

GIPS Standards and Key Questions

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WHAT ARE THE GIPS STANDARDS?

GIPS® is the acronym for the Global Investment Performance Standards. The GIPS standards focus on calculating and presenting investment performance. They aim to promote the highest standards of ethical principles of fair presentation and full disclosure of investment performance. The goal of the GIPS Executive Committee is to have all firms adopt the GIPS standards as the global standard for investment firms to present historical investment performance information.

The standards are sponsored by the CFA Institute, and are created and developed through the collaboration of the global investment community. They are maintained by the GIPS Executive Committee, a nine-member governing body, and are periodically reviewed and updated. Visit www.gipsstandards.org for more information and to sign up for the GIPS newsletter to be kept up to date.

The GIPS standards are voluntary. Any investment firm, and subsidiary or division of an investment firm that is held out to clients or potential clients as a distinct business entity, may apply to comply with the GIPS standards. The comprehensive requirements govern input data, calculation methodology, composite construction, disclosures, presentation and reporting. A composite is an aggregation of one or more portfolios managed according to a similar investment mandate, objective, or strategy.

Compliance with GIPS is claimed by a firm when the standards have been successfully applied on a firm-wide basis and performance is presented in terms of composites in a specific disclosure and presentation format.

BENEFITS OF THE GIPS STANDARDS

- Enhanced ability to **compare performance** between firms and strategies. Therefore, firms of different sizes and from different geographical regions are able to present their investment performance on a comparable basis.
- **Consistency** in calculation and presentation of performance results, such as frequency of valuation, treatment of large cash flows and handling of accruals. This provides assurance that the same principles for calculating and presenting performance are being followed across firms and strategies.
- **Transparency** in providing full disclosure of important details on presented performance data, such as fees, composite construction criteria, dispersion of returns, etc.
- Firms implementing the GIPS standards are recognized for adherence to **industry best practice**.
- Adherence to GIPS brings strengthened internal processes and controls, and improved risk management.

We address several key questions about GIPS often voiced by the investment community:

KEY QUESTIONS

Can we claim partial compliance with the GIPS standards?

No. The firm needs to comply with all the GIPS standards on a firm-wide basis. A firm is defined under the GIPS standards as an investment firm or subsidiary or division of an investment firm that is held out to clients or potential clients as a distinct business entity and manages assets in a discretionary manner. The firm definition delineates the universe of “all” portfolios that must be included in total firm assets. Compliance with selected requirements of the standards or for some selected funds managed by the firm leaving out other funds or products managed by the firm does not constitute compliance with GIPS.

The firm may be defined in such a way as to include only a distinct market or client type if they constitute a distinct business entity or if a separate and distinct investment process is used for such a specific market or client type. For example, the asset management division for institutional investors may be defined as a GIPS firm not covering other divisions or client segments of the organization, such as retail or private investors. However, the GIPS standards recommend that a firm adopt the broadest and most meaningful definition of the firm including all geographical offices operating under the same brand name.

Can a fund or portfolio or composite be GIPS compliant?

No. It is important to note that if the firm claims compliance with the GIPS standards then it needs to comply with all the GIPS standards on a firm wide basis. Therefore, funds or portfolios or composites cannot be GIPS compliant on their own. [A composite is an aggregation of one or more portfolios managed according to a similar investment mandate, objective, or strategy.]

To meet the highest ethical standards the firm is required to establish policies and procedures that are designed to calculate and present performance in a way that complies with the GIPS standards. Note that the emphasis is on policies and procedures designed to calculate and present performance, and not on the performance calculation of the actual fund or portfolio or composite.

Can calculation methods claim GIPS compliance?

No. Statements referring to the performance of a single fund or account as being “calculated in accordance with GIPS” are not permitted except when a GIPS compliant firm reports the performance of an individual account to the existing client. Compliance with GIPS involves more than just the use of a calculation methodology; therefore it is more appropriate to ask: Does your firm claim compliance with GIPS?

Who cannot claim compliance with the GIPS standards?

Only a firm that manages assets in a discretionary way, as defined by the GIPS standards, can be compliant. Software firms, for example, may not be GIPS compliant. Portfolio management software cannot be GIPS compliant, but can assist an asset management firm to implement the GIPS requirements in terms of performance calculation, portfolio to composite allocation, reporting and their relevant processes etc.

Third-party performance measurers and custodians who do not manage actual assets cannot claim compliance either but may facilitate an investment management firm’s claim of compliance.

Plan sponsors which do not manage their assets themselves may require that third-party investment management firms of their assets comply with the GIPS standards.

What is verification?

The GIPS standards recommend firms to be verified. Verification brings additional credibility to a firm's claim of compliance and is performed by an independent third-party that assesses the construction of the firm's composites as well as the firm's policies and procedures as they relate to compliance with the GIPS standards.

Note that verification examines the firm's compliance with the GIPS standards, and not the performance of a specific fund, portfolio or composite. However, in addition to a firm-wide verification a firm may choose to have a detailed performance examination of a specific composite. It is not appropriate, without a firm wide verification, to perform a performance examination only.