandate for which they do not currently have a good matching product available.

A suggested alternative wording which would achieve the desired result is:-

“A firm must provide an appropriate compliant composite presentation, where available, to all prospective clients...”

**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?**

Yes. This requirement is a logical extension of the existing requirements and should not be too onerous given that firms are already required to have such a list.

**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?**

This is a reasonable recommendation. However, as there may be exceptional circumstances when it firms may wish to provide composite statistics to a prospective client with assets below the minimum asset level set, such as where services are being offered as part of a wider relationships, a restriction on such use would be unreasonable and so this should not be made a requirement.

**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. Firms should have the ability to provide performance statistics for any composite, within a reasonable timescale, and so this requirement is reasonable.

**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?**

Yes. Fund performance has long been required to be based on a minimum of monthly valuations, so the additional effort required to calculate composites to this frequency should be minimal and the benefits in terms of increased accuracy and longer inclusion of new/lost accounts are significant. It is noted that the deadline for introduction of this requirement has been changed to 2006.

**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?**

The main justification for using carve-outs is to present a manager’s expertise in a specialist area which has previously only been managed as part of a wider mandate. Creating a requirement to only present such returns where cash has been allocated on an ex-ante basis reduces the flexibility of managers to present their expertise as market demands evolve. It would be better to provide enhanced guidance on what should, and should not, be considered appropriate to carve-out and then leave managers to work within the guidance.

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

Yes. Such a treatment can serve to significantly enhance the accuracy of returns and the timescales set out for firms to meet this requirement are reasonable notice to allow them to develop the capability.

**8) Should the GIPS standards require firms to retroactively disclose the following when carve-out 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.

Yes. For future periods. Both sets of information are useful to provide a perspective to allow recipients of reports to understand how the numbers have been calculated. However, the principle has been established that GIPS provisions will not be imposed retrospectively and it would be good to maintain that principle in this case.

### **Additional comments:-**

There are also some other elements of the changes proposed in Gold GIPS which we would like to pass comment on:-

### **Universal Applicability**

GIPS quite rightly aspires to being a standard that can be adopted by any asset manager. However, this should not be allowed to introduce significant delays to the implementation of valuable enhancements or increments, or to introduce compromises into the standards. Whilst changes should be reasonable and should allow time for most firms to implement them, there may well come a point where a few firms (or markets) are left behind in the best interests of the vast majority.

### **New Provisions**

#### **As of 2006, calendar month-end valuation required**

Whilst the move away from non-month end dates for period end valuations is a big step in the right direction the wording is still sufficiently vague to allow significant variations in valuation points. As comparability of returns is one of the key objectives of GIPS a move to requiring close of business valuation at month end (or indeed any intra-month valuation points that may be required) would be significantly beneficial. Such a move would also avoid inconsistency between valuations used for fund and composite returns and those used in the preparation of the vast majority of benchmarks.

It may be that many firms would have difficulty in achieving consistent valuation points by the end of 2005, but consideration should be given to introducing a further enhancement to require close of business (in the investment market) effective 2010.

#### **As of 2010, verification by a third party will be mandatory**

This is a move which has been supported by the vast majority of country sponsors and it will serve to add credibility to claims of compliance.

As the standards, and their interpretation, become more complex the need for external review becomes more important to ensure consistency of approach across firms and across markets.

#### **Must have written policies and procedures used for compliance**

This is a logical extension of the existing requirement to have policies and procedures in place and in effect reflects best practice within the existing GIPS compliant community.

**Must abide by guidance and interpretations, including the GIPS handbook.**

Again, this is necessary to ensure that all firms are adopting the best practice approach to GIPS compliance.

**Must disclose that the calculation methods and valuation sources are available upon request.**

This is sensible, but to be consistent with other provisions there should be an additional requirement to provide this information when it is requested.

**Must disclose any discretionary use of a Sub-advisor**

This is a sensible requirement, although as currently worded it is quite vague. Is it considered adequate for firms to make general statements such as “Sub advisors have been used for portions of the assets in this composite at times during the periods being presented” or should the disclosure be more detailed and specific?

**Must disclose a description of the investment objectives / style / strategy of the composite**

It is noted that a description may be more abbreviated than the full definition, but nowhere is a firm required to disclose the full definition of a composite. This would be useful information for recipients and may be a more appropriate disclosure within the composite report.

**Section 1.A.1.**

The requirement to capture and maintain “All” data and information has led to a situation where firms are retaining huge quantities of paper records which provide duplicate confirmation. The intention of the standards would be met by changing the first word of this section from “All” to “Sufficient” which would also allow managers to be more selective about which records need to be retained.

**Section 1.A.8**

There are many markets where it is not common practice to produce valuations on local holidays, even when other investment markets are open for trading. We would suggest that suitable wording is required to deal with this scenario when the local holiday occurs on the last day of a month.

### **Section 1.B.2**

It would appear that the term “accrued management fees” is not clear in all markets. We would suggest that a suitable definition could be added to the glossary.

### **Section 3.A.7**

We have previously received a Q&A which relates to the acceptability of asset only carve-outs being used where managers genuinely have no permission to hold cash as a strategic asset within specialist portfolios or sub-portfolios. If this response still applies, then it would be good to have the situation reflected within the standard text. Otherwise the removal of this option should be made very clear through revised guidance.

### **Section 4.A.4**

In addition to requiring that firms disclose if they employ an alternative method, they should be required to identify or describe the method.

### **Section 4.A.5**

Some of this text relates to requirements rather than disclosures. We suggest that the text beginning “and must not...” to the end of the section would be better associated with section 2.A.7.

### **Section 4.A.10**

Whilst this disclosure is useful for recipients to help them to understand the drivers of differential returns, it has very little value at only one point in time. Whilst it would be unreasonable to ask firms to calculate this information retrospectively it would be reasonable to ask that information which has been calculated should be retained within the report for future periods. We suggest that the wording of this section could be changed to:-

“For composites managed against a benchmark, the firm must disclose the percentage of the composite invested in countries, regions or sectors not included in the benchmark for 31<sup>st</sup> December 2005 and all subsequent reported period ends.”

Alternatively, the disclosure requirement may be better satisfied by asking firms to provide a descriptive disclosure of their policy with respect to limits on investments

outside of the benchmark, including changes over time, rather than single point in time numerical information

#### **Section 4.A.19 and Section 4.A.20**

Use of the word “included” in relation to fees is ambiguous. We would suggest that it could be better replaced by “deducted”

#### **Section 4.A.23**

There is a lot of room for interpretation as to what is (and is not) a material event. It would be good if the IPC could at some point in the future provide guidance on this particular disclosure requirement.

#### **Section 5.A.1**

We suggest that for clarity the first line should read “The following items must be reported for each composite being presented:”

#### **Section 5.A.4 (b)**

For the reasons discussed in 1.A.1 above, we suggest that this section should read “the firm has sufficient supporting performance records to calculate the performance.....”

Section III (Verification) section B.1.D.

There is redundant wording at the end of the opening paragraph which could more efficiently read: “At minimum, verifiers must determine the firm’s following policies and procedures.”

#### **Section 5.B.1 (d)**

For consistency with other sections we suggest that this should refer to “annual volatility” rather than simply volatility.

#### **Section III (Verification)**

Depending upon responses and decisions made about some other elements of the standards, sections of this guidance may require revision.



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We would like to re-affirm our commitment to supporting the IPC and the CFA Institute with the development of these standards. If there is any way in which you feel that we could contribute further then please do contact me.

Yours sincerely

Brian Chapman  
*Senior Manager*