



SBA Apéritif GIPS® Global Investment Performance Standard

## **GIPS® and MiFID: potential for synergies or different topics?**

Marc Siegel / Susanne Klemm

Geneva, November 13, 2007

---

### **Agenda**

#### **1. MiFID: What it means for Swiss Banks**

- § Best practice
- § Impact depending on the structure of the bank

#### **2. MiFID Requirements in the GIPS context**

#### **3. Implementation issues of those topics**

- § Analysis Phase
- § Implement compliance process

#### **4. How GIPS can help**

- § Additional MiFID topics where GIPS can help
- § MiFID as opportunity ?

## Agenda

### 1. MiFID: What it means for Swiss Banks

- § Best practice
- § Impact depending on the structure of the bank

### 2. MiFID Requirements in the GIPS context

### 3. Implementation issues of those topics

- § Analysis Phase
- § Implement compliance process

### 4. How GIPS can help

- § Additional MiFID topics where GIPS can help
- § MiFID as opportunity ?

## MiFID: What it means for Swiss banks

### MiFID: What is it all about

§ **MiFID** is a **EU Directive**, which has to be transposed into national law and implemented in **all EEA countries** (EU countries plus Iceland, Liechtenstein and Norway) as of 1 November 2007

#### § What are the objectives of MiFID?

- Create one single market for investment service providers
- Improve **transparency** and efficiency of the financial markets
- Increase investor protection and harmonize conduct of business rules

#### § To whom does MiFID apply?

- Investment firms, banks, brokers, credit institutions
- Portfolio managers, investment advisors, independent asset managers
- Multilateral trading facilities, regulated markets

#### § Which services and activities does MiFID apply to?

- Acceptance, transmission and execution of orders
- Dealing on own account or on behalf of clients
- **Portfolio management** and investment advice
- Investment research and financial analysis

#### § Which financial instruments are covered by MiFID?

- Transferable securities
- Money market instruments and financial derivatives
- Shares in funds, commodities



## MiFID: What it means for Swiss banks

### CH MiFID Impact

MiFID is not only about Swiss banks' European locations, but also relates to business relations with EEA counterparties

#### Regulatory Requirements

§ For **cross-boarder services** to clients domiciled in EEA countries ( for example in Germany: WpHG 31 Clients)

#### Litigation Risk

§ Clients domiciled in EEA countries could sue Swiss banks due to the **Lugano convention** if a Swiss Bank is not MiFID compliant (e.g. if no suitability and appropriateness tests are performed or if the reporting and disclosures are not provided in accordance with MiFID)

#### Client Expectations and Best Practice

- § Counterparties (e.g. EAMs in EEA) subject to MiFID supervision will outsource/delegate selected MiFID rules to their banking partners
- § MiFID is likely to become **best practice** in selected areas – clients will compare services received from banks in EEA and Switzerland
- § Most of the big CH wealth managers will implement selected rules of MiFID

## MiFID: What it means for Swiss banks

### CH MiFID Impact: Clients & Products

		Clients		
		CH	EEA	Other
Booked in	CH	No impact	Impact (Offshore clients)	No impact
	EEA	Usually N/A (potential impact)	Full MiFID (Onshore)	Usually N/A (potential impact)
	Other	No impact (e.g. Singapore)	Impact (Offshore clients)	No impact

		Products		
		CH	EEA	Other
Produced in	CH	No impact	Full MiFID (central PM, marketing, investment research, distribution channels, custody)	No Impact
	EEA	No impact	Full MiFID	No impact
	Other	No impact	Full MiFID (Funds, marketing, distribution channels)	No Impact

GIPS

## Agenda

### 1. MiFID: What it means for Swiss Banks

- § Best practice
- § Impact depending on the structure of the bank

### 2. MiFID Requirements in the GIPS context

### 3. Implementation issues of those topics


- § Analysis Phase
- § Implement compliance process

### 4. How GIPS can help

- § Additional MiFID topics where GIPS can help
- § MiFID as opportunity ?

## MiFID Requirements in the GIPS context

### MiFID Scope vs. GIPS Scope

MiFID Scope		GIPS Coverage
§ MiFID concerns information on investment products independently of the specific service provided to the client		§ GIPS only concern portfolio management mandates. There are no advisory relationships covered
§ MiFID implements information requirements towards potential and existing clients		§ GIPS concern potential / future clients
§ MiFID sets additional specific reporting requirements to client (especially "retail clients") for portfolio management services		§ GIPS are not mandatory to be used for existing clients § The portfolio reporting of a GIPS compliant firm does not need to be GIPS compliant. § GIPS concern composites. A composite is defined as an aggregation of individual portfolios managed according to a similar investment mandate, objective of strategy.

This means GIPS does not cover MiFID reporting requirements like:

Reporting on specific client transaction	Portfolio Management Statements	Loss Reporting
§ Clients have to be promptly advised of the details of a transaction (next business day) with additional features (e.g. execution venue, date and time of execution) compared to the existing Swiss practice.	§ Specific requirements for content (e.g. benchmark, total amount of dividends and interests received etc.). § Requirements for portfolio management statement frequency.	§ Losses exceeding a predetermined threshold need to be reported to retail clients.

## MiFID Requirements in the GIPS context

Financial Promotion – Requirements and Definition

### MiFID overall requirements

- § Under MiFID all publications are treated either as **investment research** or **marketing material**.
- § Specific rules apply to these two types of Financial Promotion material

### Investment research

### Marketing material

- § All Information given to client must be fair, clear, not misleading, accurate and appropriate for the target audience. Recommendation which is addressed to the public and does not meet the conditions of "Investment Research"
- § Is clearly identified as Marketing material
- § Balanced in terms of description of potential benefits and relevant risks

## MiFID Requirements in the GIPS context

Financial Promotion

### MiFID

Art. 19 II MiFID	All information, including marketing communications, addressed by the investment firm to clients or potential clients shall be <b>fair, clear and not misleading</b>
Art. 19 II MiFID	Marketing communication shall be clearly <b>identifiable as such</b>
Art. 27 II MiFID II	Marketing communication shall include the <b>name of the investment firm</b>
Art. 27 II MiFID II	Marketing communication shall be <b>accurate</b> and in particular shall not emphasise any potential benefits of an investment service or financial instrument without also giving a fair and prominent <b>indication of any relevant risks</b>



### GIPS Coverage

The objective of the GIPS (and of a GIPS Composite Report) is to be transparent and fair	<b>4</b>
GIPS do not specifically address this point	<b>8</b>
GIPS reports mention the definition of the GIPS firm ( <b>Art. 4.A.1</b> )	<b>4</b>
The Requirements of GIPS to indicate risk are <b>limited</b> : § <b>Art. 4.A.5</b> . FIRMS MUST disclose the presence, use, and extent of leverage or derivatives (if material), including a sufficient description of the use, frequency, and characteristics of the instruments to identify risks.	
§ <b>Art. 5.A.1 d</b> A measure of DISPERSION of individual PORTFOLIO returns for each annual period.	▲
GIPS <b>recommend</b> composite level risk measures ( <b>Art. 5.B.2</b> ): § It is <b>RECOMMENDED</b> that FIRMS present relevant COMPOSITE-level risk measures, such as beta, tracking error, modified duration, information ratio, Sharpe ratio, Treynor ratio, credit ratings, value at risk (VaR), and volatility, over time of the COMPOSITE and BENCHMARK.	

## MiFID Requirements in the GIPS context

### Financial Promotion

MiFID	
Art. 27 II MiFID II	Marketing communication shall be sufficient for, and presented in a way that is likely to be <b>understood</b> by, the average member of the group to whom it is directed, or by whom it is likely to be received
Art. 27 II MiFID II	Marketing communication shall not disguise, diminish or obscure <b>important items, statements or warnings</b>
Art. 27 IV MiFID II	The performance indication must <b>not be the most prominent</b> feature of the communication
Art. 27 IV MiFID II	The performance indication must include appropriate performance information which covers the immediately <b>preceding 5 years</b> or the whole period for which the financial instrument has been offered but at least the performance indication must be based on a complete 12-month periods
Art. 27 IV MiFID II	The <b>reference period</b> and the <b>source of information</b> must be clearly stated
Art. 27 IV MiFID II	The performance indication must contain a <b>prominent warning</b> that the figures refer to the past and that past performance is not a reliable indicator of future results



GIPS Coverage	
Key objective of GIPS	4
Covered by disclosure requirements	4
GIPS proposes a balanced presentation consisting of performance reporting and disclosures.	4
<b>Art. 5.A.1.a.</b> At least 5 years of performance (or a record for the period since firm or composite inception ...) that meets the requirements of the GIPS standards; after presenting 5 years of performance, the firm must present additional annual performance up to 10 years.	4
<b>Art. 5.A.1.b.</b> Annual returns for all years.	4
The reference period is clearly stated. The source of information is not specifically addressed.	▲
A warning is not mentioned in GIPS and has to be added to a GIPS compliant composite report.	8

10 | GIPS and MiFID: potential for synergies or different topics?  
Ernst & Young 2007

ERNST & YOUNG

## MiFID Requirements in the GIPS context

### Financial Promotion

MiFID	
Art. 27 IV MiFID II	Where the performance indication rely on figures denominated in <b>another currency</b> that the one of the client or potential client's state of residence, the currency must be clearly stated, together with a warning that the return may increase or decrease as a result of currency fluctuations
Art. 27 IV MiFID II	Where the performance indication is based on gross performance, the effect of <b>commissions, fees or other charges must be disclosed.</b>



GIPS Coverage	
<b>Art. 4.A.4</b> FIRMS MUST disclose the currency used to express performance.	▲
There is no warning required by GIPS, this has to be added to a GIPS report.	▲
<b>Art. 4.A.6.</b> FIRMS MUST clearly label returns as GROSS-OF-FEES or NET-OF-FEES.	4
<b>Art. 4.A.12.</b> FIRMS MUST disclose the FEE SCHEDULE appropriate to the presentation.	4
<b>Art. 4.A.14</b> If a COMPOSITE contains PORTFOLIOS with BUNDLED FEES, FIRMS MUST disclose the various types of fees that are included in the BUNDLED FEES.	4
<b>Art. 4.A.15</b> When presenting GROSS-OF-FEES RETURNS, FIRMS MUST disclose if any other fees are deducted in addition to the direct TRADING EXPENSES.	4
<b>Art. 4.A.16</b> When presenting NET-OF-FEES RETURNS, FIRMS MUST disclose if any other fees are deducted in addition to the INVESTMENT MANAGEMENT FEE and direct TRADING EXPENSES.	4

11 | GIPS and MiFID: potential for synergies or different topics?  
Ernst & Young 2007

ERNST & YOUNG

## MiFID Requirements in the GIPS context

### Financial Promotion

MiFID	
Art. 29 VII MiFID II	Marketing Communication has to be <b>consistent</b> with any information that the firm provides to clients in the course of carrying on investment and ancillary services
Art. 29 VIII MiFID II	Where a Marketing Communication contains an <b>offer or an invitation to enter into an agreement</b> in relation to a financial instrument or investment service, the relevant Marketing communication has to include all information required by Art. 30 to 33 MiFID. This does not apply if, in order to respond to an offer or invitation contained in the marketing communication, the potential client must refer to another document, which alone or in combination contain that information.
Art. 27 VIII MiFID II	The information shall not use the <b>name of any competent authority</b> in such a way that would indicate or suggest endorsement or approval by the authority of the products or services of the investment firm



GIPS Coverage	
GIPS do not address this point	<b>8</b>
GIPS do not address this point	
See separately the information provided by GIPS in response to Art. 30-33 MiFID II.	▲
GIPS do not address this point	<b>8</b>

## MiFID Requirements in the GIPS context

### Financial Promotion

MiFID	
Art. 27 VII	Where the information refers to a particular <b>tax treatment</b> , it shall be prominently state that the tax treatment depends on the individual circumstances of each client and may be subject to change in the future
Art. 51 I MiFID II	Marketing Communication has to be kept at <b>least 5 years</b>



GIPS Coverage	
Tax treatment relates to the treatment of the withholding tax for the purpose of performance calculation.	
<b>Art. 4.A.7 FIRMS MUST</b> disclose relevant details of the treatment of withholding tax on dividends, interest income, and capital gains. If using indexes that are net-of-taxes, the FIRM MUST disclose the tax basis of the BECHMARK (e.g., Luxembourg based or U.S. based) versus that of the COMPOSITE.	▲
GIPS has specific Record Keeping Requirements: all GIPS relevant underlying information (e.g. records to allow the recalculation of composite returns) need to be maintained for each year presented in a GIPS compliant track record.	▲
It is recommended to keep GIPS-relevant marketing information.	

## Agenda

### 1. MiFID: What it means for Swiss Banks

- § Best practice
- § Impact depending on the structure of the bank

### 2. MiFID Requirements in the GIPS context

### 3. Implementation issues of those topics

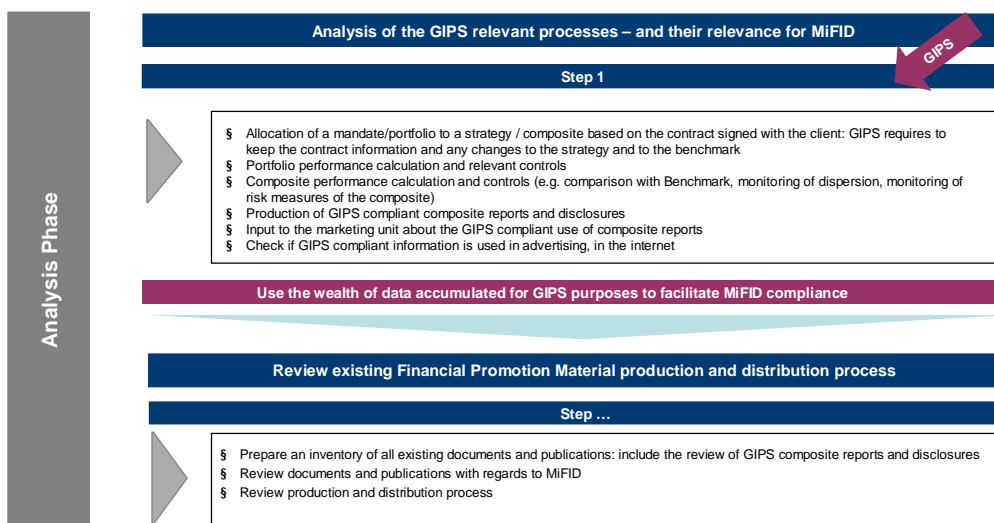
- § Analysis Phase
- § Implement compliance process

### 4. How GIPS can help

- § Additional MiFID topics where GIPS can help
- § MiFID as opportunity ?

## Implementation issues

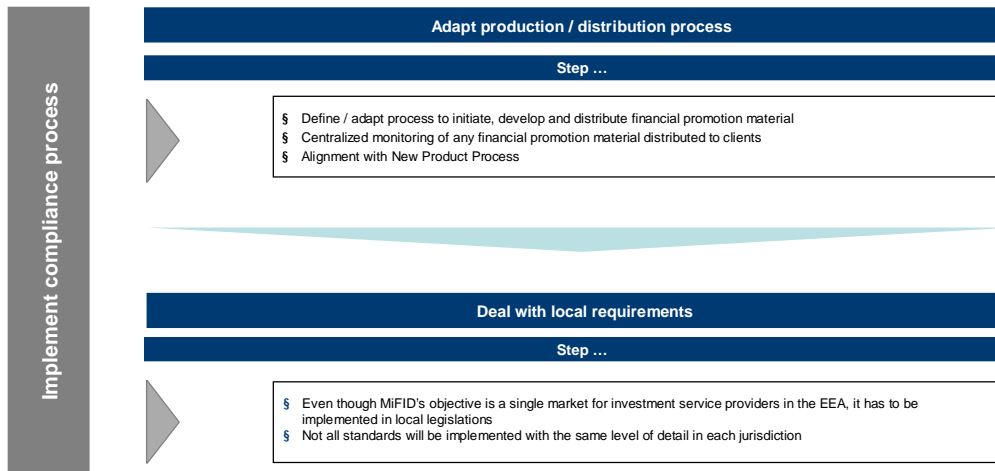
Review of production / distribution process





## Implementation issues

Review of production / distribution process



## Agenda

### 1. MiFID: What it means for Swiss Banks

- § Best practice
- § Impact depending on the structure of the bank

### 2. MiFID Requirements in the GIPS context

### 3. Implementation issues of those topics

- § Analysis Phase
- § Implement compliance process

### 4. How GIPS can help

- § Additional MiFID topics where GIPS can help
- § MiFID as opportunity ?

## Additional MiFID topics where GIPS can help

### Portfolio Management Information

MiFID	
Art. 30 (3) MiFID II	a) Information on the <b>method and frequency of valuation</b> of the financial instruments in the client portfolio
	b) Details of any <b>delegation of the discretionary management</b> of all or part of the financial instruments or funds in the client portfolio



GIPS Coverage
<b>Art. 1.A.2</b> PORTFOLIO valuations <b>MUST</b> be based on MARKET VALUES (not cost basis or book values).
<b>Art. 1.A.3</b> For periods prior to 1 January 2001, PORTFOLIOS <b>MUST</b> be valued at least quarterly. For periods between 1 January 2001 and 1 January 2010, PORTFOLIOS <b>MUST</b> be valued at least monthly. For periods beginning 1 January 2010, FIRMS <b>MUST</b> value PORTFOLIOS on the date of all LARGE EXTERNAL CASH FLOWS.
<b>Art. 1.A.4</b> For periods beginning 1 January 2010, FIRMS <b>MUST</b> value PORTFOLIOS as of the calendar month-end or the last business day of the month.
<b>Art. 4.A.25</b> FIRMS <b>MUST</b> disclose if, prior to 1 January 2010, calendar month-end PORTFOLIO valuations or valuations on the last business day of the month are not used.
<b>Art. 4.B.2</b> FIRMS <b>SHOULD</b> disclose when a change in a calculation methodology or valuation source results in a material impact on the performance of a COMPOSITE return.
<b>Art. 4.A.18</b> Beginning 1 January 2006, FIRMS <b>MUST</b> disclose the use of a subadvisor(s) and the periods a subadvisor(s) was used.

## Additional MiFID topics where GIPS can help

### Portfolio Management Information

MiFID	
Art. 30 (3) MiFID II	c.) A specification of any <b>benchmark</b> against which the performance of the client portfolio will be compared
	d.) The <b>types of financial instruments</b> that may be included in the client portfolio and <b>types of transactions</b> that may be carried out in such instruments, including any limits;
	e.) The <b>management objectives, the level of risk</b> to be reflected in the manager's exercise of discretion, and any specific constraints on that discretion.



GIPS Coverage
<b>GIPS require the disclosure of a benchmark (or a customized benchmark) per composite</b>
<b>Art. 5.A.6</b> The total return for the BENCHMARK (or BENCHMARKS) that reflects the investment strategy or mandate represented by the COMPOSITE <b>MUST</b> be presented for each annual period. If no BENCHMARK is presented, the presentation <b>MUST</b> explain why no BENCHMARK is disclosed. If the FIRM changes the BENCHMARK that is used for a given COMPOSITE in the performance presentation, the FIRM <b>MUST</b> disclose both the date and the reasons for the change. If a custom BENCHMARK or combination of multiple BENCHMARKS is used, the FIRM <b>MUST</b> describe the BENCHMARK creation and re-balancing process.
<b>Art. 4.A.20</b> GIPS requires to disclose the composite description (= strategy description)
<b>Art. 4.A.5</b> Firms must disclose the presence, use, and extent of leverage or derivatives (if material), including a sufficient description of he use, frequency, and characteristics of the instruments to identify risks.
GIPS do not address the question of limits.
The management objectives and limited risk information need to be reflected in the definition of the composite strategy. Constraints on discretion need to be specified in the investment mandate (contract).

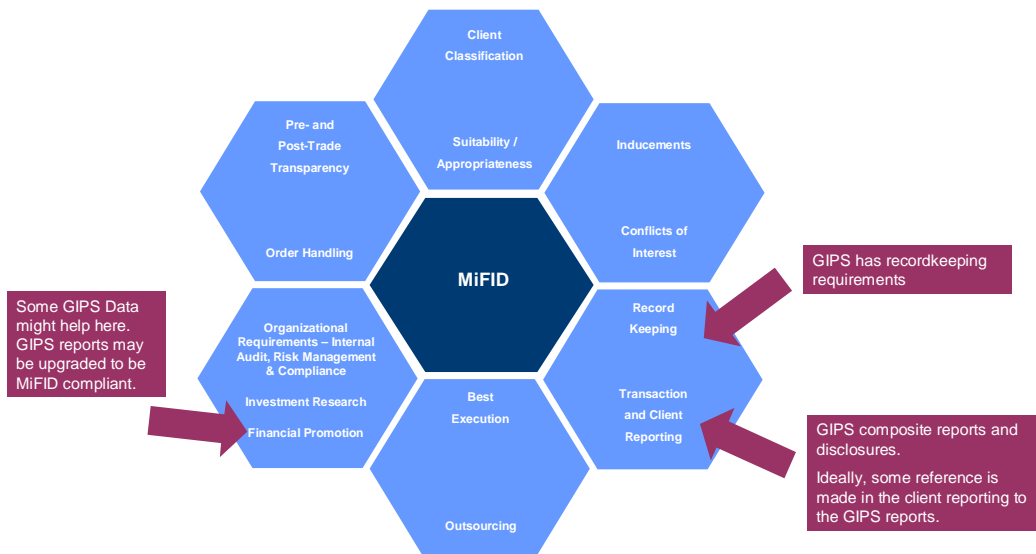
## Additional MiFID topics where GIPS can help

### Risk disclosures

MiFID		GIPS Coverage	
Art. 31	Investment firms to provide clients / potential clients with a <b>general description of the nature and risks of financial instruments</b>	<b>GIPS will give information on the nature of the strategy (on the composite level).</b>	
2. a)	.... including an <b>explanation of leverage</b> ...	<b>Art. 4.A.5</b> Firms must disclose the presence, use, and extent of leverage or derivatives (if material), including a sufficient description of he use, frequency, and characteristics of the instruments to identify risks.	
2. b)	the <b>volatility of the price</b> of such instruments and any limitations on the available market fur such instruments	<b>GIPS recommends (5.B.2) to present information on the volatility of the strategy (composite) and the benchmark.</b>	
		<b>Art. 5.B.2.</b> It is RECOMMENDED that FIRMS present relevant COMPOSITE-level risk measures, such as beta, tracking error, modified duration, information ratio, Sharpe ratio, Treynor ratio, credit ratings, value at risk (VaR), and volatility, over time of the COMPOSITE and BENCHMARK.	

## MiFID as an opportunity ?

How can information available and produced for GIPS be helpful to meet MiFID requirements



[www.ey.com/ch](http://www.ey.com/ch)

© 2007 Ernst & Young Ltd  
All Rights Reserved.  
Ernst & Young is a  
registered trademark

**Marc Siegel**  
Senior Manager  
Ernst & Young Ltd  
CH-1213 Geneva  
Tel +41 58 286 57 17  
Mobile +41 58 289 57 17  
Fax +41 58 286 59 45  
eMail [marc.siegel@ch.ey.com](mailto:marc.siegel@ch.ey.com)

**Susanne Klemm**  
Senior Manager  
Ernst & Young Ltd  
CH-3004 Bern  
Tel +41 58 286 69 14  
Mobile +41 58 289 69 14  
Fax +41 58 286 69 69  
eMail [susanne.klemm@ch.ey.com](mailto:susanne.klemm@ch.ey.com)