

New Q&A Furthers Inconsistent Cash Flow Guidance

The guidance outlined in the GIPS standards (and previously, the AIMR-PPS standards) for dealing with accounts that experience significant cash flows has been inconsistent throughout time.

- The first version of the AIMR-PPS standards, adopted in 1993, was silent on the issue.
- In the AIMR Newsletter published in January-February of 1996, a Q&A response indicated that “the AIMR-PPS standards do not permit a manager to remove a portfolio from a composite because of a large cash flow and then to return it to the composite the next measurement period.” Other subsequent Q&A mirrored this sentiment.
- The 1997 re-draft of the AIMR-PPS standards introduced the recommendation to treat large cash flows as temporary new accounts, i.e. the cash flow (not the total portfolio) would be excluded from the composite until fully invested to the strategy. It was further specified in this version of the Standards that this recommendation “should reduce the tendency of some managers to move accounts into and out of discretionary status as a result of large cash flows.” Nowhere is it indicated that removing accounts that experience large cash flows would jeopardize a firm’s claim of compliance. This version of the Standards also explicitly outlined that “all of the requirements and recommendations of the Standards are set forth in this Statement,” i.e., any other guidance or interpretations should not be considered binding.
- It was not until the 2001 re-draft of the

Here’s your opportunity to comment on the GIPS standards

If you want your comments to be considered during the 2010 review of the GIPS standards act now, the deadline is **August 15th!** It is imperative that you offer your input by completing the questionnaire which has been posted by the GIPS Executive Committee at the following link <http://is-nri.com/take/?i=117819&h=h0zM7ArRIAsD5mERNsrUg>

AIMR-PPS standards was published that it was clarified that “Firms that claim compliance with the AIMR-PPS standards must understand all the requirements and recommendations of the AIMR-PPS standards, including any updates, reports, or clarifications published by the AIMR-PPS Implementation Committee or the Investment Performance Council, including the most recent version of the AIMR Performance Presentation Standards Handbook.” At this point, Q&A and other interpretations published by AIMR (now the CFA Institute) became, essentially, an extension of the Standards.

- The original Guidance Statement on the Treatment of Significant Cash Flows was adopted with an effective date of June 30, 2002. The Guidance Statement allows the temporary removal of accounts that experience large cash flows, as long as certain documentation requirements are met and specific disclosures are made. The Guidance Statement does not permit retroactive application of a cash flow removal policy prior to June 30, 2002, and remained silent on whether firms that already had such a policy were or were not in compliance.
- Now, a new Q&A issued by the North American Investment Performance Council in January 2007 states that “for the period from January 1996 to June 2002 removing portfolios from composites due to large cash flows was not

permitted under the AIMR-PPS standards (i.e., firms could not use cash flows as a criterion to define portfolios as temporarily non-discretionary).”

For firms that came into compliance prior to 2002, (when the Q&A was not as accessible or considered a required extension of the Standards) Ashland believes it is inappropriate for the NAIPC to take such a stance and require the earliest adoptees of the Standards to restate material performance if removed accounts were re-included. It is a disservice to the industry if such re-inclusion actually shows performance based on a large cash position rather than performance of the manager’s fully invested portfolios. ■

Do the GIPS police exist?

So who polices firms that claim compliance with the GIPS standards? While nothing has been formally outlined, the SEC does act as the GIPS police. If a firm is registered with the SEC and also is claiming compliance with GIPS, the SEC **does** have authority to note any deficiencies that they find during their examination which pertain to GIPS compliance. Many firms in need of guidance after having received a deficiency letter because the SEC found their claim of compliance to be false decide to engage Ashland Partners. ■

Gross Versus Net in Advertisements

The GIPS standards do not specify whether firms show gross or net. The requirement is simply to disclose which type of performance is being shown. However, in the US, the SEC dictates that when a marketing piece is distributed in any fashion other than a one-on-one presentation (thus deemed an advertisement), net must be shown net of management fees. Firms are permitted to also show gross performance but net must be at least equally prominent.

The SEC's requirement to show net in an advertisement only pertains to **performance**. The SEC has **not** specified that statistics such as alpha, tracking error, and sharpe ratio, must also be shown net of fees. Ashland recommends clearly labeling the ratio as having been calculated

using gross performance. Comparing two different managers' net-of-fee performance statistics distorts the true picture. ■

Ashland Compliance Group – The CCO Resource

The U.S. Securities and Exchange Commission has released the information for the 2007 CCO Outreach Regional Seminars. This year's seminars will discuss the following topics:

- The Examination and Risk Assessment Process;
- Books and Records and Disclosures and Filings;
- Brokerage Arrangements, Best Execution, Trade Allocation, and Soft Dollars;
- Portfolio Management; and
- Marketing, Performance, Advertising, and Distribution.

The seminars last about 3 or 4 hours depending on location. Attendance for the seminars is limited and is offered on a first come/first served basis with priority given to CCOs (one seminar in New York is already full). For additional information go to www.sec.gov/info/cco/ccorsgeninfo2007.htm. Click on the Registration link for information relating to dates, locations and times. ■

NEW Website Launched

There is now a new website dedicated solely to the GIPS standards. For those of you who had tried searching for information on the old website, you will find this one much easier to navigate. Thanks to the CFA Institute!

<http://www.gipsstandards.org/>

THE ASHLAND CORNER

2007 CIPM Examination Prep Webinar

This online seminar is designed to be a convenient educational solution to complement CIPM reading materials and courseware. **Interactive lunch-hour presentations** combined with practice questions, weekly **open labs** and **24/7 Q&A access** via email offer both Principle and Expert candidates a comprehensive solution for exam success. Please visit our website for more information on dates and curriculum. www.ashlandpartners.com. ■

Join us for a full day

Principle Level CIPM Review Course

August 21, 2007, in Philadelphia ■ 8:00am–7:00pm

This workshop is designed for those who are taking the CIPM Principles Exam in September–October 2007.

The Exam Review is not intended as a substitute for independent study. It will be most effective for those candidates that have already read the material and seek further clarification on key topics and to synthesize material.

CFA Charterholders will be able to earn Professional Development (PD) hours.

Special Notice: There are only 24 spots in this review session. Please visit our website www.ashlandpartners.com to sign up early and secure your spot!

ASHLAND PROFILE

Geoff C. Lowry

Director – Ashland Partners International Limited



Geoff joined Ashland Partners International in February 2007 as a Director, with over 15 years of experience in the Investment Industry. After initially gaining experience in a client relations role, Geoff moved into the Performance Measurement arena. Geoff's experience covers over 12 years of performance measurement, attribution and statistical analysis. Prior to joining Ashland, he spent the last 8 years as Head of Performance for two London-based firms in which he gained broad exposure to GIPS.

Geoff manages our Australian office, and is based at Southport on the Gold Coast of Queensland. ■