

Global Investment Performance Standards (GIPS®) Guidance Statement on Benchmarks for Firms

Adopting Release

The Exposure Draft of the Global Investment Performance Standards (GIPS®) Guidance Statement on Benchmarks (Exposure Draft) was available for public comment from 30 October 2017 through 29 January 2018. We delayed finalizing and issuing this Guidance Statement until the 2020 edition of the GIPS standards was released because the 2020 edition of the GIPS standards could, and did, affect the final Guidance Statement.

We received comment letters from 27 groups and individuals, and 25 of these gave permission to have their [comment letters](#) posted online. We evaluated and considered every comment, resulting in a recommendation for several changes to the Guidance Statement. The proposed changes were then reviewed with, and approved by, the GIPS Standards Technical Committee.

The Exposure Draft and public comments received were taken into account when we drafted the 2020 edition of the GIPS standards, as well as the GIPS® Standards Handbook for Firms. Although much of the guidance in the Guidance Statement on Benchmarks for Firms is also included in the GIPS Standards Handbook, we believe this Guidance Statement is necessary for two reasons:

- The benchmark-related guidance appears in different parts of the GIPS Standards Handbook, and it will be helpful for firms to have all of the benchmark-related guidance consolidated in one place.
- Some of the explanatory language in this Guidance Statement is not included in the GIPS Standards Handbook. For example, the GIPS Standards Handbook does not contain all of the Guidance Statement language about the role of benchmarks, benchmark selection criteria, types of benchmarks, and practical considerations.

This Adopting Release includes key topics and describes the rationale for the changes made to the Exposure Draft.

1. Name of the Guidance Statement was changed to reflect that it applies only to firms

The 2010 edition of the GIPS standards focused solely on firms, although it has always been possible for both firms and asset owners to comply with the GIPS standards. Guidance for asset owners was included in the Guidance Statement on the Application of the GIPS Standards to Asset Owners.

The 2020 edition includes three chapters:

- GIPS Standards for Firms,
- GIPS Standards for Asset Owners, and
- GIPS Standards for Verifiers.

Each chapter is tailored to its intended audience.

The name of the Guidance Statement on Benchmarks was changed to the Guidance Statement on Benchmarks for Firms because it includes content that is applicable only to firms. We are creating a separate Guidance Statement on Benchmarks for Asset Owners that will be tailored for asset owners.

2. New concepts reflected in the 2020 edition of the GIPS standards

The Exposure Draft focused primarily on the selection and presentation of benchmarks for composites that use time-weighted returns, which was consistent with the 2010 edition of the GIPS standards. The 2020 edition of the GIPS standards includes new and different requirements that affect benchmarks and benchmark returns, including:

- the presentation of pooled funds in addition to composites,
- more options for presenting money-weighted returns versus time-weighted returns, and
- the use of custom benchmarks.

The Guidance Statement on Benchmarks for Firms was updated to reflect these items.

3. Withholding tax status consistent with the portfolios in the composite

In the Exposure Draft, we proposed that when a composite uses an international index as a benchmark, and both gross-of-withholding-tax and net-of-withholding-tax benchmark options are available, firms must select the benchmark that is most consistent with the withholding tax status of the portfolios in the composite. We received numerous comments stating that it would be difficult for firms to determine which benchmark is appropriate given that the population of portfolios in a composite can change each period. We agree with this concern. This requirement, therefore, was changed to a recommendation.

4. Using an exchange-traded fund (ETF) as a benchmark

The Exposure Draft proposed requiring firms that choose to use an ETF as a benchmark to present the returns of the ETF that are comparable to the presented composite returns (e.g., if composite gross-of-fees returns are presented, then ETF returns must also be gross.) Commenters stated that there is a lack of consensus on what the most comparable returns are, given the variety of fees that can be reflected in composite and ETF returns. The amount of fees charged to ETFs is often much smaller than the amount of fees reflected in composite returns, and determining comparability would be challenging.

Given these concerns, the final Guidance Statement does not require firms to use comparable ETF returns. Instead, when using an ETF as a benchmark, firms are recommended to present composite or pooled fund net returns. Aligning with the GIPS standards principles of fair representation and full disclosure, when a firm uses an ETF as a benchmark, it must disclose a list of the ETF's features as part of the benchmark description. The Exposure Draft also proposed requiring firms to disclose the reason for selecting the ETF as a benchmark rather than using a market index. With the continued increase in the use of ETFs as benchmarks, this disclosure seemed less relevant. The proposed requirement, therefore, is not included in the final Guidance Statement.

5. Disclosure of hedging criteria for hedged benchmarks

The Exposure Draft proposed requiring disclosure of the hedging criteria for the benchmark when a hedged or partially hedged benchmark is used, as well as any material difference in hedging between the composite and the benchmark. The final Guidance Statement was revised as follows:

- Firms are not explicitly required to disclose the hedging criteria for a hedged or partially hedged benchmark as a separate disclosure. Instead, firms are expected to include this information in the disclosure of the benchmark description. A benchmark description is general information regarding the investments, structure, and characteristics of the benchmark, and it must include the key features of the benchmark. Because hedging criteria are a key feature of the benchmark, a separate disclosure requiring this information is not needed.
- Firms are required to disclose the composite description, which includes all key features of the composite's investment mandate, objective, or strategy. As described earlier, firms are also required to disclose information about the investments, structure, and characteristics of the benchmark. The use of hedging would typically be included in both the composite and benchmark descriptions. Given these two disclosures, the requirement to disclose material differences in hedging between the composite and the benchmark is not necessary.

6. Portfolio-weighted custom benchmark component disclosure

A portfolio-weighted custom benchmark is created using the benchmarks of the individual portfolios in the composite. When using a portfolio-weighted custom benchmark, the firm must disclose information about the benchmark, including the components that constitute the benchmark and the weights that each component represents, as of the most recent annual period end.

Some composites, such as those for liability-driven investing strategies, may include portfolios that have highly customized benchmarks, which causes the portfolio-weighted custom benchmark to have a very large number of underlying benchmarks. In these cases, some of the weightings of the component parts may be so small, and the list of benchmarks so long, that listing all of them would make the disclosure difficult to read. Although firms may list each component to meet this requirement, the Guidance Statement allows a different option. Firms may instead disclose the major components and weighting of the customized benchmark and offer to make the undisclosed components available upon request.

7. Custom net benchmarks

The Exposure Draft proposed that when a firm used a custom benchmark that reflects the deduction of fees or trading costs, it would be required to disclose the fee schedule or trading costs used to calculate the benchmark returns. The 2020 edition of the GIPS standards includes new disclosure requirements for when any custom benchmark, including a custom net benchmark, is used. Disclosure requirements for custom net benchmarks were aligned with these requirements. When using a custom net benchmark, firms must clearly label the benchmark to indicate it is a custom benchmark as well as disclose the calculation methodology, which would include the fees or costs used to calculate the benchmark net returns.

8. Income sweeping

The Exposure Draft included guidance addressing how firms should reflect income that is swept out of the portfolio, when clients require income distributions to be paid to them directly. The Exposure Draft stated that firms should generate the income transactions in the portfolio and then balance these transactions using cash withdrawals. We determined that this workaround was not the correct approach in all circumstances, and this topic was deleted from the final Guidance Statement.

9. Price-only return benchmarks

The Exposure Draft proposed that price-only return benchmarks would never be allowed to be included in a compliant presentation. (In the 2020 edition of the GIPS standards, compliant presentations have been renamed GIPS Reports.) Recognizing that price-only benchmark returns may be useful in certain situations, the final Guidance Statement allows a price-only benchmark to be included in a GIPS Report as supplemental information, but only if it is presented in addition to a total return benchmark. If no appropriate total return benchmark exists for the composite or pooled fund, the firm may not present a price-only benchmark in the GIPS Report.

10. Effective date

Given the delay in issuing this Guidance Statement, we have updated the effective date. Because this Guidance Statement contains no new requirements beyond those included in the 2020 edition of the GIPS standards or the GIPS Standards Handbook for Firms, the effective date is 1 April 2021.

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