



July 16, 2017

*Via Electronic Submission (standards@cfainstitute.org)*

Jonathan A. Boersma  
Executive Director  
Global Investment Performance Standards  
CFA Institute  
915 E. High Street  
Charlottesville, VA 22902

**Re: GIPS 20/20 Consultation Paper Seeking Comment on Potential Changes to GIPS**

Dear Mr. Boersma:

The Investment Adviser Association (“IAA”)<sup>1</sup> appreciates this opportunity to comment on the CFA Institute’s (“CFA’s”) *GIPS 20/20 Consultation Paper Seeking Comment on Potential Changes to GIPS* (“**Consultation Paper**”), proposed by the Global Investment Performance Standards (“GIPS”) Executive Committee on May 18, 2017.<sup>2</sup> We commend CFA’s efforts to update and streamline GIPS to ensure they are “as relevant and straightforward as possible,” but are concerned that the broad vision of universal demand and adoption articulated in the Consultation Paper will lead to a burdensome overlay of GIPS compliance on top of and potentially inconsistent with well-developed local laws relating to disclosure of performance information. The potential changes described in the Consultation Paper would significantly modify GIPS and have a substantial impact on investment managers in the United States and other jurisdictions in which the IAA has members.<sup>3</sup> In this letter, we suggest important overarching principles that we believe CFA should consider in rethinking its approach to the development of GIPS 20/20. We also provide specific feedback on the questions in the Consultation Paper.

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<sup>1</sup> The IAA is a not-for-profit association that represents the interests of investment adviser firms registered with the U.S. Securities and Exchange Commission (“SEC”). The IAA’s membership consists of more than 600 firms that collectively manage approximately \$20 trillion for a wide variety of clients that are individual and institutional investors, including pension plans, trusts, investment companies, private funds, endowments, foundations, and corporations. For more information, please visit [www.investmentadviser.org](http://www.investmentadviser.org).

<sup>2</sup> The Consultation Paper is available at [https://www.gipsstandards.org/standards/Documents/Guidance/gips\\_2020\\_consultation\\_paper.pdf](https://www.gipsstandards.org/standards/Documents/Guidance/gips_2020_consultation_paper.pdf).

<sup>3</sup> The IAA, together with the Asset Management Group of the Securities Industry and Financial Markets Association, expressed and expanded upon these same concerns in our comment letter to CFA on its *Exposure Draft of the Guidance Statement on Broadly Distributed Pooled Funds*. That letter is available at <https://higherlogicdownload.s3.amazonaws.com/INVESTMENTADVISER/aa03843e-7981-46b2-aa49-c572f2ddb7e8/UploadedImages/publications/160429cmnt.pdf>.

## Overarching Principles that Should Guide Exposure Draft

As CFA considers its *GIPS 20/20 Exposure Draft* (“**Exposure Draft**”) in the coming months, we urge CFA to be guided by the following principles:

*Costs and Benefits.* Given the magnitude of the potential changes to GIPS, CFA should carefully weigh the costs (to firms and investors) against the potential benefits to investors, especially in jurisdictions with comprehensive regulatory schemes. We commend CFA’s efforts to eliminate burdens on and minimize unnecessary costs for GIPS-compliant firms. In this regard, any revised standards should build in sufficient flexibility to allow for different business models and position firms to be able to respond to developments and innovations in markets, products, investment strategies, and delivery capabilities, such as permitting clients to view performance numbers for their accounts and composites on a website.

*Safe Harbors for Regulated Activity.* CFA should provide safe harbors to investment managers already subject to specific and robust regulation of the calculation and disclosure of performance. Thus, for example, CFA should make clear that products subject to and in compliance with the U.S. Investment Company Act of 1940 (as amended) (“**Investment Company Act**”) or the Undertakings for Collective Investment in Transferable Securities (“**UCITS**”) Directive, all of which are separate entities from their advisers and have their own boards of directors, will be deemed to be in compliance with GIPS.<sup>4</sup> To prevent conflicts with local laws, unnecessary burdens on asset managers, and investor confusion, CFA should provide safe harbors in contexts other than broadly distributed pooled funds as well, for example for regulated investment products in highly-developed disclosure jurisdictions.

*Recommended and Voluntary vs. Required.* To ensure consistency, GIPS 20/20 should also incorporate and apply the principles behind any other relevant guidance or relief provided in the recent Pooled Funds Guidance. For example, CFA should maintain GIPS verification as a recommended item and reclassify certain “required items” as recommended where that would be more appropriate and more in keeping with the voluntary nature of GIPS.

*Flexibility.* It is also critically important that any revised standards permit firms to elect whether on not to claim GIPS compliance for *individual* portions of their business, based on the firm’s determination of relative costs and benefits of claiming GIPS compliance for a particular asset type or investment structure. Enhanced flexibility is not only consistent with the voluntary nature of firms’ compliance with GIPS, but is more likely to facilitate greater adoption of GIPS.

*Simplification.* GIPS should also be simplified wherever possible, and we support CFA’s expressed interest in eliminating unnecessary or duplicative disclosures and requirements.

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<sup>4</sup> The CFA Institute adopted *Guidance for Broadly Distributed Pooled Investment Vehicles* (“**Pooled Funds Guidance**”) on March 13, 2017, which will be effective January 1, 2018, available at [https://www.gipsstandards.org/standards/Documents/Guidance/gs\\_pooled\\_funds.pdf](https://www.gipsstandards.org/standards/Documents/Guidance/gs_pooled_funds.pdf).

*Transition Time.* Finally, CFA should provide ample transition time—at least 18 months from adoption of revised GIPS—for implementation of policies and procedures needed to comply with any new requirements.

With these general principles in mind, we address each of CFA’s questions below.

## **Consultation Paper Questions**

CFA seeks feedback on 13 potential proposed changes to GIPS. We briefly describe each proposed change and the questions asked and then provide our response.

### **1. Structure**

The current GIPS focus primarily on the use of composites. This structure would be reorganized in GIPS 20/20 to reflect situations in which firms are not selling a composite strategy. Instead of a composite-centered approach, there would be three “pillars,” which would be based on: (i) “one to one”—composite performance (for typical institutional separate accounts, similar to current GIPS standards); (ii) “one to many”—fund performance for all pooled funds (limited distribution pooled funds, closed-end funds, fixed-life funds, fixed commitment portfolios); and (iii) “one to none”—for asset owners with no prospective clients (similar to GIPS standards for asset owners).

#### **Question 1: Do you agree with the pillars concept? If so, should there be any other pillars?**

We generally agree with the proposed structural approach. However, we recommend that CFA consider permitting combinations of pillars and the ability to use presentation data for more than one pillar or for a dynamic interchange between pillars. For example, data from GIPS one-to-one presentations could also serve as the building blocks for one-to-none presentations, including fund of funds and ownership reporting presentations for pension plans or sovereign wealth reports. We commend CFA for proposing a more flexible structure than the current “one size fits all” approach, and urge CFA to build in additional flexibility.

### **2. Pooled Funds**

Firms managing any type of pooled fund would be required to present to prospective investors in those funds a pooled fund report that would include only the pooled fund’s information – which would depend on whether the fund is broadly distributed or not and whether it is a closed-end, fixed life, fixed commitment fund where the manager controls the cash flows – and would be presented net of all fees and expenses. Firms could choose to present gross-of-fees returns as well, as permitted by regulatory requirements. Pooled funds would still be required to be included in the appropriate composite according to investment mandate, objective, or strategy if they meet the composite definition, but firms would not be required to create single-fund composites.

**Question 2: Do you agree with the proposed treatment of pooled funds?**

We do not support any new requirements for pooled funds. As to fees, firms should have the flexibility to report as permitted in local national jurisdictions, including reporting both or either net of fees and gross of fees. To require otherwise would impose substantial costs on firms that do business on a global basis. The recent Pooled Funds Guidance reflects a flexible approach by creating some safe harbors for broadly distributed pooled funds. GIPS 20/20 should incorporate safe harbors for all pooled funds, provided that the funds are in compliance with adequate regulatory requirements of local jurisdictions. As discussed in response to Question 8, GIPS 20/20 should also provide latitude as to whether to include funds for which no fee is charged.

**3. Asset-Class Specific Guidance**

The number of asset-class specific guidance would be consolidated and reduced where possible.

**Question 3: Do you agree that asset-class-specific guidance should be consolidated where possible?**

We support consolidation of asset performance guidance where appropriate, and urge CFA to eliminate or minimize redundancy and inconsistency where possible. However, standards should remain sensitive to particular characteristics of different asset classes as well as to investment vehicles that include different asset classes. We note that some investment vehicles may include several types of investment assets, structures, wrap arrangements, real estate, and commodities. Reporting on a cross-portfolio basis could be appropriate even if it involves different asset classes that may need to be valued differently or on different time schedules. What is important is that the composite results be reported consistently and on a regular basis. (See our response to Question 10.) Consolidation of guidance should consider these circumstances and allow for prudent judgments to be made.

**4. Time-Weighted Rates of Return (“TWRRs”) vs. Internal Rates of Return (“IRRs”).**

Under GIPS 20/20, TWRRs would be required for open-end funds and composites with separate accounts. Firms would be permitted to present either IRRs or TWRRs for closed-end, fixed-life, or fixed commitment funds, for which the investment manager controls the cash flows. The Consultation Paper seeks comment on the criteria that should be required to permit a firm to use IRRs.

**Question 4a: Do you agree with the proposal that firms should be allowed to choose whether to present IRRs or TWRRs for any closed-end, fixed life, fixed commitments fund where the firm controls the timing of the cash flows?**

Yes. We agree that firms should be permitted to choose IRRs as described in the Consultation Paper, unless such presentation(s) would be misleading. However, we believe that IRRs should be the default or recommended method for closed-end, fixed-life, or fixed commitment funds.

This position would establish a baseline accepted practice, thereby increasing consistency of reporting across firms, but still give firms the flexibility to deviate from the recommendation where appropriate, consistent with their policies and procedures.

**Question 4b: What criteria should be required for a firm to be allowed to present an IRR versus TWRR?**

As noted above, we believe that IRRs should be the default method for closed-end, fixed-life, and fixed commitment funds. TWRRs would also be acceptable subject to the firm's documented policy for when TWRRs may be the more appropriate option.

**5. Valuation Frequency**

Portfolios would be required to be valued: (i) annually and (ii) whenever performance is calculated and reported to prospective clients or prospective fund investors. The Consultation Paper seeks comment on whether valuing monthly and at the time of all large cash flows is sufficient for calculating TWRRs. It also seeks comment on whether the proposed valuation frequency is appropriate for all portfolios regardless of the underlying investment or asset class for calculating IRRs.

**Question 5a: For calculating TWRRs, do you believe that valuing monthly and at the time of all large cash flow suffices?**

Yes. Valuing monthly and at the time of all large cash flows would be sufficient. Firms should be permitted to value more frequently if they choose. CFA should consider providing guidance on what constitutes a "large" cash flow.

**Question 5b: For calculating IRRs, do you agree with the proposed valuation frequency for all portfolios regardless of the underlying investment or asset class?**

Yes. Annual calculations should be sufficient for composite returns using IRRs. An annual reporting schedule allows firms to formulate policies and procedures appropriate for their organization and business model, the type of investments in accounts, and most importantly, is consistent with their reporting to current clients. Expecting greater valuation frequency would be expensive, unnecessarily burdensome, and perhaps practically impossible for many firms.

**6. Distribution of Presentations**

Firms are currently required to "make every reasonable effort" to provide a composite compliant presentation to prospective clients on an annual basis. No GIPS-compliant information is required to be provided to existing clients. GIPS 20/20 would extend this requirement to pooled fund reports as well. CFA is also considering requiring investment managers to provide, or alternatively, offer to provide a composite compliant presentation or pooled fund report to *existing* clients/pooled fund investors annually as well. The proposal seeks comment on these alternatives.

**Question 6a: Do you agree that firms should be required to provide a pooled fund report to investors in the pooled fund on an annual basis?**

We read this question as asking whether we agree that firms should be required to provide a pooled fund report annually to *existing* pooled fund investors. For the reasons stated below, we strongly disagree.

Firms are generally already required by regulation or contract to make regular reports to existing clients. Such individualized reporting serves a different purpose than a GIPS presentation. A GIPS-compliant presentation is intended to help an investor compare potential asset managers and not to provide information about existing client relationships or improve client servicing. The additional burdens associated with having to provide an annual GIPS report to existing clients would not be justified by any marginal benefits to those existing clients, but would create a significant new burden for firms. Receiving two different types of reports may also prove misleading for existing clients. Moreover, if GIPS were to impose this requirement, it could lead to reduced adoption of GIPS going forward and many firms currently claiming compliance may elect no longer to do so.

**Question 6b: Do you agree that firms should be required to provide a compliant presentation to existing clients in the composite on an annual basis?**

No. See response to Question 6a.

**Question 6c: Do you agree that firms should be required to make an offer to provide a composite compliant presentation or pooled fund report to existing clients or pooled fund investors on an annual basis?**

No. We do not believe it is necessary to require firms to offer to make a presentation or report available to existing clients since doing so may not be significantly less burdensome than requiring the presentation itself. For example, where a fund has no new investment opportunities available, a firm would not need to prepare a presentation or report for prospective investors and so would not have one available to offer to existing clients. If the firm were required to offer a presentation or report annually to existing clients, it would need to prepare one regardless of whether it had prospective investors.

## **7. Total Firm Assets**

GIPS would require that “advisory assets” (such as unified managed accounts (“UMAs”), model portfolios, and advisory-only portfolios) be included in compliant presentations by creating a new category of assets that includes assets managed, advised, and overlaid. Currently, the “advisory assets” and the underlying portfolios in overlay strategies that are not managed by the firm are excluded from firm total assets. The Consultation Paper seeks comment on whether a new category should be created and, if so, which assets should be included. It also asks whether the information should be required or recommended to be included.

**Question 7a: Do you agree with creating a new category of assets as described above?**

Yes, but the new category should be recommended rather than required. It could be presented as additional information.

**Question 7b: Which assets should be included in this new category of assets (e.g., UMAs, models, overlay, and advisory-only portfolios)?**

Whether the adviser to the funds is actually managing the assets and whether the results could be documented would be relevant in determining whether assets should be included in this new category. UMAs, overlays, and advisory-only portfolios would likely meet this test, but, since elements of this category, such as “models,” could take many forms, not all would meet this test.

**Question 7c: Should firms be recommended or required to report this new category of assets as well as total firm assets in compliant presentations?**

A firm’s existing policies and procedures and books and records may constrain the firm’s ability to include this new category. If included, the new category could be presented as additional information. If CFA determines to include this new category, inclusion should be recommended but not required. We note that advisers rely on information received from sponsor firms that report UMA assets. We recommend that CFA adopt a “reasonable basis” standard for reliance on reports from third-party firms.

## **8. Non-Fee Paying Portfolios**

GIPS 20/20 would require that all actual discretionary portfolios be included in a composite (*i.e.*, it would remove the “fee-paying” limitation). The Consultation Paper seeks comment on whether firms should be prohibited from excluding non-fee paying portfolios from composites and how non-fee paying portfolios should be treated for net-of-fees calculations.

**Question 8a: Do you agree with no longer allowing firms to exclude non-fee-paying portfolios from composites based solely on fee-paying status?**

No. Firms should retain the option to exclude non-fee-paying portfolios, because some firms’ composites might be more meaningful without the inclusion of these accounts.

**Question 8b: How should non-fee-paying portfolios be treated for net-of-fees calculations?**

Firms should have the flexibility to choose whether to include non-fee-paying portfolios in composites based solely on fee-paying status since firms are in the best position to determine whether their inclusion or exclusion best serves investors’ interests. Firms should also be able to use model fees to calculate net-of-fees performance including average fees in similar portfolios. The lack of fee deduction for non-fee paying accounts could be addressed through disclosure.

If, notwithstanding our recommendation, firms are required to include non-fee paying portfolios in composites, they should be able to include such portfolios without additional requirements attaching.

### **9. References to the Firm's Claim of Compliance**

Under GIPS 20/20, firms would be able to demonstrate compliance in additional ways. Currently, firms may use any of three methods—a compliant presentation, an advertisement prepared in accordance with the GIPS Advertising Guidelines, and a GIPS Pooled Fund Claim of Compliance included in the official pooled fund document or fund-specific marketing material for a broadly-distributed pooled fund.

#### **Question 9: Do you agree that firms should have more flexibility to state that the firm complies with the GIPS standards?**

Yes. We encourage greater flexibility in this area. In addition to additional uses of traditional media, demonstration of GIPS compliance in a computerized world might include references in databases, links on websites, and other forms of evolving electronic access.

### **10. Timeliness and Frequency of Compliance Presentations**

Firms would be required to provide compliant presentations to prospective clients on a “timely” basis that must include more current performance. The proposal seeks comment on the appropriate timeliness of the performance data.

#### **Question 10a: Do you agree with requiring firms to update compliant presentations on a timely basis?**

Yes. While firms may conduct many assessments and reports of performance results, we believe it is appropriate to require a compliant presentation on an annual basis. Firms should be permitted but not required to report more frequently if more frequent reporting is consistent with their business, nature of the assets, policies and procedures, and commitments to investors.

#### **Question 10b: How current should the information be required to be in a compliant presentation?**

It is important to note that reports to existing clients on their holdings or the results of their investments are not the thrust of GIPS. Rather, GIPS presentations are about historical performance results to prospective clients considering future investments in assets managed under the composite. Nevertheless, we agree that, to remain compliant, firms should update information at least on an annual basis, consistent with their firm's policies and procedures.

In addition, CFA could consider allowing firms to use data from a verified GIPS presentation for up to 18 months after finalization in limited circumstances and consistent with their policies and

procedures. For example, this could help protect firms from foot-faults if they find it necessary to change vendors or firm personnel that may disrupt the process.

### **11. Estimated Trading Expenses**

Under GIPS 20/20, firms would be permitted to use estimated trading expenses, “if returns are equal to or lower than those that would have been calculated if actual trading expenses had been used.” Firms would be expected to determine the estimated trading expense rate based on other portfolios managed by the firm that do pay such expenses. The proposal notes that allowing estimated trading expenses could eliminate the need for specific wrap fee/SMA requirements and recommendations.

#### **Question 11: Do you agree with allowing firms to use estimated trading expenses?**

We generally agree. We believe that firms should have the flexibility to use estimated trading expenses, model trading expenses, or actual trading expenses. We recommend that CFA eliminate the condition that estimated trading expenses may only be used “if returns are equal to or lower than those that would have been calculated if actual trading expenses had been used,” because firms should have the flexibility to use estimated trading expenses in other instances as well, as long as their use is appropriately disclosed and not misleading. Firms that use estimated expenses would need to comply with the firm’s policies and procedures, and any use of estimated expenses would need to be clearly labeled as such and be internally and externally consistent.

### **12. Compliant Presentation Numerical Information and Disclosures**

CFA seeks to eliminate any terms or information that are not helpful or informative, but also wants to include any terms or data points that should be included. For example, GIPS 20/20 could permit removal of required data for periods outside a certain time as no longer relevant.

#### **Question 12a: Which existing numerical information and disclosure requirements, if any, should be removed?**

Numerical information should only be included if it is still relevant and material. Thus, for example, the “percent of non-fee paying accounts” should only be required if it is material, or if, in the judgment of the firm, failure to include it would result in a false or misleading presentation. In addition, consistent with relief to GIPS presentations provided in the recent Pooled Funds Guidance, use of a “benchmark” for comparison should be moved from “required” to “highly recommended.”

#### **Question 12b: Is there any information not currently required that should be required in compliant presentations?**

In keeping with the general principles outlined above, we recommend against any additional requirements for firms and instead suggest that inclusion of any proposed new information be

recommended. To the extent CFA requires additional information in a compliant presentation, however, IAA members would oppose requiring attribution, asset allocation, or similar information because it is difficult to standardize.

**Question 12c: Are there any disclosures that can be discontinued after a certain period-of-time?**

Disclosures should be discontinued (consistent with a firm's policies and procedures) once they are no longer relevant to the information being presented. Required disclosures should be relevant to the presentation and related to the time period covered. Some details about past mergers, name changes, benchmark changes, and years without verification, for example, particularly if they occurred in periods beyond required disclosure, should be able to be discontinued at the election of the compliant firm. We also suggest eliminating the requirement to state that the three-year standard deviation is not presented because monthly returns are not available.

**13. General**

**Question 13: Are there other issues that are important to address as part of the GIPS 20/20 project (e.g., private wealth, outsourced CIO, model/hypothetical performance, carve-outs and "building blocks")?**

As discussed above, any new guidance or requirements, if CFA determines to adopt new requirements, should defer to existing regulatory schemes, provide flexibility to firms, and carefully consider costs and burdens to firms and investors alike.

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We appreciate your consideration of our comments on this important consultation. Please do not hesitate to contact us if we may provide any additional information or assistance to you during this process.

Respectfully,



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