

The Security Analysts Association of Japan

5 F, Tokyo Stock Exchange Building, 2-1 Nihonbashi-Kabutocho, Chuo-ku, Tokyo 103-0026, Japan
Tel: 81-3-3666-1515 Fax: 81-3-3666-5845

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CFA Institute
Professional Standards and Advocacy Department
P.O. Box 3668
Charlottesville, Virginia 22903
USA

**Re: INVITATION TO COMMENTS:
Revising the GIPS Standards (“Gold” GIPS)**

Dear Sir/Madam,

Thank you for affording us the opportunity to comment on revising the GIPS standards.

The Security Analysts Association of Japan (SAAJ) is the sponsor of the SAAJ Investment Performance Standards (SAAJ-IPS[®]), the Japanese Version of GIPS. SAAJ has translated the proposed revisions to the GIPS standards into Japanese for comments from the investment industry in Japan and received comments from investment management firms, trust banks, and related industry associations such as the Japan Securities Advisers Association and Trust Companies Association of Japan.

Following are our comments that are based on discussions within the SAAJ-IPS Committee considering comments received from the investment industry in Japan.

General Comments

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

- We support IPC’s efforts to improve the GIPS standards to secure complete and fair presentation of investment performance as five years have passed since the GIPS standards were first established in 1999.

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

- We support the IPC’s strategy that it should review provisions of the GIPS standards about every five years taking into consideration the environment within each country/region and also avoiding any undue disruption to the investment industry.

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

- Since the native languages of a lot of countries that have adopted the GIPS standards as TGs/CVGs are not English, the language of the Standards should be clear and easy to understand as much as possible so as not to lead to any misinterpretations. From this viewpoint, we have some comments/proposals as below.

- GIPS Glossary (Appendix C):

The “GIPS Glossary” (Appendix C) is very helpful in understanding key words used in the GIPS provisions. However, as no explanation is given about the role of the Glossary, we suggest that the purpose of the Glossary and the relation with the GIPS provisions should be clearly explained in the introduction to Section II.

We understand that specific terms the first letters of which are capitalized in the GIPS provisions are defined in the Glossary. However, some such terms do not appear in the Glossary but are defined/explained in the relevant Guidance Statements. All of the terms using capital letters should be covered in the Glossary.

In addition, whether the definitions in the Glossary are consistent with the definitions and usage of terms in the GIPS provisions should be crosschecked. For instance, the definitions of “Gross-of-Fees Return” and “Net-of-Fees Return” are not necessarily appropriate to real estate and private equity investments although capital letters are used, and such should be noted in relevant places in the Glossary.

- Guidance Statements:

Since interpretations by the users of the Standards may be broad, in order to maintain consistency, the clarification of interpretations is indispensable. In response to the revision and expansion of the GIPS standards, Guidance Statements and Q&As should be expanded accordingly.

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

Definition of the Firm and Total Firm Assets

- Under “Deleted Provisions” in the Summary of Proposed Provisions to the GIPS standards, the following is mentioned:

Definition of Firm is no longer permitted as:

- an entity registered with the appropriate national regulatory authority overseeing the entity’s investment management activities;

However, it is possible that there is such a registered entity that is appropriate as a Distinct Business Entity as provided under FC.A.2. We therefore think it inappropriate to eliminate “registered entity” from the definition of the firm.

Accordingly, it should be clearly mentioned in the relevant Glossary (“Distinct Business Entity”) or Guidance Statement that if such a registered entity meets the criteria of “Distinct Business Entity” then such firm can be defined as a registered entity.

- We oppose the deletion of the required disclosure of total firm assets (4.A.2) because:

- Total firm assets depend on how the firm is defined as provided under 4.A.1 (the definition of “firm” used to determine the firm’s total assets and firmwide compliance) and therefore should be clearly disclosed together with definition of the firm. (Total firm assets are also necessary to verify appropriateness of the definition of the firm.)
- To be able to estimate total firm assets from the required disclosure of the percentage of the firm’s total assets represented by the composite (5.A.1(c)) does not justify the deletion.

When FC.A.6 is provided as the required provision, it should read “Total Firm Assets must be defined as ...” not “Total firm assets are equal to ...”. Also, FC.A.6 and the relevant Glossary (“Total Firm Assets”) are partly inconsistent and should therefore be unified.

Section II.6 (Real Estate)

- Effective Dates:

As the postponement of the effective date of the real estate provisions to 1 January 2006 is proposed by IPC, the effective date of quarterly valuation (6.A.1), 1 January 2008, should also be moved to 1 January 2009 and the deadline for the completion of the first external valuation to 31 December 2008 (from 31 December 2007).

In this regard, there is comment that as real estate funds are only settled on an annual basis it is very difficult to value them quarterly and that if business practice is not changed by the target effective date how funds can be valued quarterly will come into question. We think there may be similar issues in other countries/regions and some guidance will be necessary for quarterly valuation.

- Sample Presentations (Appendix A):

Sample presentation for real estate should also be provided in Appendix A.

- Provisions and Interpretations:

Since there are various vehicles for real estate investments, in particular for indirect investments (through real estate funds, SPC, etc.), the current provisions may cause confusion with respect to what presentation/disclosure should be made by firms that may or may not have control over management and performance reporting of such investment.

In Japan, real estate investments have been rapidly expanded. In order to have the GIPS real estate provisions accepted in the market, provisions of Section II.6 should continuously be reviewed including consistency with provisions of Section II.7 (private equity/venture capital) as discussed below.

In addition, as the current Guidance Statement for real estate is insufficient vis-à-vis that for private equity, it is indispensable to provide more guidance in implementing the provisions.

Relationship between Sections II.1-5 and Sections II.6/II.7

- Since the relationship between Sections II.1-5 (main provisions) and sections II.6 (Real Estate)/II.7 (Private Equity) is not clearly explained, misinterpretations may be caused in applying relevant provisions to those alternative assets.

Accordingly, explanations made in some parts (Section I.31 that is incomplete, the introduction to Section II, the first part of Section II.6, and the first part of Section II.7) should be reviewed and modified in the interest of consistency and also so as to be more easily understood. In particular, the purpose of establishing Sections II.6 and II.7 and the relationship with the main provisions (Sections II.1-5) should be more clearly given in the introduction to Section II.

- The introduction to Section II (under “Real Estate”) mentions that the rules apply regardless of the level of control the firm has over management of the investment. The meaning is vague (it could mean the provisions apply regardless of direct and indirect investments) and may cause confusion. Thus, this part should be more clearly written and further explanation given in the

Guidance Statement.

- One of the salient features of real estate and private equity investments is the use of leverage or gearing. Although 4.A.7 (disclosure of the presence, use, and extent of leverage or derivatives) is a common required provision, such should also be provided as disclosure requirement under Sections II.6 and II.7.

Consistency between Section II.6 and Section II.7

- Although types of risks are quite different between real estate and private equity, there are common elements in terms of disclosure/presentation as private investments: they are long-term oriented, present valuation difficulties, and are evaluated using IRR until the exit of the investment. While Sections II.6 and II.7 were prepared by different IPC subcommittees, two sections should be compared from the viewpoint of consistency: e.g.
 - While only IRR is required in private equity provisions, TWR is required and IRR recommended in real estate ones.
 - While provisions for investment advisors are given in private equity provisions, no such provisions appear in real estate ones.

Introduction to Section II

In addition to modifications as mentioned above, the following points should also be modified:

- The explanation about “Fundamentals of Compliance” is inconsistent with actual provisions in that section and should be modified accordingly. For instance, although the definition of discretion is not included in that section, such an explanation is given.
- The last paragraph “The standards for each section are divided between requirements ... and recommended guidelines. Firms ...” should be incorporated in the first part of the introduction (i.e. before “Fundamentals of Compliance”) because it is related to the whole GIPS provisions.

Appendix A (Sample Presentations)

- The first sample presentation is exactly the same as what appears in the 1999 version of GIPS and does not reflect revised/added requirements and should therefore be re-prepared including all of the required elements of the revised GIPS standards.

Appendix B (GIPS Advertising Guidelines)

- There are no explanations about GIPS Advertising Guidelines in the main body of the GIPS standards. We therefore suggest that explanation should be given in Section I or the introduction to Section II.

With respect to other modifications, please see the remaining part.

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

Structure of the Fundamentals of Compliance Section

- The Fundamentals of Compliance section should be restructured. For instance, provisions not directly related to the definition of the firm (FC.A.3-5, etc.) are included in “Definition of the Firm”. Accordingly, we propose a structure such as:

- Definition of the Firm (comprising definition of the firm, total firm assets, changes in a firm's organization, etc.): FC.A.2, FC.A.6, FC.A.7, FC.A.8, and FC.B.1
- Firm's Fundamental Responsibilities (comprising firmwide compliance, performance presentation to prospective clients, marketing, document policies/procedures, and understanding of all provisions and interpretations): FC.A.1, FC.A.3, FC.A.5, FC.A.9, and FC.A.10. (As for FC.A.4, please see comments under specific comment 2.)

Section I.15 (Compliance Check) could also be incorporated here.

- Claim of Compliance: FC.A.12 - 14

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

- As in Section I.24, in order to drive success of the GIPS standards in the real meaning, it is essential that an appropriate reliable organization (investment professional organization, etc.) in each country/region adopts them as its own, and has responsibility to translate them into its local language, promote recognition of the GIPS standards, and has a close relation with the IPC by submitting comments on proposals and representing local interests.

In this context, we strongly desire that IPC undertakes some measures to further enhance the relation with local sponsors.

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?

- Since what are "prospective clients" varies by firm and the provision (FC.A.3) may be interpreted as that firms are required to present compliant performance to all prospective clients regardless of the existence of such a request from prospective clients, some compliant firms seem to feel the requirement a burden.

As it is difficult to represent the meaning only by the provision, it is indispensable to provide a relevant guidance statement or Q&A to fully explain the purpose and how the provision should be interpreted. To this end, we think it important to clarify the points as follows:

- Claiming compliance means that the compliant firm must disclose the availability of a complete list and description of all of the firm's composites and full compliant presentation of any composite upon request.
- Those to which firms must present compliant performance are those to which firms claim compliance. There are generally two methods to claim compliance: a) to claim compliance on a one-on-one basis (i.e. existing clients or those who, firms identify, have high potential to become clients) and b) to claim compliance by advertisements.

In the case of a), it is ethical to claim compliance to any of those whom firms identify as "prospective clients" and firms must present compliant performance upon request.

In the case of b), there is a possibility that firms may not identify beforehand who will see an advertisement (in particular an advertisement in newspapers, magazines, and

media) and that firms must present compliant performance upon request from any person who sees an advertisement.

- What are “prospective clients” should be determined by each firm and cannot be defined uniformly.

There is another issue of how compliance with the required provision of FC.A.3 can be verified.

- Question on FC.A.3:

When a prospective client has received a verified compliant presentation within the previous 12 months, can the firm present unverified interim performance? Is it allowed if such fact is disclosed?

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?

- Because it is still unclear to what extent “description” should abbreviate the full definition, it should be further clarified. We suggest that sample list and descriptions of composites should be indicated as an appendix.
- It seems that FC.A.4 and 4.A.3 overlap. If there is no substantial difference, FC.A.4 is not necessary.

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?

- We agree with the new recommendation since marketing a composite to a prospective client with assets less than the composite’s minimum asset level is meaningless.

However, we do not think it appropriate to include the recommendation in the required provision 4.A.5 (disclosure). As the recommendation is related to an issue of suitability of investments and marketing, it can be included as a separate recommendation under the “Fundamentals of Compliance” section.

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?

- We agree with the new requirement because it supports the basic principle that firms must take all steps necessary to ensure that they have satisfied all of the GIPS requirements before claiming compliance.

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)?

- We agree with the new requirement as the SAAJ-IPS standards have already required firms to value portfolios at least monthly since its establishment of 1999 and it has already been a common practice to calculate composite performance at least monthly in Japan.

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?

- Considering the fact that portfolio management systems have not yet evolved to implement the requirement, the postponement of the effective date from 2005 to 2010 seems unavoidable.
- With respect to development of systems, we can't afford to be optimistic about the realization in 2010. Even if systems become available, whether achieving each segment's cash accounted for separately at the custodian is uncertain. On the other hand, the firms' needs of carve-outs would potentially exist at any time.

Accordingly, if technical issues will not be resolved by 2010, the IPC should reconsider whether cash allocation methods should continue to be allowed or not after 2010.

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

- In order to implement the requirement the following issues have to be resolved and the IPC should continue to carefully discuss the matter.
 - Whether fair market values can be obtained for various asset classes at any markets and at any time. If not, the requirement to value portfolios on the date of any external cash flow may undermine the accuracy of performance results. The realization depends on the ability of system/data vendors and custodians to offer such information.
 - Cost performance: at the cost of meeting the requirement, to what extent firms can improve the accuracy of performance results in comparison with the use of alternative methods such as Modified Dietz Method.

Unless the above issues are resolved, we think it very difficult to make the provision required in 2010. We therefore suggest that the latter part of 1.A.3 should read:

“For periods beginning 1 January 2001 portfolios must be valued at least monthly. It is anticipated that the firm will be required to value portfolios on the date of any external cash flow but no earlier than 2010”.

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.**

- 5.A.6 (b):

As explained in the Guidance Statement for Carve-outs, due to the ambiguity of current 5.A.6 (b) different disclosure practices have been established and therefore revision is proposed to provide more clarity so that disclosure practice is unified.

Since some firms (that have conducted different disclosure from the revised one in accordance with the 1999 version of GIPS) may feel retroactive disclosure a burden, it should not be mandatory but firms should be able to decide whether they retroactively disclose the item on their discretion.

Accordingly, retroactive disclosure should be recommended not required as mentioned in the Guidance Statement. Not to mislead clients, we also suggest that, when the firm decides not to retroactively disclose the item, the firm must clearly indicate the fact (i.e. different disclosure is made for the specific periods in accordance with the provision of the 1999 version).

- 5.A.6 (a):

We think it enough to disclose the item at the end of the most recent period only.

Other Specific Comments

9. Requirement to disclose Fee Schedule (4.A.16)

- 4.A.16 provides “The firm must disclose the Fee Schedule appropriate to the presentation.” Also, the relevant Glossary defines “Fee Schedule” as “a list of the firm’s current Investment Management Fees or Bundled Fees for a particular presentation” and also mentions “This schedule ... should be appropriate to the particular prospective client.”

Interpretations on these parts may be different by firm with respect to what should actually be disclosed. As mentioned in the Guidance for Fees Provisions, fees are sometimes negotiable and therefore we understand that “Fee Schedule appropriate to the presentation” means “Standard Fee Schedule” as a basis for negotiation. In order to avoid confusion, Q&A should be given to clarify that “Standard Fee Schedule” is appropriate to be disclosed under 4.A.16 and that it is also acceptable for verification.

10. Requirement to disclose the use of a sub-advisors (4.A.22)

- Q&A should be given to clarify to what extent disclosure should be made.

11. Requirement to disclose any events which help a prospective client interpret the performance record (4.A.23)

- Although there are some examples of such events, items to be disclosed and to what extent disclosure should be made are still unclear.

In order to upgrade the provision from a recommendation to a requirement, appropriate guidance is necessary for firms to identify any such significant event and about how disclosure should be made. Unless such guidance is given, it seems to be difficult to make it mandatory and verification is also difficult.

12. Requirement to disclose a description of the investment objectives, style, and/or strategy of the composite (4.A.23)

- To help firms to understand to what extent disclosure should be made, a description of the investment objectives, style, and/or strategy of the composite should be included in Sample Presentation (Appendix A).

13. First part of Section II.6 (Real Estate)

- The first part of Section II.6 states as follows:

“If a portfolio includes a mix of Private Equity Real Estate and other investments that are not equity real estate, then these requirements and recommendations only apply to the Private Equity Real Estate portion of the portfolio and the GIPS carve-out provisions (Sec II.3.A.7.) must also be applied.”

Whether the firm carve-outs the Private Equity Real Estate portion of the portfolio or not depends on the firm’s discretion and therefore the last part of the paragraph should read:

“... Then these requirements and recommendations only apply to the Private Equity Real Estate portion. When the firm carve-outs the Private Equity Real Estate portion of the portfolio, the GIPS carve-out provisions (Sec.II.3.A.7.) must also be applied.”

Sincerely yours,

The Security Analysts Association of Japan