

## **Input on Selected Four Key Sections of GIPS 2010 From the Investment Manager Subcommittee**

### **Scope of Verification**

The Subcommittee recognizes that verification is not a guarantee but it also acknowledges that third party verification provides clients with added sense of confidence in the FIRM's claim of compliance. Members feels the softening of the language with words such as "intended" and "helps to" diminishes the importance of verification and asks the GIPS Executive Committee to take a more affirmative stand. Additionally, Members ask for guidance on the definition of qualified as well as clarification on what verification is and is not.

Specific comments and suggestions on Section III: Verification are listed below:

Introduction Recommend revising the opening paragraph to: The primary purpose of VERIFICATION is to give both the FIRM and its existing and PROSPECTIVE CLIENTS added confidence in the FIRM's claim of compliance. This is done by having a qualified independent third-party review the FIRM's internal processes and procedures and ensure compliance to the GIPS standards on a FIRM-wide basis. VERIFICATION gives added assurance to (and often increases) the consistency and quality of the FIRM's COMPLIANT PRESENTATIONS and also reviews key internal processes and procedures that the presentation relies upon.

A.2 Recommend replacing the phrase "is intended to determine" with the word "assesses" to read: VERIFICATION assesses whether: follow by a) and b).

A.4 Suggest revising the sentence to read: VERIFICATION brings additional, independent credibility to the claim of compliance and supports the overall guiding principles of full disclosure and fair representation of a FIRM's investment performance. This is consistent with the GIPS EC support for verification as best practice.

A.7 Request further elaboration on how reliance would work as the current proposal is confusing. For example, guidance is needed on 'professional skepticism' to give better examples of where issues from current verification might highlight concerns over previous periods performed by another independent third party.

A.8 This section on sample account selection was originally part of the required 8 verification procedures (III.B.2.d in Second Edition). The Subcommittee questions the significance of emphasis here in the scope section and wonders if this undermines the other aspects of the verification procedures in section III.B Required GIPS Verification Procedures.

B.1.d. Concur with the added language that the verifier must ensure that all applicable policies and procedures are properly included and adequately documented. However,

the itemized list i-xiv in the original version helps to identify minimum documentation.

B.1.e. Similar to B.1.d, the itemization is not an exhaustive list and highlights the consistency of FIRM's policies to the GIPS standards. The removal of sub-bullets i-v (*which are not reflected in the tracked changes version*) precludes verifiers from determining if the methodologies are appropriate and from confirming the policies and procedures are consistent with the Standards

B.2.d. The original sample account selection was scoped out (*deletion not reflected in the tracked changes version*) and included in A.8 above.

B.2.f. Verification provides more assurance that returns are correctly calculated and presented than non-verification! Recommend replacing the phrase "does not provide assurance" with "does not guarantee" so that the sentence reads: Recognizing that VERIFICATION does not guarantee that specific COMPOSITE returns are correctly calculated and presented...etc.

### **Claim of Compliance Statement**

Members concur with the recommendation for verification with explicit disclosure of whether or not the firm has been verified in the compliance statement. However, the majority of the Subcommittee advocates for *only* two claims of compliance statements – either a firm is or is not verified - and the reader can judge how current the verification is based on the periods disclosed. The declaration of compliance will comprise of two parts:

1. Firm's claim of compliance with the Global Investment Performance Standard and that it has prepared and presented this report in compliance with the GIPS standards; *AND*
2. Firm's verification status:
  - a) If verified, firm declares that it has been independently verified for the specified interval and the availability of verification report upon request
  - b) If not verified, firm discloses that it has not been independently verified

The statement that refers to non-current verification status may potentially have negative connotation associated with it. First, firms coming into compliance may *only* have an initial verification which ensures proper process and procedures are established for compliancy on the firm-wide basis and for the part of the track record that the firm claims compliance. Firms may NOT have additional validations in the immediate and/or subsequent years. Second, boutique firms may be disadvantaged as a result of leaner staffs and tighter financial constraint compared to major conglomerates with adequate resources and financial capability to secure more

frequent verifications. Efficiency of the firm should not be the determining factor of 'staleness'. Third, the acceptability of time lag between verification is dependent on the market. It may be common practice to have the last annual calendar year verified to be considered current in the developed country whereas the process may be longer in emerging countries. The concept of current is subjective.

In addition, members recommend developing a Q&A to specifically address situation where the firm could not make the full verification status statement (e.g. including the timeframe). A consultant database is an example of such where the firm is being asked a simple "yes" or "no" questionnaire without an option to clarify when the verification took place. Verification become stale at some point and the firm should not be able to say that it has been verified. Clarification on the definite period of time after which a firm could not claim it was verified because of a past stale verification should be addressed – 24 months appears a sensible length of time, although it should be clarified from what point this starts.

### **Fair Value**

The Subcommittee acknowledges that fair value is the concept towards which the global accounting markets are moving and proposes fair value as a recommendation (i.e. not a requirement). International Accounting Standards Board, the Financial Accounting Standards (FASB), as well as many local accounting organizations and regulatory agencies are providing guidance on how to value assets. The complexity of fair value and interpretation of valuation hierarchy should remain with these experts rather than being prescribed in the performance standards. Members are concerned about getting into the situation of the Executive Committee is constantly rewriting the Standards as accounting standards change. Members recommend the removal of Appendix D on GIPS valuation principles (or that it be re-written at higher principal-based level) with reference to the local laws, regulation and accounting standard best practices.

### **Risk Disclosures**

The Subcommittee agrees conceptually with the inclusion of a Risk Disclosure in the Standards. Members recognize that the Risk Working Group is working on the Guidance Statement to clarify the application of risk. Members could not fully support or be against sufficient risk measure without examples of qualitative risk disclosure and quantitative risk presentation. Most are comfortable with the required Standard Deviation and the flexibility to show additional measures appropriate to the strategy. In addition to comparability between managers of similar strategies from the standard deviation disclosure, a rolling measure of the fund and the benchmark provides a more information of how it has changed over time in line with performance records.