

# Performance Reporting Basics



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Laws and regulations

Annual investment performance reports

Market value

Performance and sales communications

- Section 75.2 of the Act requires firms to deal fairly, honestly and in good faith with their clients
- Section 100(2) of the Act prohibits registrants from making statements about matters that a reasonable investor would consider important if such statements are untrue or omit information that is necessary to prevent the statements from being false or misleading.

- NI 31-103
  - Section 14.18 - Investment performance report
  - Section 14.19 - Content of investment performance report
  - Section 14.20 - Delivery of report on charges and other compensation and investment performance report

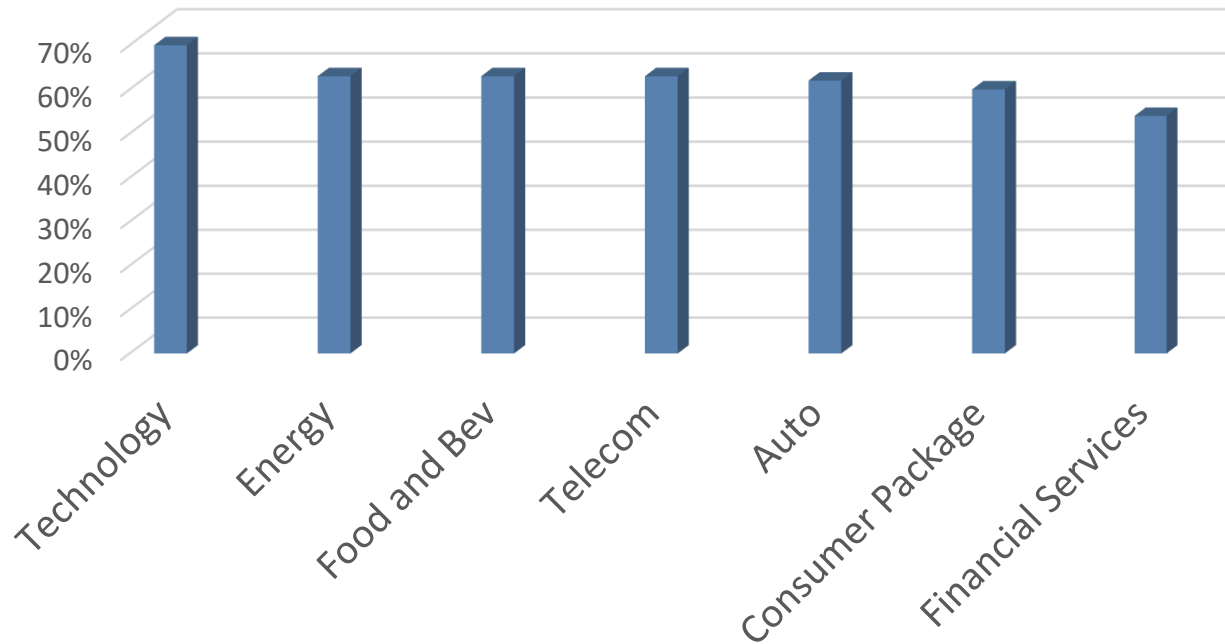
- NI 81-106
  - Part 14, Calculation of Net Asset Value
  
- NI 81-102
  - Part 15, Sales Communications and Prohibited Representations

- NI 31-103CP
  - Part 14
- NI 81-106 CP
  - Part 9, Net Asset Value
- NI 81-102CP
  - Part 13, Sales Communications and Prohibited Representations
- ASC Notice 33-705
- CSA Staff Notice 31-345 Cost Disclosure, Performance Reporting and Client Statements
- CSA Staff Notice 31-325 Marketing Practices of Portfolio Managers (July 2011)

- Client Relationship Model Phase 2 (CRM2)
- Three year transition period, from 2013 to 2016

# “Do you trust this industry to do the right thing?”

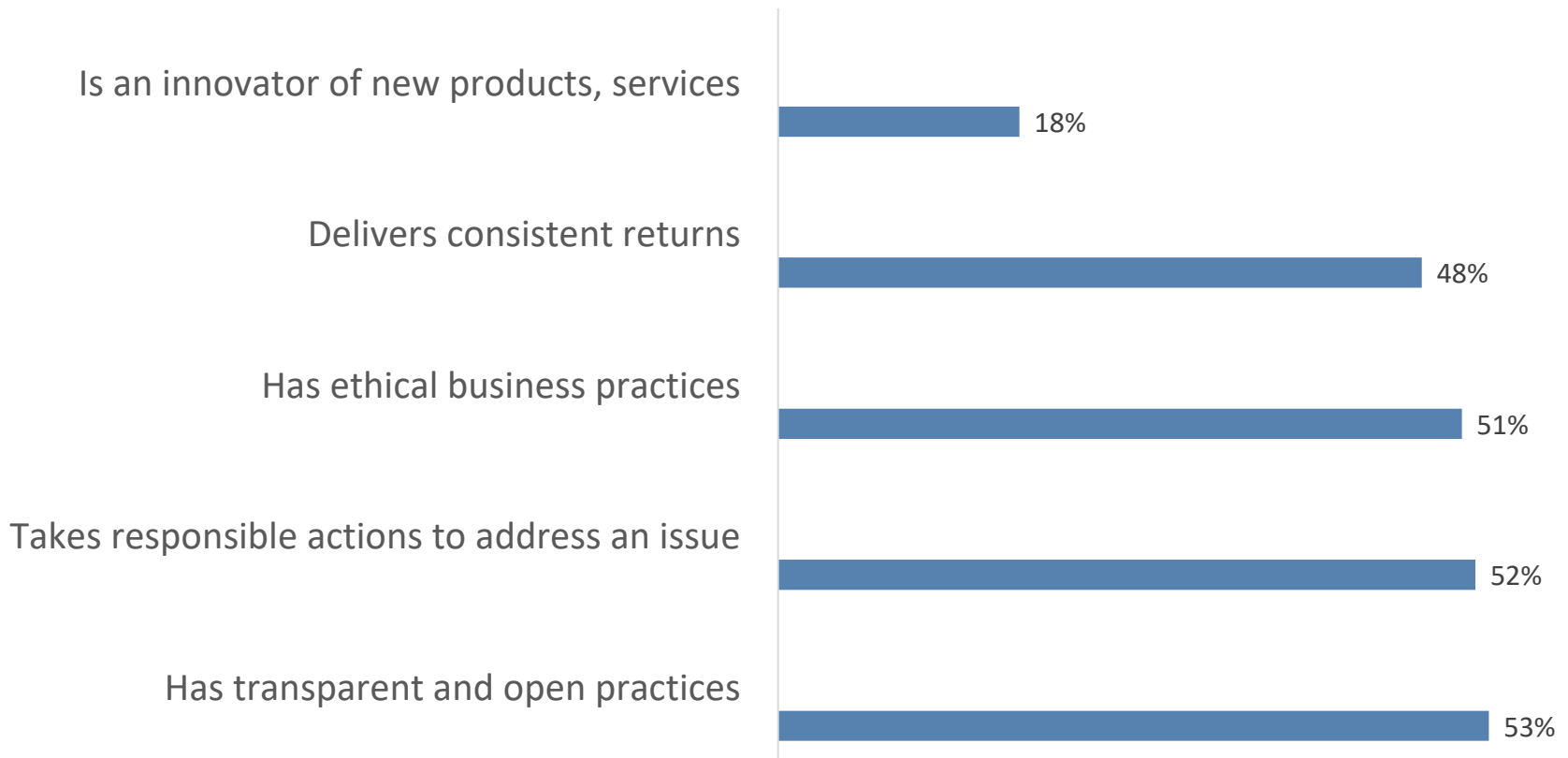
## 2018 Edelman Trust Survey





# Top attributes that build trust in an investment manager

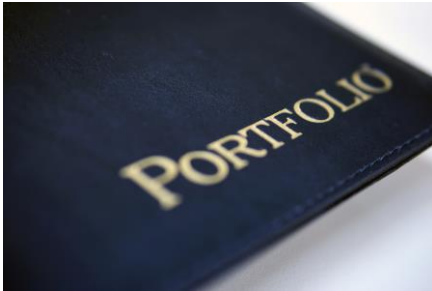
## 2013 CFA/Edelman Survey



Who must send investment performance reports to clients?

- Advisers
  
- And EMDs if...

# Performance statements are sent to clients



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## When must performance reporting be sent?

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- The account has existed for at least 12 months and within 24 months of the first trade
- Every 12 months thereafter

Not required:

- Where a client account has existed < 12 months
  - For a dealer executing trades only as directed by a registered adviser acting for the client
  - For permitted clients that are not individuals
  - When no market value can be determined for any of the securities
  - When client ceases to be a client
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Must contain text, tables and charts showing:

- Change in value for 12 month period
- Change in value since inception
- Annualized total % return net of charges (money-weighted)
- Definition of annualized total return
  - Including that it is net of charges
  - The calculation method used (money-weighted)
  - Simple explanation of what the calculation method takes into account

## Change in value – 12 month period

A	Market value of all cash and securities at Y/E	\$1,015
B	Market value of all cash and securities at beginning of 12 month period	\$1,000
C	Market value of all deposits and transfers in	\$4
D	Market value of all withdrawals and transfers out	\$17
	Annual change in market value of account    A - B - C + D	\$28

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## Change in value – since account opening

A	Closing market value at Y/E	\$49,785.21
E	Market value of all deposits and transfers in since account opening*	\$22,500.00
F	Market value of all deposits and transfers out since account opening	\$4,900.00
	Cumulative change in market value of account    A - E + F	\$32,185.21

\*Date Opened: dd/mm/yr



- Money-weighted rate of return
  - Personal rate of return, that is, what the account has experienced
  - Equivalent to the IRR (internal rate of return)
  - Takes into account cash flows in the account, if any
  - Calculated with a financial calculator or Excel IRR formula

	Past year	Past 3 years	Past 5 years	Past 10 years	Since inception
Your account	12.40%	5.42%	4.67%	6.77%	9.88%

## Excel XIRR example

		Year 1	Year 2	Year 3
Starting value	-\$ 100,000.00			
Deposits (+)		\$ 10,000.00		
Withdrawals (-)			-\$ 4,000.00	
Dividends (+)		\$ 4,000.00	\$ 6,000.00	\$ 6,000.00
Ending Value				\$ 98,000.00
Total Cash Flows	-\$ 100,000.00	\$ 14,000.00	\$ 2,000.00	\$ 104,000.00
			<b>IRR</b>	<b>6.89%</b>

- “This shows the total percentage return of your account for the period ending MM/DD/YYYY. Returns are calculated after charges have been deducted. These include charges you pay for advice, transaction charges and account-related charges, but not income tax.”
- “We use a money weighted method to calculate rates of return. The returns in this table are your personal rates of return.”
- “Your returns are affected by changes in the value of the securities you have invested in, dividends and interest that they paid, and also deposits and withdrawals to and from your account.”
  - Appendix E, NI 31-103CP

- For now, at a minimum it must include the 12-month return and annualized “since inception” return
  - A period of less than one year from inception must not be annualized
  
- 3 year return – statement period ending December 31, 2018
- 5 year return – statement period ending December 31, 2020
- 10 year return – statement period ending December 31, 2025  
(calendar year-end examples above)

### 14.1.1 Duty to provide information

- IFM has the duty to provide information, including NAV, to enable dealers and advisers to meet their reporting obligations
- For a non-listed investment fund, market value will be the NAV provided by the investment fund manager

For other securities, market value is “the amount that the registered firm reasonably believes to be the market value of the security” after referring to:

- Last bid (long) quoted on a market or last ask (short) and making any adjustment necessary
- Inter-dealer price quote or published market reports and making any adjustment necessary
- Policies of the firm, using
  - Observable inputs
  - Unobservable inputs

- What are the valuation policies and procedures of the firm?
- What are the firm's policies with respect to estimates?
- Notification to client
  - “There is no active market for this security so we have estimated its market value.”

- Process for monitoring significant events or other situations that could affect the security
- Methodology for determining fair value for illiquid securities
- Methods by which the manager will review and test valuations to evaluate the quality of the prices obtained as well as the general functioning of the valuation process
- Should consider whether its valuation process deals with conflicts of interest



- The security is illiquid
- There is little or no issuer and issuer-related financial data available, or the data is stale
- There is little or no financial data available for comparable issuers or for the issuer's business sector
- There is not enough data to use the International Financial Reporting Standards (IFRS) based valuation methodologies
- The acquisition cost of the security is no longer a good estimate of the security's market value as the cost is outside the range of possible values for the security

- If the firm reasonably believes it cannot determine the market value of a security, it must report its value as “not determinable” in client statements and exclude it from the calculations in client statements and performance reports
- Must be reasonable basis for “not determinable”
  - Not just because the security is illiquid
- Firm must make a judgement in moving from “not determinable” to “\$0”

Can the firm rely on the valuation provided by the issuer?

- The firm is responsible for the information reported to its clients.

*“The firm may not simply take valuation information from an issuer and pass it on to clients as the market value for purposes of the firm’s reporting obligations. The firm must exercise its professional judgement as to the reliability of information provided by an issuer as an input to the firm’s determination of market value. It should retain a record of the reasons for its decision.”* – CSA Staff Notice 31-345

- For mortgage investment entities, portfolio impairments must be recognized and NAV adjustments made
- *IFRS 9 Financial Instruments* will apply to 2018 financial statements and will have a particular impact on accounting for impairments
- Dividend distributions are not the same as annualized rates of return

*“Ethical standards for investment performance to ensure fair representation and full disclosure of investment performance”*

- CFA Institute developed global standards for calculating and presenting investment performance
- Continually updated through interpretations, guidance and new provisions
- Many institutional investors, and increasingly, the HNWI sector, demand GIPS compliance. GIPS compliance enhances a firm’s credibility when marketing to institutional investors and investment consultants

- Must disclose a benchmark, and if you can't find an appropriate one, disclose why there isn't one
- If there are assets which have been hard to value and you have applied anything other than a market price, you must disclose what method you have used to value them
- Use of hypothetical or back-dated portfolios or a model return is not permitted under GIPS
- Mandatory disclosures

A representation of investment performance would be misleading if it is:

- a portrayal of past income or asset growth that gives an impression of investment results that is not justified;
- a representation about security of capital that is not justified, or a representation about possible future gains or income; or
- a presentation of past investment performance that implies that future gains or income may be inferred from past performance.

- “Over 20% gain in 2016”
  - Which fund?
  - Net of fees or gross of fees?
  - Selective time period
- Graphs that compare performance against completely different types of securities (i.e. inappropriate benchmarks)
- Stale performance
- “Outperformed the industry benchmark at key times”



- Question of fairness
- If you refer to a credit rating, that rating must be current and prepared by a designated rating organization
- If you use a benchmark, it must be a fair comparison, and not misleading

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## Questions?

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- Thank you for your attention!