



GUIDANCE FOR COLLECTIVE INVESTMENT SCHEMES ON VALUATION, INVESTMENT PERFORMANCE MEASUREMENT, REPORTING AND OTHER RELATED MATTERS

Introduction

The Capital Markets Master Plan recognizes that the asset management sector is an important component of the Capital Markets. A robust asset management sector is critical to facilitate access to the capital markets by investors and to support the development and economic transformation of the Country.

The Capital Markets Authority (the Authority) has over time noted inconsistencies in performance measurement and presentation in the Collective Investment Schemes (CIS) industry. Following our observations and feedback received from the market, there has arisen the need to standardize investment performance measurement and presentation by CIS's. It is on this basis that the Authority has developed the following guidance to enhance comparability and consistency of information presented in the performance measurement report disseminated across the industry to ultimately boost investor confidence.

This Guidance borrows from the principles for the Valuation of Collective Investment Schemes by the International Organization of Securities Commissions (IOSCO) and the Global Investment Performance Standards (GIPS®) to entrench international best practice in the sector.

1. Application

This Guidance is intended for all Collective Investment Schemes approved by the Authority and should be read together with the Capital Markets (Collective Investment Schemes) Regulations.

2. CIS Operations

- 2.1** The fund manager shall establish comprehensive, documented investment policies and procedures to govern the valuation of assets held by a CIS;
- 2.2** The policies and procedures should identify the methodologies that will be used for valuing each type of asset and should clearly indicate how performance shall be calculated measured and presented. These policies

and procedures should be consistent across similar types of assets and across all funds;

- 2.3 The fund manager shall ensure that all policies referred to in 2.2 above comply with this guidance and shall disclose in the performance measurement report, any material changes in these policies and methodologies;
- 2.4 The fund manager shall identify and document, in the valuation policies and procedures, conflicts of interest and measures to address them;
- 2.5 The fund manager shall have policies and procedures in place that seek to detect, prevent and correct pricing errors. Pricing errors that result in material harm to CIS investors should be addressed promptly and investors fully compensated;
- 2.6 In establishing the different funds, the fund manager shall be guided by the following criteria on composition of the funds:
 - a) **Money Market Fund:** Invests only in interest-earning money market instruments which have a maximum weighted average tenor of thirteen (13) months and includes commercial papers, treasury bills, Government securities, call Deposits, certificate of deposit, and any other like instruments as specified by the Central Bank of Kenya from time to time;
 - b) **Equity Fund:** The fund shall invest a minimum of 80% of the market value of its asset under management in equities listed locally, listed in other regulated exchanges and unlisted equities. Any funds not invested in equities shall be invested in cash and cash equivalents;
 - c) **Fixed Income Fund:** The fund shall invest a minimum of 80% of the market value of its asset under management in fixed income securities at all times. Any funds not invested in fixed income instruments shall be invested in cash and cash equivalents;
 - d) **Balanced Fund:** The fund shall invest in all eligible asset classes provided that investments in money market, equities and fixed income instruments shall each have a maximum exposure of 60% of the market value of assets under management. The maximum investment in any other asset class shall be in compliance with the limits provided under Regulation 78 of the Capital Market (Collective Investment) regulation, 2001;

e) **Special Funds-** these shall be based on the fund managers' investment strategy which shall be clearly described in the information memorandum as approved by the Authority on a case by case basis.

- 2.7 **Naming of the funds-** The fund manager shall ensure that except for special funds, every fund name includes the specific generic name relevant to the fund. For special funds, the name shall at best describe the characteristics of the constituent assets of the fund;
- 2.8 The fund manager of a CIS shall provide the approved trust deeds, information memorandum and a list of all the funds offered including a summary of the description of each fund on its website and any other relevant medium that is accessible to current and prospective investors; and
- 2.9 The firm shall disclose the current fee schedule to current and prospective investors including all performance-based fees and expenses.

3. CIS Performance Reporting

- 3.1 In addition to the existing reporting obligations, the fund manager shall prepare and submit to the Authority a performance measurement report at least quarterly. This report shall be submitted within twenty-one (21) days after the end of each quarter and shall be made available to all existing and prospective clients;
- 3.2 The performance measurement report shall include updated performance and performance related information (on general areas of investment for the selected fund) including correction of material errors if any;
- 3.3 The fund manager of a CIS shall calculate and present time-weighted returns for each fund;
- 3.4 The fund manager of a CIS shall not link actual performance to historical theoretical performance;
- 3.5 The fund manager of a CIS shall not present performance or performance-related information that is false or misleading;
- 3.6 The fund manager shall present total returns according to at least one-, three-, and five-year annualized returns through the most recent period;

- 3.7** The fund manager of a CIS shall disclose its historical fees at least for the last 24 months;
- 3.8** The fund manager shall present in each CIS fund performance report:
- a) The CIS returns for each quarterly period;
 - b) When the initial period is less than one year, the return from CIS from the inception date through the end of the quarter;
 - c) The inception date for each fund;
 - d) The return from the last quarterly period end through the termination date, if the fund is terminated.
 - e) The total return for the benchmark for each quarterly period and for all other periods for which fund returns are presented where applicable.
 - f) Total Assets Under Management under the Collective Investment Scheme for each quarterly period end;
- 3.9** The firm shall present the fund expense ratio appropriate to prospective investors. The fund expense ratio shall be computed as, all fund expenses for the period including performance fees divided opening and closing assets under management for the period;
- 3.10** All information in the CIS performance report shall be presented in the same currency;
- 3.11** The firm shall present proprietary assets as a percentage of the CIS fund assets as of each quarter;
- 3.12** For special funds which invest predominantly in real estate, the fund manager shall present CIS fund and benchmark component returns for all periods presented;
- 3.13** The fund manager shall disclose all significant events that would help a prospective investor interpret the CIS performance report. This disclosure shall be included for a minimum of one year and for as long as it is relevant to interpreting the track record; and
- 3.14** The fund manager shall include comparable figures from the immediate previous period.

4. Performance Calculation

4.1 Assets:

- 4.1.1** In the determination of total Assets Under Management, total assets of a CIS shall:
- a) be the aggregate fair value of all assets and the assets shall not be double counted;
 - b) be actual assets managed by the fund manager of the CIS including both fee-paying and non-fee-paying portfolios;
 - c) Include assets where the fund manager has outsourced the management of the assets to another fund manager;

- 4.1.2 CIS performance shall be calculated using only actual assets managed by the firm;
- 4.1.3 Returns for periods of less than one year shall not be annualized;
- 4.1.4 The fund manager shall report returns that are net of all fees charged against the fund which include transaction costs (cost of buying and selling, investment-brokerage fees, taxes, exchange fees) and administrative cost (audit, legal, custodial, trustee, AGM fees, performance-based fees etc). Administrative fees shall be prorated per fund and per period;
- 4.1.5 If the fund manager of a CIS chooses to use a benchmark for risk and return analysis, it shall disclose in the performance report:
 - i. The benchmark description, which shall include the key features of the benchmark or the name of the benchmark for a readily recognized index or other point of reference;
 - ii. The periodicity of the benchmark if benchmark returns are calculated less frequently than monthly.
 - iii. The benchmark used shall be of the same return type, in the same currency and for the same periods for which the returns are presented.
- 4.1.6 The fund manager of a CIS fund shall choose and present an appropriate risk measure such as maximum draw down or qualitative disclosure or any other measure that current and prospective investors are likely to understand. When calculating risk measures:
 - iv. The periodicity of the fund returns, and the benchmark returns shall be the same;
 - v. The risk measure calculation methodology of the fund and the benchmark shall be the same.

5. Fund Accounting

In preparation of financial statements of the fund:

- 5.1 Total returns shall be used, including dividend income, interest income and capital gains.
- 5.2 Assets and liabilities shall be recognized on the trade date and not the settlement date.
- 5.3 Accrual accounting shall be used for fixed-income securities and all other investments that earn interest income. Any accrued income shall be included in the opening and closing portfolio values when performance is calculated.
- 5.4 Management, performance-based and other fees shall be accrued.
- 5.5 Dividend income shall be recognized as of the ex-dividend date.

6. Calculating Returns

- 6.1 When calculating returns for CIS funds using time-weighted method, all assets except those without readily available market prices, shall be valued daily and returns calculated at least monthly.
- 6.2 The fund manager of a CIS shall calculate sub-period returns at the time of all cash flows exceeding 10% of the Assets Under Management.
- 6.3 When calculating returns the fund manager shall geometrically link periodic and sub-period returns.
- 6.4 When calculating returns the fund manager shall consistently apply the calculation methodology used for an individual portfolio.

7. Valuation

- 7.1 Portfolios shall be valued daily and in accordance with the definition of fair value as set out in IFRS 13.
- 7.2 If the firm uses the last available historical price or preliminary estimated value as fair value, the firm shall:
 - i. Consider it to be the best approximation of the current fair value.
 - ii. Assess the difference between the approximation and final value and the effect on CIS assets, total firm assets, and performance, and also make any adjustments when the final value is received;
- 7.3 External valuations for real estate investments shall be performed by an independent registered property valuer.

8. Advertisement Guidelines

- 8.1 For purposes of Regulation 81 of the Capital Markets CIS Regulations, an advertisement includes any materials that are distributed to or designed for use in newspapers, magazines, firm brochures, CIS fund fact sheets, CIS fund offering documents, letters, media, websites, or any other written or electronic material distributed to more than one party.
- 8.2 For all publications, the fund manager must include at a minimum Net Asset Value (NAV), Yield (Year-to-date, Month-to-date and Quarter-to-date) where applicable.
- 8.3 The fund manager shall adhere to the principles of fair presentation and full disclosure when advertising and shall not present performance or performance-related information that is false or misleading.
- 8.4 The fund manager shall maintain all data and information necessary to support all items included in the advertisement. Where a firm has summarized aspects of the performance reports in the advertisement, it shall disclose how to obtain the full performance report.
- 8.5 In an advertisement(s) the firm shall clearly label or identify:
 - a) the name and description of the fund(s)
 - b) the name of the benchmark used, where applicable, which shall include the key features of the benchmark or the name of the benchmark for a readily recognized index or other point of reference and;
 - c) the periods that are presented.
- 8.6 All information in an advertisement shall be presented in the same currency.
- 8.7 The firm shall present total returns according to at least one-, three-, and five-year annualized returns through the most recent period.
- 8.8 The fund manager shall disclose the current expense ratio and which fees, including performance-based fees and expenses are included in the expense ratio.
- 8.9 The fund manager shall disclose the risk measures or qualitative disclosure that a prospective investor is likely to understand.
- 8.10 The fund manager shall disclose the CIS fund's sales charges and loads and how they are reflected in the CIS fund's returns, if applicable.

