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Comment letters on Proposed Statement of Position, Amendment to Scope of Statement of Position 95-2, Financial Reporting by Nonpublic Investment Partnerships, to include commodity pools

American Institute of Certified Public Accountants. Accounting Standards Executive Committee

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INTERNAL MEMORANDUM

Date: December 5, 2000
To: Pat Meyer, Library
From: Dan Noll, Accounting Standards *DV*
Subject: Comment Letters for public record

Enclosed are four comment letters received in response to the exposure draft of the Proposed Statement of Position, Amendment to Scope of Statement of Position 95-2, *Financial Reporting by Nonpublic Investment Partnerships*, to Include Commodity Pools.

Please retain the letters as part of the public record for one year.

Enclosures

**List of Respondents to
AcSEC's Proposed Statement of Position, Amendment to Scope of
Statement of Position 95-2, *Financial Reporting by Nonpublic Investment
Partnerships*, to Include Commodity Pools**

| <u>Letter Number</u> | <u>Respondent</u> | <u>Affiliation</u> |
|---------------------------------|---|---------------------------|
| 1 | Ernst & Young LLP | Big 5 |
| 2 | Blackstone Alternative Asset Management L. P. | Industry |
| 3 | Deloitte & Touche LLP | Big 5 |
| 4 | Managed Funds Association | Industry Association |



September 7, 2000

Mr. Daniel Noll
Technical Manager
Accounting Standards
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

Proposed Statement of Position
“Amendment to Scope of Statement of Position 95-2, *Financial Reporting by*
Nonpublic Investment Partnerships, to Include Commodity Pools”
(File No. 3170.AM)

Dear Mr. Noll:

We agree that commodity pools subject to regulation under the Commodity Exchange Act of 1974 should be required to show financial statements in accordance with Statement of Position (“SOP”) 95-2. These entities were previously excluded from the scope of SOP 95-2 because a separate Audit and Accounting Guide for commodity pools was to be issued. The planned Audit and Accounting Guide became instead a non-authoritative practice aid, *Audits of Futures Commission Merchants, Introducing Brokers, and Commodity Pools*.

Because there is no current authoritative guidance related to commodity pools regulated under the Commodity Exchange Act of 1974, it is reasonable to require these entities to follow the accounting requirements of other entities, the only notable difference in their operations being the status of registration under the Commodity Exchange Act of 1974. As such, we support the issuance of this amendment to the scope of SOP 95-2.

* * * * *

We would be pleased to discuss our letter with AcSEC or the AICPA staff at your convenience.

Very truly yours,

A handwritten signature in cursive script that reads "Ernst & Young LLP".

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Blackstone Alternative Asset Management L.P.

The Blackstone Group Inc., *General Partner*

Fedex

November 2, 2000

Mr. Daniel Noll
Accounting Standards, File 3170.AM
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Mr. Noll:

Blackstone Alternative Asset Management L.P. ("BAAM") sponsors a group of private "fund of funds" (the "Blackstone Funds") that invest in a broad spectrum of hedge funds (the "Investments"), which are also CFTC registrants. The investors in the Blackstone Funds are sophisticated investors and/or qualified purchasers, (e.g., 3(c)1 and 3(c)7 investors), collectively, "Sophisticated Investors". This letter will serve as a commentary to the Exposure Draft for the Proposed Statement of Position Amendment to Scope of Statement of Position 95-2 (SOP 95-2), *Financial Reporting by Nonpublic Investment Partnerships to Commodity Pools*, dated August 15, 2000 (the "Proposed SOP"). Generally, we strongly believe the Proposed SOP and/or SOP 95-2 should be modified for all private "fund of funds", i.e., 3(c)1 and 3(c)7 type investment vehicles.

The Blackstone Funds use proprietary allocation models to blend different investment strategies to achieve a unique investment objective for each fund. Blackstone's investment strategies have been disclosed to our investors in the offering documents and partnership agreements prior to their decision to invest in the fund.

We are able to offer our Sophisticated Investors an attractive, compelling investment choice due in large part, to our proprietary allocation models and the keen knowledge of the financial markets possessed by our investment professionals. Consequently, in order for Blackstone to protect these valuable assets, we strongly believe that it is imperative that we continue to maintain confidential the names of our underlying hedge fund managers and their related allocations.

Our Sophisticated Investors decide to invest with Blackstone after performing their own extensive due diligence on our firm and portfolio managers. On an ongoing basis, we maintain a continuing dialogue with these investors including responding to their questions relating to their individual investments in the Blackstone Funds and/or the funds' investments, their current strategies, etc.

345 Park Avenue
New York, NY 10154
212 583-5000

Blackstone Financial ServicesSM

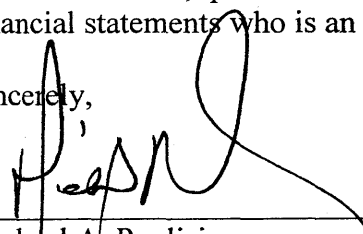
2 cont'd

In the past, due to the exclusion for CFTC registrants set forth in SOP 95-2, the Blackstone Funds have not been required to (per the AICPA Audit Guide) and have not elected to, disclose a detailed schedule of Investments (e.g., with the name of each of the underlying funds) within their annual audited financial statements. However, within the footnotes to the financial statements, each Blackstone Fund discloses detailed information about the underlying funds (such as liquidity features by strategy, cost and fair value of the investments within each investment strategy and incentive and performance fees by strategy). We strongly believe that the specific name of the underlying funds can be kept confidential provided that these additional disclosures, particularly strategies for all significant underlying funds (e.g. of greater than 5 or 10% of net assets) are disclosed in the footnotes and provided to investors. This view is consistent with the approach that we take for the internal communications with our Sophisticated Investors.

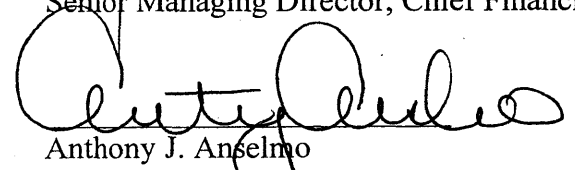
As you are aware, the Proposed SOP removes the "exclusion" from SOP 95-2 for investment funds that are CFTC registrants. If approved, the Proposed Statement of Position will require the Blackstone Funds to include a detailed schedule of investments (including the name, cost and fair value of the "underlying funds" which represent greater than 5% of the net assets of each fund) within the audited financial statements.

Instead, we believe that providing detailed information which outlines the objective, strategy and type of security, not the names of the underlying investments (and/or underlying funds in the case of "fund of funds") should be, and in fact to date has been, sufficient detail for the Sophisticated Investors in the Blackstone Funds. Furthermore, we strongly believe that the aforementioned disclosure, which has been accepted by the CFTC and our investors, each of whom must be a Sophisticated Investor in order to invest in Blackstone (or other 3(c)1 and 3(c)7 "fund of funds", provides more appropriate and relevant information to the reader of the financial statements who is an investor in these type funds.

Sincerely,



Michael A. Puglisi
Senior Managing Director, Chief Financial Officer



Anthony J. Anselmo
Vice President and Contoller

345 Park Avenue
New York, NY 10154
212 583-5000

Blackstone Financial ServicesSM

7en Westport Road
P.O. Box 820
Wilton, Connecticut 06897-0820

Tel: (203) 761 3000
www.us.deloitte.com

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**Deloitte
& Touche**

November 15, 2000

Mr. Daniel Noll
Technical Manager
American Institute of Certified Public Accountants
1211 Avenue of the Americas, New York, NY 10036-8775

File Reference No. 3170.AM

Amendment to Scope of Statement of Position 95-2, Financial Reporting by Nonpublic Investment Partnerships, to Include Commodity Pools

Dear Mr. Noll:

Enclosed is our letter of comment on AcSEC's Proposed Statement of Position, *Amendment to Scope of Statement of Position 95-2, Financial Reporting by Nonpublic Investment Partnerships, to Include Commodity Pools.*

If you have any questions regarding our response, please contact John T. Smith at (203) 761-3199.

Yours truly,



Enclosure

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November 15, 2000

Mr. Daniel Noll
Technical Manager
American Institute of Certified Public Accountants
1211 Avenue of the Americas, New York, NY 10036-8775

File Reference No. 3170.AM

Amendment to Scope of Statement of Position 95-2, Financial Reporting by Nonpublic Investment Partnerships, to Include Commodity Pools

Dear Mr. Noll:

We are pleased to comment on AcSEC's Proposed Statement of Position, *Amendment to Scope of Statement of Position 95-2, Financial Reporting by Nonpublic Investment Partnerships, to Include Commodity Pools*, (the "Exposure Draft"). We support the issuance of the Exposure Draft as a final Statement of Position.

We believe that the accounting for commodity pools should provide adequate transparency and comparability of financial statement disclosures. We acknowledge that the accounting for commodity pools is currently scoped out of the current guidance of SOP 95-2. As such, it is possible that two commodity pools with similar operations and investment portfolios may have different disclosures in the financial statements if one is subject to Commodity Futures Trading Commission ("CFTC") regulations and the other is not.

Although some may argue that the requirement to provide a condensed schedule of investments may not be meaningful due to the frequent turnover of most commodity portfolios, we believe that there should be consistency in the accounting treatment and financial statement disclosures among similar-type investment vehicles. The presentation of condensed schedules of investments by commodity pools will assist financial statement users in better assessing such pools.

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American Institute of Certified Public Accountants
November 15, 2000
Page 2

However, the Exposure Draft could be improved by providing more specific guidance regarding the appropriate disclosures for holdings in commodity futures and forward contracts and whether a commodity pool should disclose each individual contract or contracts by some other grouping. Furthermore, as discussed in SOP 95-2, paragraph 10, investment partnerships that are exempt from registration under the Investment Company Act of 1940, are only required to present a condensed schedule of investments disclosing each investment that constitutes more than five percent of net assets. It would appear that the likelihood of any individual commodity futures or forward contract constituting more than five percent of net assets would be remote.

If you have any questions regarding our response, please contact John T. Smith at (203) 761-3199.

Yours truly,

Deloitte & Touche



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MANAGED FUNDS ASSOCIATION

November 15, 2000

*The Association for investment
professionals in futures, hedge funds
and other alternative investments.*

American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775
Attn: Daniel Knoll, Technical Manager, Accounting Standards

Re: Statement of Position 95-2, File 3170.AM.

Dear Mr. Knoll:

Managed Funds Association (the "MFA") appreciates the opportunity to provide comments in response to the American Institute of Certified Public Accountants' Exposure Draft related to Statement of Position 95-2 (the "Exposure Draft") which was released on August 15, 2000.

MFA is a national trade association of more than 700 members, representing a diverse group of alternative investment professionals, including hedge fund and commodity trading managers, commodity pool operators, and fund-of-funds managers as well as major end-users of the futures markets. MFA generally supports initiatives that are intended to treat all similarly situated market participants equally.

MFA, however, does not agree that the Exposure Draft is merely correcting an exemption that exists solely as a result of oversight. MFA believes that there are fundamental differences between the capital markets and the futures and other speculative markets that merited the carve-out in 1995 and continue to warrant consideration today. MFA continues to believe that the investment strategies of managers in these markets are proprietary and that its confidentiality should be respected. We further believe that it is in the best interest of the investors in these products that such confidentiality be maintained.

To put it simply, compliance with the Exposure Draft may do more harm than good. By failing to consider these inherent differences, compliance with the Exposure Draft will permit other market participants to "piggyback", or even worse, trade against the positions of large commodity pools in the futures and derivative markets. This potentially will exacerbate overall market volatility or liquidity concerns during difficult periods.

Similarly, we are concerned with the application of the Exposure Draft to managers operating investment vehicles commonly referred to as “fund-of-funds”. A fund-of-funds is an investment vehicle that purchases interests in other pooled vehicles rather than directly purchasing securities or other instruments. A fund-of-funds manager’s sole asset is its selection process and relationship with underlying fund managers – which often allows it to negotiate better terms than such managers offer to the public. Because the SOP includes investments in other pooled vehicles as “investments” requiring disclosure, compliance with the Exposure Draft will require these managers to virtually “give away” the work product of their proprietary business activities.

Finally, we are concerned that the Exposure Draft will not result in a level playing field, but in fact, cause greater disparity in financial reporting. Already, a number of hedge fund managers are willing to take qualified opinions from their auditors. Managers who object to complying with the exposure draft may be further motivated to take their business outside the United States or to not prepare their financial statements in accordance with US generally accepted accounting principles.

Also, managers desiring greater secrecy may utilize swaps or other creative financial instruments to gain exposure to certain investments, yet keep the value of such investments below five percent of the net assets of the pool. For example, a pool investing 5% of its assets in an instrument must disclose that instrument on its financials. But another pool may use a swap to gain the same level of exposure (i.e., the same “notional amount”) yet will have no reporting obligation unless the swap has either an unrealized profit or loss equal to or greater than 5% of its net assets. Furthermore, even if the profit or loss is greater than 5%, the manager can avoid disclosure by merely settling the swap on December 31 (or such other date that is the last day of the pool’s fiscal year). The end result, therefore, could be less disclosure rather than more, and certainly the disclosure across market participants will be inconsistent.

MFA would like to suggest three possible amendments to the Exposure Draft:

1. Limit the specific disclosure of positions to publicly traded equities. As already noted, we believe the fundamental differences in the markets warrant having different levels of disclosure.
2. Provide alternative meaningful disclosure for all “other” greater than 5% investments. For example, in the fund-of-funds context, a pool could provide information on the size of each investment, the gross fees paid, net profit or loss, a description of the trading strategy and liquidity terms but withhold the name of the fund. A number of our members have confirmed that the Commodity Futures Trading Commission (“CFTC”) has accepted this information in lieu of the name of the fund in statements filed with the CFTC.
3. Also in the fund-of-funds context, increase the percentage for required disclosure from 5% to 10%. This would conform the disclosure with the CFTC recommendation on material disclosure for investments representing greater than 10% of the reporting pool’s assets. See, for example, the CFTC’s letter to all Commodity Pool Operators dated January 19, 2000.

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MFA urges the AICPA to reconsider the Exposure Draft and the comments noted above. MFA would be happy to clarify any of the issues that are raised in this comment letter. Please feel free to contact me at (202) 367-1140.

Sincerely yours,

Patrick J. McCarty

Patrick J. McCarty
General Counsel