

Professional Standards and Advocacy  
Association for Investment Management and Research  
P.O. Box 3668  
Charlottesville, Virginia 22903  
Re: GIPS Guidance Statement

December 31, 2001

Dear Sir/Madam:

**Proposed Guidance Statement on Composite Definition**

PricewaterhouseCoopers wishes to thank the Association for Investment Management and Research (AIMR) for this opportunity to comment on the Proposed Guidance Statement on Composite Definition. Our comments are provided in the attached appendix. Please note these comments are not meant to detract from the many favourable aspects of GIPS™. The issue of defining composites is of paramount importance and we welcome the Guidance proposed by the Interpretations Subcommittee of the Investment Performance Council.

## **Appendix: PwC Comments on the Proposed Guidance Statement on Composite Definition**

### **1. Response to specific questions (“Comments Requested”)**

#### ***Do you agree with the principles established in the Guidance Statement?***

We welcome and generally support the recommendations made by the IPC, as presented in the Proposed Guidance Statement on Composite Definition. It is our opinion that any guidance should not, in any way, lead to a situation where accounts move between inclusion and exclusion in a particular composite with out documented client imposed guidelines.

#### ***Do you agree with the treatment of portfolios that fall below a minimum asset level?***

Generally, we agree with the proposed guidance except for the following:

*Statement* “If a firm establishes a minimum, it must document its policies regarding how portfolios will be treated if they fall below the minimum and must apply these policies consistently”

We suggest incorporating an example of a firm’s policy with respect to minimum asset level; such example should address portfolios that fall below the established minimum asset level due to client withdrawals and market movements. We recommend the example establish a criterion for including/excluding accounts that fall below the minimum for more than a defined number of investment periods (i.e. 3 consecutive months or 2 consecutive quarters), such number should be defined at the firm level and be applied consistently across all composites.

*Statement* “If the portfolio falls below the minimum due to market movements, the firm must leave the portfolio in the original composite until there is a documented change in client guidelines or acknowledgment from the client that the firm considers the portfolio too small to implement the composite strategy”.

As it is the firm’s responsibility to determine composite assignment as well as minimum asset level for an account to be included in a composite (not the client’s), the criterion described above eliminates the firm’s judgement regarding composite assignment. The firm’s policy as to when a portfolio should be removed from the composite must be based on a consistently applied policy determined by the firm at the firm level, for example, a portfolio has been below the composite minimum for 3 consecutive months or 2 consecutive quarters.

#### ***Should firms be allowed to exclude a portion of a portfolio as non-discretionary?***

We do not believe that firms should be allowed to exclude a portion of a portfolio as non-discretionary as such a task would be cumbersome and non-practical.

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*How should portfolios with different measurement periods be treated?*

We agree with the proposed guidance.

*Do you agree with the proposed Implementation Date of April 1, 2002?*

We would suggest the guidance be effective no earlier than January 1, 2003 this will allow firms, which are currently in the process of implementing the re-drafted Standards, enough time to reconsider the way they are going to define their composites.

We also recommend clarifying whether the implementation date is for performance measurement periods after such date or for performance presentations presented after such date.

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### 2. Specific Comments on the Proposed Guidance Statement

Section	Comment
<b>Discretion (Page 3)</b>	<p>The Guidance should make it clear that an account may be considered non-discretionary due to documented client imposed restrictions and legal regulations.</p> <p>The Discretion section states “Firms should review all of their portfolios (both discretionary and non-discretionary) on a regular basis to determine if any portfolios should be re-classified.” The guidance should define a “regular basis” and provide an example of what firms’ policy with respect to reviewing its portfolios should be.</p> <p>The Discretion section states “Firms are only permitted to move portfolios into and out of composites due to changes in discretion resulting from documented changes in client guidelines or in the case of the re-definition of a composite.” This statement requires clarification as to whether documentation needs to be sent to clients contemporaneously with oral conversations or whether an internal memo (contemporaneous or not) is adequate if documentation is not otherwise received from the client as to the change requested. Clarification should also be provided on the “re-definition of a composite” and what the required communications should be when a firm determines that a strategy will no longer be offered.</p>
<b>Minimum Asset Level (Page 4)</b>	<p>The Minimum Asset Level section states “Portfolios below the minimum must represent a small percentage of the composite assets and thus, should not have a material impact on the asset weighted composite return.” It is possible that for the very reason the minimum asset level is established is because accounts that fall below the minimum size requirement could have vastly different returns that, could impact the overall return. As the subject of assessing materiality comes up in a number of applications of the standards, we recommend that the subject of materiality be addressed in a separate section of the Standards.</p>
<b>Composite Definition (Page 5)</b>	<p>The guidance needs clarification as to when a composite may be re-defined and how a firm may determine that the result of the re-definition does not cause the creation of a new composite and loss of linking the historical track record. This section also needs clarification of the disclosures necessary when a composite is re-defined; we recommend providing an example of such disclosures.</p>

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<p><b>Composite Definition Criteria</b> (Page 6)</p>	<p>The Composite Definition Criteria section states “Comparability of similar strategies or products is a fundamental objective of the Standards and only works if firms define strategies with similar terminology and substance.” We recommend adding, “focusing on the uniqueness of the firms strategy in the market place” to the end of the sentence.</p> <p>In the sub-section “<b>Benchmarks</b>”, clarity is required to prohibit composite definition as the weighting of several benchmarks. Once a strategy goes beyond a published benchmark, the definition of the strategy is no longer based solely on the benchmark. If a firm has the ability to allocate between the benchmarks this in and of itself is part of the strategy and maybe unique to the firm.</p> <p>In the sub-section “<b>Risk/Return Characteristics</b>”, please provide clarification of “return objectives may be grouped together into different composites”. The example provided is not clear as to whether the “Japanese Equity” and “US Equity” strategies are to be included in the same composite or in different composites.</p>
<p><b>Constraints and Guidelines</b> (Page 7)</p>	<p>We recommend providing separate bullet point clarification where composites are managed using different currencies.</p> <p>In the sub-section “<b>Type of Client</b>”, we recommend an example be provided (i.e. wrap client vs. non-wrap client).</p> <p>In the sub-section “<b>Size of Portfolios</b>”, we recommend that clarification be made to further describe that composites may not be defined purely on size of portfolios. It is imperative portfolios that are managed in the same style or strategy are included in the same composite regardless of size. Further clarification may also be necessary in the section “<b>Minimum Asset Level</b>”, to fully address this matter.</p> <p>In the sub-section “<b>Portfolio Types</b>”, the guidance states “Pooled funds, including mutual funds and unit trusts, may be treated as separate composites or combined with other portfolios into one or more composites of the same strategy, style or objective.” A clear distinction should be provided between the areas “<b>Portfolio Types</b>” and “<b>Type of Client</b>”. Theses topics overlap in many ways and as such we recommend the guidance be made consistent and state that “Pooled funds, including mutual funds and unit trusts, <i>should</i> be treated as separate composites or combined with other portfolios into one or more composites of the same strategy, style or objective.”</p>

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<p><b>Additional Considerations (Page 8)</b></p>	<p>In the sub-section “<b>Investment Guidelines – Multi Asset Portfolios</b>”, the statement “Only multi-asset portfolios for which the firm has discretion over the asset mix are to be included in multi-asset composites” needs clarification. Further guidance is needed as to when the difference in the range of the composite and the range of the client’s portfolio is too large and therefore should be excluded from the multi-asset composite.</p> <p>In the sub-section “<b>Firms with Multiple offices, branches, or investment groups</b>”, further clarification is necessary to describe whether this relates to composites with in the same defined firm or different defined firms. We also recommend an example be provided to further clarify this guidance.</p>
<p><b>Additional PwC Comments</b></p>	<p>The guidance statement should address the impact of internal reorganizations on composite construction and disclosures (i.e. mergers of like composites, creation of new divisions – defined as separate firms for GIPS purposes and movement of assets between GIPS compliant firms which are both part of the same legal structure). This has continuously been the subject of much ambiguity and should be addressed in detail to consider historical track records, minimum asset level of surviving composite, notification to clients and necessary disclosures.</p> <p>The guidance should provide clarification of what firms should do with historical track records of composites that may be impacted due to the adoption of this guidance.</p>