



Principles for the valuation of Collective Investment Schemes (CIS). July 2013.

The Board of the IOSCO published, the 3rd of May, the final report on principles for the valuation of Collective Investment Schemes (forward CIS). This report, drafted by Committee on Investment Management (C 5), contains a list of principles intended to serve as a basis for both industry practitioners and regulators to assess the quality of regulation and industry practices regarding the valuation of CIS.

Principles for CIS valuation described in the report have taken into account the feedback to the previous consultation paper (February 2012) and update the IOSCO Principles originally developed in 1999 to adapt them to regulatory, industry and market developments. The report also takes in consideration the IOSCO Principles for the valuation of Hedge Fund Portfolios issued in 2007, the Examination of Governance for CIS published in 2005 and other relevant reports elaborated more recently.

Many complex and hard-to-value assets are now eligible for CIS portfolios including some that did not exist a decade ago. The value of such assets cannot be determined by using quoted prices (so-called mark-to-market) but instead CIS may rely on internal techniques which imply managements' judgement (so-called mark-to-model). The difficulty and subjectivity needed for certain valuations increases regulatory risks and calls for a set of principles of guide the identification of policies and procedures designed to ascertain the proper valuation of CIS assets.

The implementation of comprehensive policies and procedures for the valuation of CIS assets is a fundamental principle underpinning investment management. It is critical that a CIS properly value all assets in its portfolio, including those instruments for which market quotations are not readily available. CIS valuations are extremely important because if portfolio securities and assets are incorrectly valued, on one side, investors may unfairly end up paying more for their shares or receive less upon redemption and, on the other, remaining investor also may be adversely affected.

The principles do not provide directly applicable standards for firms and have to be implemented in every local regulatory framework but aim to reflect a level of common approach and to be a practical guide for regulatory and industry practitioners.

The principles are addressed to the entity responsible for the overall operation of the CIS and for its compliance with the legal and regulatory framework in the respective jurisdiction. The entity responsible, in some jurisdictions, could be the management company (or the management company overseen by the Board of Director) and, in others, the CIS itself.

Principle 1: The responsible entity should establish comprehensive, documented policies and procedures to govern the valuation of assets held or employed by a CIS. The portfolio manager may be heavily involved in formulating the policies and procedures while the responsible should seek to ensure integrity in the valuation process.

Principle 2: The policies and procedures should identify the methodologies that will be used for valuing each

type of asset held or employed by the CIS. Where possible, assets should be valued according to current market prices, providing that those prices are available, reliable, and frequently updated, but if the assets have not been traded frequently, are complex or illiquid (hard-to-value assets), appropriate internal valuation techniques are needed as well as staff with suitable level of knowledge and experience for the proper application of those techniques. Portfolio manager should monitor the liquidity in markets which the CIS is invested as part of a liquidity management policy; the more illiquid such markets are, the more robust the valuation process may need to be. The policies and procedures could consider valuation practices in normal and stressed market conditions. When taking into account the opinion of a third party, the responsible entity should consider whether the opinion is suitable.

Principle 3: The valuation policies and procedures should seek to address conflicts of interest. The most common conflict of interest occurs when the CIS operator that values the assets is, at the same time, the most reliable or only source of information about pricing for a particular asset because its fees are calculated based on the CIS's assets under management. Conflicts of interest can be addressed in a number of ways in order to obtain independent valuations performed by the CIS operator (internal auditor or committee revisions) or by the Depository or other third party.

Principle 4: The assets held or employed by CIS should be consistently valued according to the policies and procedures. The policies should generally be consistent across similar types of assets and across all CIS that have the same CIS operator. If, in certain exceptional circumstances, the value of an asset calculated with the original methodology may not be appropriate (for example, when does not result in the fair treatment of investors) the policies and procedures should describe a different methodology in which the price override (deviation) is reasoned and revised by a third party.

Principle 5: A responsible entity should have policies and procedures in place that seek to detect, prevent, and correct pricing errors. Pricing errors that result in a material harm to CIS investors should be addressed promptly, and investors fully compensated.

Principle 6: The responsible entity should provide for the periodic review of the valuation policies and procedures to seek to ensure their continued appropriateness and effective implementation. A third party should review the CIS valuation process at least annually.

Principle 7: The responsible entity should conduct initial and periodic due diligence on third parties that are appointed to perform valuation services. Third parties, for example valuation agents, must have appropriate system, controls and valuation policies and procedures as well as sufficient personnel with an appropriate level of knowledge and experience. The responsible entity retains responsibility and liability for the valuations of the CIS's assets.

Principle 8: The responsible entity should seek to ensure that arrangements in place for the valuation of the assets in the CIS's portfolio are disclosed appropriately to investors in the CIS offering documents or otherwise made transparent to investors. Disclosure could include information about how assets are valued and how frequently they are valued and should be updated in case of material changes.

Principle 9: The purchase and redemption of CIS interests generally should not be effected at historic Net Asset Value (NAV). The recommended practice is to purchase and redeem at the next computed NAV after the receipt of the order, so that investors will not know the NAV per share at the time of placing the order and all investor orders will be treated the same if the orders are received by the cut-off time in good order.

Principle 10: A CIS's portfolio should be valued on any day that CIS units are purchased or redeemed.

Principle 11: A CIS's NAV should be available to investors at no fee. The price of a CIS is generally available on a daily basis in financial publications and websites and may also be available on the CIS's or CIS operator's

website.

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