

Association for Investment Management and Research
Professional Standards and Advocacy
Reference: "Gold" GIPS Standards
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Oslo, 06.07.2004

**INVITATION TO COMMENT:
Revising the GIPS Standards ("Gold" GIPS)**

Dear Sir or Madame,

We would like to thank you for the opportunity to make comments on the revising of the GIPS Standards ("Gold" GIPS).

The Norwegian Society of Financial Analysts (Norske Finansanalytikeres Forening, hereafter named NFF), is the sponsor for GIPS® in Norway. Our comments are given as country sponsor in Norway.

Our comments to IPC are as follows:

GENERAL COMMENTS:

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

❖ NFF:

- Yes we do. It is important that the GIPS Standards are revised in order to remain effective as a global standard. The "grace" period from 2000 to 2005 with no alteration of the standards has been helpful to firms recently claiming compliance and to firms in the process of implementation. The revision of the Standards at a future date has been known since the launch of the GIPS Standards in 1999.

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

❖ NFF:

- Yes we do.

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

❖ NFF:

- Yes, except for the situations listed below.
 - It should be stated in the beginning of the glossary whether the purpose of the glossary is to explain and define words in the GIPS Standards (the document) only, or also include words in the Guidance Statements. The glossary is not comprehensive enough if the intention is to include the wording of the Guidance Statements.
 - Some words in the revised standards should be included in the glossary (example: Incentive allocations 6.B.7)
 - The wording in the standards should be the same in all sections (example: Trading expenses 2.A.6, Transaction expenses 7.A.4; Net-of-fees, Net-Of-Fees, e.g. 6.B.7; SI-IRR (Since Inception Rate of Internal Return) 7.A.2, since inception rate of internal return 6.B.4, 6.B.6, 6.B.7)

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

❖ NFF:

- In comparison with the situation in Norway we suggest the following modifications to the standards.
 - 1.A.6, The requirement to use accrual accounting for dividends from 1. January 2005 should be retained and not postponed to 1. January 2010.
 - 3.A.7, The requirement to manage the asset separately with own cash balance from 1. January 2005 should be retained and not postponed to 1. January 2010. Please see our answer to question 6 in the specific comments section.

These requirements have been known since the launch of the GIPS Standards. As far as we know these requirements have never been an obstacle for GIPS implementation in Norway.

In order to be regarded as a reliable standard for performance presentation we believe that such “technical requirements” should not be postponed.

- We believe the text on page 3 “Deleted Provisions” **is misleading**:

“Definition of Firm **is no longer permitted** as an entity registered with the appropriate national authority overseeing the entity’s investment activities”.

We believe there is no violation between FC.A.2

“The firm must be defined as an investment firm, subsidiary, or division held out to clients or potential clients as a Distinct Business Entity”

and defining the firm as an entity registered with the appropriate national authority, as long as the investment firm equals the entity registered at the national authority.

The Executive Summary should emphasise in which situations defining the firm as an entity registered with the appropriate national authority **is not sufficient as a firm definition**.

Most Norwegian firm definitions are defined according to such registrations at the national authority overseeing the entity’s investment activities.

- The new requirement in 1.A.8 means that the firm must value their portfolios at **calendar month end**. This requirement is different from valuation at the last trading **date** in the month. When calendar month end occurs during a weekend this requirement can be an obstacle for GIPS implementations.

We believe firms with such a requirement will have to recalculate both accrued interest and discount all fixed income securities and derivatives to calendar month. It is not sufficient to do this at (or to) the last trade date in the month.

All pooled vehicles will with the new requirement (calendar month end) have to calculate NAV (net-asset values) during weekends, in situations where calendar month end occurs during weekend, even though no transactions take place between shareholders at this date (month end = weekend).

The requirement to value the portfolios during weekends (month end = weekend) can increase the costs of becoming / or being GIPS compliant.

- The phrase “true” Time-Weighted Rate of Return, 2.A.2 should be avoided unless the phrase is explained in the glossary. The wording “True” is too ambiguous.

- We do not support a **remove** of the recommendation to present “equal-weighted means and median returns for each composite”, 5.B.1 (c). Instead the recommendation might be upgraded to a requirement.

Equality between equal-weighted return and asset-weighted return indicates that a firm is able to produce the same performance to small and large accounts. We regard this as relevant information to a prospective client.

Equal-weighted **dispersion numbers** are meaningful for the prospective client. Asset-weighted dispersion numbers can sometimes be materially distorted by large accounts in the composite.

Removing the equal-weighted return as a recommendation forces the firm to treat this figure as **supplemental information** only in accordance with the Guidance Statement on the use of supplemental information for the treatment of such information.

- We believe assets below a **minimum level** and portfolios **under termination and implementation** should be included in the definition of firm assets in FC.A.6.
- The footnote reference 1, 4.A.7 appears to be an error, and should be replaced by 3.
- We believe it can be difficult to disclose the percentage of the composites invested in **sectors** not included in the benchmark, 4.A.10. Such a requirement requires that all information about the benchmark is available to the firm retroactively, and that the firms apply the same sector classification as the benchmark.
The requirement in the current GIPS is to disclose the percentage invested in **regions** outside the benchmark.
- The explaining text for the previous recommendations 4B.1-4.B.5 seems to include wrong references.
- The Standards inform on the first page of the Verification part (page 28) that the next GIPS revision cycle is planned for an effective date of 1 January 2010. We believe that the plans to revise the Standards as of 2010 ought to be described in the Introduction part of the Standards (IMPLEMENTING A GLOBAL STANDARD).

5. IPC: Do you agree with the numbering and format of the proposed revised GIPS Standards?

❖ NFF:

- Yes we do.

We would welcome a **sample presentation** for real estate composites. Sample presentations are given for both a balanced composite and a private equity composite.

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

❖ NFF:

- No suggestions.

SPECIFIC COMMENTS:

1. IPC: Is the 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?

❖ NFF:

- We believe the wording “prospective client” should be properly defined in the standards. It is not relevant to provide a compliant presentation in situations where investment performance is not the main topic.

We believe the requirement should be limited to those situations where the prospective client investment objectives have been properly defined, either by the client himself or by the firm itself.

2. IPC: 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?

❖ NFF:

- We believe this requirement is almost present in the current GIPS Standards, 4.A.3. Consequently, it should not be regarded as too onerous a burden.

3. IPC: 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?

❖ NFF:

- Requirement 4.A.5 includes the phrase "should". The phrase "should" is reserved for the recommendations and should be avoided in the requirements. We therefore suggest to move the sentence "The firm should not market a composite to a prospective client with assets less than the composite's minimum asset level." to a new recommendation in section 4.B.

4. IPC: 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?

❖ NFF:

- We believe the requirement should be limited to those situations where the prospective client investment objectives have been properly defined.

We also believe the requirement should be limited to situations where the prospective clients' assets are above the minimum asset level.

5. IPC: 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)?

❖ NFF:

- Yes we do.

The new requirement in 1.A.8, "...the firm must value portfolios as of **the calendar month end**", necessitates monthly asset-weighting.

6. IPC: 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?

❖ NFF:

- No we do not.

This requirement has been known since the launch of the GIPS Standards. The requirement has never been an obstacle for GIPS implementation in Norway as far as we know.

In order to be regarded as a reliable standard for performance presentation we believe that such “technical requirement” should not be postponed.

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

❖ NFF:

➤ Yes we do.

We agree with the rewording from “time” to “date” in Gold GIPS. The current GIPS require valuation at the “time” of any external cash flow. We believe the date is sufficient in order to calculate a reliable performance number.

8. IPC: 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.

❖ NFF:

- As mentioned in General Comments question 4 we believe the requirements to manage the asset separately with own cash balance should not be postponed to 2010.
- Question 8 a): We believe information from which composites the carve – outs are drawn is of minor interest to the prospective client
- Question 8 b): We believe information about the percentage of the composite that is composed of carve – outs **is** relevant information to prospective clients.

The percentage indicates if the composite is an individual product at the asset manger, or if it only is derived from other products (composites).

ADDITIONAL COMMENTS TO GOLD GIPS:

➤ Upgrading of the part covering **Verification:**

We agree that verification should become mandatory, as this promotes credibility and reliability of the claim of compliance and of composite performance reports. This ensures the fulfillment of the aim of the standards, which is to ensure accurate and consistent investment reporting data, as well as comparability both within and between markets. The act of making verification mandatory has also been signaled in the present version of the GIPS standards.

We do not have an opinion of the timing of making verification mandatory.

We register that **no change** has been made to the actual verification procedures. Based on the changes to the GIPS standards that have been proposed in Gold GIPS we encourage some changes or rather additions to the verification procedures, as follows:

- Add a requirement to verify that the firm has established written policies and procedures used for GIPS compliance, including a description of the calculation methods and valuation sources/methods used for all relevant asset classes.
- Verification Procedures 2.B.vii says that the verifier must be satisfied that “the firm’s list of composites is complete.” We recommend adding to this that one must ensure that reasonable descriptions of the composites are included.
- Provisions related to Real Estate and Private Equity. We would welcome the addition of specific procedures or comments relating to these asset classes, as we believe both they and the related provisions are distinct to such an extent that they require special procedures or treatment in the verification section. This could for instance be a requirement to check valuation of such assets (and how), as well as the calculation of IRR and other types of returns.

➤ Appendix A – Sample presentations:

Balanced portfolio: The sample presentation for the balanced portfolio is not complete / updated

- The Fee schedule is **not** disclosed, 4.A.16
- The Firm Assets are **included**. According to 4.A.2 this requirement is removed in Gold GIPS.

Private Equity: The sample presentation for the balanced portfolio is not complete.

- The Fee schedule is not disclosed, 4.A.16. The Fee schedule should be **appropriate** to the presentation. The difference between the Net-of-fees returns and Gross-of-fees returns, in 7.A.20, is not necessarily appropriate to the client as a fee schedule.

➤ Real Estate:

- It should be clarified whether the GIPS Standards focus on the presentation and calculation of returns from **real estate** assets, from **portfolio** of real estate assets, or from **composites** of real estate portfolios. This is not obvious in the proposal. Page 22:

“Following are the provisions that apply to the calculation and presentation of **real estate assets**”

Such a clarification will also make clear whether or not the value of **gearing** is supposed to be included in the performance calculation and presentation.

- **Gearing** in real estate composites at year-end should be disclosed.
- The treatment of **taxes** from realisation of real estate should be included in the GIPS Standards. In ordinary portfolios of liquid assets this tax is normally paid by the client, not by the asset manager. We believe taxes from realisation of real estate assets will be paid by the asset manager (real estate investment company) and not by the client. We believe the GIPS Standards should address the treatment of taxes in real estate portfolios.
- The definitions in the glossary should include examples other than those that apply to liquid assets:

Example Trading Expenses: “The costs of buying or selling a security”. This definition should be upgraded to include real estates.

- The distinction between administrative fees and investment management fees is not obvious for real estate. This should be clarified in the glossary or in the final Guidance Statement for Fees or Real Estate.
 - The expenses to the external professionally designated / governmentally certified / licensed commercial property valuer should be clearly defined as either part of an administrative fee or part of an investment management fee.

➤ Private Equity:

- The treatment of **taxes** from realisation of unlisted securities should be included in the GIPS Standards. In ordinary portfolios of liquid assets this tax is normally paid by the client, not by the asset manager. We believe taxes from realisation of unlisted securities occur to be paid by the asset manager (private equity investment company) and not by the client. We believe the GIPS Standards should address the treatment of taxes in private equity portfolios (closed-end portfolios).
- The distinction between administrative fees and investment management fees may not be obvious for private equity portfolios.
 - The consulting fees, legal fees, accounting fees, etc. should be clearly defined as either part of an administrative fee or part of a normal investment management fee.
- The heading on page 24 should be Private Equity **and Venture Capital** and not only Private Equity (refer to the top of page 13; “Private Equity and Venture Capital”).

The Outline section on page 6 should equally be changed to “Private Equity and Venture Capital”.

- The paragraph 7.A.1 should include a reference to the document that includes the GIPS Private Equity Valuation Principles.
- 7.A.15 appears to be covered by 4.A.24. GIPS paragraph 4.A.24 requires firm to disclose the objective, style and / or the strategy of the composite.

Best regards,
The Norwegian Society of Financial Analysts (NFF)

Guri Angell-Hansen
Deputy Secretary General

All inquiries or comments related to GIPS should be sent to the chairman of the “NFF Committee on Performance Measurement” Mr. Jorn Kleven, AFA, CEFA,
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