

October 24, 2002

Association for Investment Management and Research  
Reference: AIMR-PPS standards-Wrap Fees  
P.O. Box 3668  
Charlottesville, VA 22903

Fellow Charterholders:

The purpose of this letter is to comment upon the proposed AIMR-PPS Guidance standards for Separately Managed Accounts. This investment choice has grown significantly in recent years. At my firm, Kayne Anderson Rudnick, it represents the largest single distribution channel. As the partner who is responsible for operations, compliance, and analytics, I may have a broader, and perhaps deeper, perspective than other CFA Charterholders.

The firm and I continue to support AIMR, and we believe that the PPS standards represent an important contribution to the investment management community. While this new guidance for the Separately Managed Accounts (“SMA”) product represents a good start, there is room for improvement. It seems to this observer that the new guidance misses some of the subtleties between the “traditional” institutional account and the SMA.<sup>1</sup> For example, the execution, clearing, and portfolio accounting is often done solely on the sponsor’s system. This limits the investment manager’s access to the complete records. The advent of Multi-Discipline Accounts where more than one investment manager trades in a single sponsor’s account not only complicates the accounting and record-keeping but also raises Graham-Leach-Bliley privacy concerns. Some investment managers have adopted the questionably accurate and non-economic practice of shadowing.<sup>2</sup> This is clearly not a panacea, and only adds overhead cost to an investment choice which is already under extreme pricing pressure.

Further, the sponsor, and not the investment manager, sets the overall, bundled fee which the investor pays to the sponsor. The investment manager (who receives but a pittance of that fee) has no control over the total fee. Gross returns are the only returns which the investment manager can influence, and hence the manager should be allowed to report them. Each sponsor, and often each employee of the sponsor, is able to set a unique fee for an investor. This causes a multiplicity of fees. Reporting net of fees just compounds these disparate decisions into a meaningless relative figure. Gross of fees returns are clear of this noise and provide a fair cross-manager comparison.

These two points show that a wider discourse on SMA-PPS standards would be useful. I suggest AIMR engage in direct discussions with SMA industry specialists such as the Money Management Institute.

Best regards,

RCW/eab  
cc:Stephanie Reeves

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<sup>1</sup> It is not unusual for industry initiatives to not fully reflect the nuances of the SMA (or “Wrap”) business. Anyone familiar with the recent SIA T+1 model notices immediately that the SMA Account has been ignored in the overly complicated VMU messaging and cross messaging protocols.

<sup>2</sup> Most managers who choose shadowing did so during the halcyon days of the recent technology bubble. Many of them now privately rue its extravagant costs.