



Global Investment Performance Standards

EXPOSURE DRAFT OF GIPS® GUIDANCE STATEMENT ON VERIFIER INDEPENDENCE

Effective Date: 7/1/2018

Retroactive Application: Not Required

Public Comment Period: 7/28/2017–10/26/2017

GUIDANCE STATEMENT ON VERIFIER INDEPENDENCE

Executive Summary

The purpose of revising the GIPS® Guidance Statement on Verifier Independence is to clarify as well as strengthen existing independence guidance that was issued in 2005.

For example, the proposed guidance would require that the verification firm create and document its own policies and procedures that address independence at both the verification firm and the employee level. The verifier would also be required to provide to the firm upon request, a summary of its independence policies.

The proposed revised guidance indicates that both the verifier and the firm must each assess independence. The assessment must be performed prior to the commencement of each verification engagement and affirmed by both the verifier and the firm at the conclusion of the engagement, as evidenced by the issuance of the verification report and the representation letter, respectively. A reassessment must be made whenever any new information comes to light during or after the engagement that could affect independence.

The verifier and the firm must discuss with each other identified issues that could potentially impact independence (potential independence issues) as they arise. The verifier and the firm must determine whether potential independence issues can be resolved such that independence is achieved. The verifier and the firm must each document the conclusions reached and the rationale for their conclusions.

The proposed guidance also indicates that the verifier must adhere to any independence guidance for its profession, if applicable.

Invitation to Comment

Exposure Draft of the Guidance Statement on Verifier Independence

CFA Institute established the GIPS Executive Committee as the governing body for the Global Investment Performance Standards (GIPS). The GIPS Technical Committee, responsible for technical oversight of the GIPS standards, seeks comment on the proposal set forth here regarding the Guidance Statement on Verifier Independence.

Two questions are included in this document to obtain feedback on specific issues. In addition to responding to these questions, please provide feedback on the entire document, including items you support. All comment letters will be considered and are greatly appreciated.

Comments must be submitted and received no later than 26 October 2017. Responses will be accepted by email, hard copy, and fax. Please submit your comments as early as possible to facilitate the review process. Unless you request otherwise, all comments and replies will be made public on the GIPS standards website (www.gipsstandards.org). Comments may be submitted as follows:

Email: standards@cfainstitute.org

Fax: +1 (434) 951-5687

Post:

CFA Institute
Global Investment Performance Standards
Re: Guidance Statement on Verifier Independence
915 East High Street
Charlottesville, VA 22902
USA

Introduction

Verification is a process by which a verification firm (verifier) assesses whether the firm (firm) has complied with all the composite construction requirements of the Global Investment Performance Standards (GIPS) on a firm-wide basis and whether the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. Verification must be performed by an independent third party. For the verifier to be an "independent third party," there must be no independence issues between the verifier and the firm. Independence issues must be resolved for the verifier to be independent. If the independence issue is not resolved, the verifier is not independent. The purpose of this Guidance Statement is to guide firms and their potential or current verifiers in the process of determining whether independence issues exist between them.

The firm has the ultimate responsibility for appointing a qualified verifier. The GIPS standards require independence as part of a verifier's qualification requirements. Verifier qualification requirements are discussed in the Guidance Statement on Verification. The self-regulatory nature of the GIPS standards necessitates a strong commitment to ethical integrity on the part of the firm as well as the verifier.

This guidance also applies to performance examinations, if conducted. The term "verification report" as used in this document refers to both the firm-wide verification report and the performance examination report(s), if applicable. For further information on performance examinations, please see the Guidance Statement on Performance Examinations.

This Guidance Statement serves as minimum guidance. The verifier must also adhere to any applicable professional independence guidance. If any conflicts exist between this guidance and the verifier's professional independence guidance, the verifier must adhere to whichever guidance is more restrictive.

Defining Independence

Defining the term "independence" is not a simple process. Crucial to the verification process is the assumption by all interested parties that the verifier performs its service in an unbiased manner and is not testing its own work.

When considering a verification engagement, the firm and the verifier must determine any independence issues existing between the two organizations. The verifier must create and document its own policies and procedures that address independence at both the verification firm and employee level. At a minimum, the verifier must provide to the firm, upon request, a summary of its independence policies. The firm should create and document its own policies and procedures that address independence. The firm should consider drawing on the resources from its own GIPS oversight committee, if one exists.

If the firm is contemplating hiring a verifier that offers additional products and services that the firm could or does use, the firm must understand how the verifier maintains independence from the firm.

During the process of determining whether any independence issues exist, both the firm and the verifier must be cognizant of actual as well as perceived independence issues. When considering verifier independence, each organization must keep in mind the following question: *If a prospective client of the firm places reliance on the fact that the firm has been verified, could the prospective client's perception of the value of the verification potentially be changed if the prospective client knew about other existing relationships between the firm and the verifier?*

For verifiers that provide services in addition to verification services, it may prove difficult for the verifier to identify other services provided by the verifier's organization. For example, a verifier may serve in an advisory role in a corporate acquisition/sale, which would not be disclosed to the verifier's or firm's employees involved with the verification engagement. Depending on the nature of the other services

provided to the firm by the verifier, an independence issue may or may not be created. Verifiers must establish policies and procedures to attempt to identify all services provided to a firm so the potential impact on independence may be assessed.

The verifier and the firm must spend as much time as is reasonably necessary for them to, independently and jointly, satisfy themselves that none of the relationships between the two organizations will impair the independence of the verifier.

The verifier and the firm must each assess independence. The independence assessment is not a one-time event; it is an ongoing process. The assessment must be performed prior to the commencement of each verification engagement. The assessment must be affirmed by both the verifier and the firm at the conclusion of the engagement. Additionally, a reassessment must be made whenever any new information comes to light during or after the engagement that could have an impact on independence.

Independence Issues

The verifier and the firm must discuss with each other identified issues that could potentially impact independence ("potential independence issues") as they arise. The verifier and the firm must determine whether potential independence issues can be resolved such that independence is achieved. The verifier and the firm must each document the conclusions reached and the rationale for their conclusions. Disclosure alone does not resolve an independence issue.

It may be helpful for both the verifier and the firm to consider independence as a continuum. At one extreme of the continuum is a verifier with no other relationships with the firm. At the other extreme is a verifier with existing relationships and independence issues with the firm that cannot be resolved, such that the verifier cannot conduct the engagement because independence cannot be achieved. The firm and the verifier must determine where their relationship is on this continuum and whether it is appropriate to proceed with the verification engagement.

When a verifier determines that an independence issue prevents it from continuing to provide verification services to a firm, the verifier must immediately inform the firm of the independence issue. The verifier and the firm must also determine whether the newly discovered independence issue extends to any periods that have been previously verified. If it does, the firm must cease making any claims of verification for the period the independence issue existed and the verifier must rescind any previously issued verification reports covering the affected time period. The firm may choose to subsequently have the affected time period verified by an independent third party.

Guiding Principles

- The verifier must be independent from the firm.
- The verifier must adhere to this Guidance Statement.
- The verifier must adhere to any independence guidance for its profession, if applicable.
- The verifier must create and document its own policies and procedures that address independence.
- To the best of their ability, the verifier and the firm must consider their entire relationship when analyzing potential independence issues.
- The verifier and the firm must each conclude that the verifier is independent prior to the start of the engagement, as evidenced by the engagement letter.
- The verifier and the firm must discuss and document all potential independence issues that arise during or after the engagement and how they were resolved.
- All independence issues must be adequately resolved prior to issuing a verification report.
- If at any time an independence issue cannot be adequately resolved, the verification firm must not perform the verification.

- The independence assessment must be affirmed by both the verifier and the firm at the conclusion of the engagement as evidenced by the issuance of the verification report and the representation letter, respectively.
 - Representation Letter:
The representation letter obtained from the firm must include a representation that the firm, based on its policies and procedures, concludes that the verifier is independent from the firm.
 - GIPS Verification Report:
The verification report must include a statement to the effect that the verifier is independent from the firm. This can be accomplished by including the word “independent” in the report title (e.g., using the title “Independent Verification Report”). The verifier may also include a statement acknowledging its independence within the verification report.
- The verifier and the firm must reassess independence whenever any new information comes to light during and after the engagement that could have an impact on independence. The conclusions reached and rationale for the conclusions must be documented by both the verifier and the firm.
- If it is determined that the verifier that has issued a verification report to the firm was or is not independent of the firm, the firm must cease making any verification claim for the period for which the verifier was not independent and must consider this to be a material error. Please see the Guidance Statement on Error Correction for further information on material errors.
- Verifiers must not engage in the following:
 - stepping into a management role on behalf of the firm;
 - undertaking any management function or a decision-making role relative to the implementation of and compliance with the GIPS standards; or
 - testing their own work.
- “Management functions” are tasks and responsibilities that are related to the GIPS-compliance process. Management functions include, but are not limited to, the following:
 - identifying all portfolios of the firm;
 - assigning portfolios to composites;
 - determining firm definition;
 - determining discretion definition and/or status;
 - creating composite criteria;
 - establishing or modifying policies and procedures;
 - calculating portfolio- and composite-level returns; and
 - preparing compliant presentations.

Assessment of Verifier Independence

In addition to verification services, verifiers may provide additional services (or products) to the firm. The verifier must be particularly cognizant of its role as adviser to the firm on issues relating to compliance with the GIPS standards. The verifier must take into account past services provided to the firm, particularly if the period covered by the past services is also covered by the verification. Independence issues must be resolved in order for the verifier to be independent. Because each situation is unique, the following section contains considerations of other services provided by the verifier. While not exhaustive, these considerations are provided to assist verifiers in more precisely defining the types of services and products that result in an independence issue.

Consideration of Other Services Provided by the Verifier

A verifier can provide consulting services to a firm, including both GIPS- and non-GIPS-related services. However, when the verifier provides GIPS-related services, the verifier must not step into a management role or undertake any management function. Further, the verifier must not perform, or have performed in the past, any services that would result in the verifier reporting on its own work and decisions or calling its own work into question during the verification.

Examples of services that, if performed by the verifier, are unlikely to create an independence issue, include the following:

- providing advice to the GIPS compliance project management team, which must not include making decisions on these issues for the firm;
- identifying issues that hinder a firm's compliance with the GIPS standards;
- educating firm personnel about the GIPS standards and the compliance process;
- providing advice on GIPS implementation or compliance issues;
- providing generic examples of compliant presentations;
- providing GIPS compliance checklists;
- providing formulas and calculation examples;
- providing training on performance-related topics;
- providing examples of policies and procedures language;
- reviewing results of performance-system conversion testing;
- providing a spreadsheet template to a firm that includes calculation examples as long as the firm assumes full responsibility for the calculation methodology; and
- providing advice to the firm on selecting a new performance measurement system for a firm. The verifier must not receive any monetary or nonmonetary compensation from the system providers for their review or recommendation.

Examples of services that, if performed by the verifier, create an independence issue include, but are not limited to, the following:

- establishing policies and procedures;
- functioning as a project manager or as a member of the firm's GIPS compliance project management team that has responsibility for performing management functions (e.g., constructing composites, establishing policies, etc.);
- making decisions about GIPS compliance issues for the firm;
- assigning portfolios to composites;
- identifying all portfolios of the firm;
- identifying and/or defining composites of the firm;
- collating or creating the underlying data required to calculate portfolio-level returns, composite-level returns, or other statistics presented in compliant presentations, including the following:
 - providing systems used to calculate underlying data and
 - providing valuation or reconciliation services;
- providing asset servicing (e.g., custody, depositary, administration, and transfer agency services);
- calculating portfolio, composite, or benchmark returns or other statistics included in compliant presentations;
- preparing compliant presentations;
- participating in the implementation of a new performance measurement system for the firm; and
- functioning as a data warehouse on behalf of the firm. The verifier can maintain data duplicated for its own purposes, but these data must not serve as the firm's primary data source.

Question 1) Are there other services that, if performed by the verifier, create an independence issue?

Other Issues That Must Be Considered When Determining a Verifier's Independence Status

Other issues that are not directly related to verification services or GIPS compliance may impact a verifier's independence. For example, if the verifier serves as an advocate for the firm (e.g., the verifier promotes the firm through marketing efforts or acts on behalf of the firm in litigation or in resolving disputes with third parties), it creates an independence issue.

A verifier and its employees must also consider their personal and financial relationships with their clients and consider whether they are, in fact, independent or could be influenced by such relationships. Mere disclosure of a personal or financial relationship does not resolve the independence issue.

Question 2) This Guidance Statement highlights the relationship between the verifier and the firm. However, the verifier may have other business relationships, including fee arrangements, with other businesses, such as performance system providers or insurance companies. Should we require that these types of relationships be reviewed for independence issues?

Effective Date

This Guidance Statement was originally effective 1 January 2006. Verifiers must conduct their verification and performance examination engagements in accordance with this revised Guidance Statement for all such engagements contracted on or after 1 July 2018. The contract date is typically evidenced by the date of the engagement letter signed by management of both the verification firm and the investment management firm. Verifiers may also voluntarily conduct their engagements in accordance with this Guidance Statement for engagements contracted prior to 1 July 2018 and are encouraged to do so. The prior version of this Guidance Statement is available on the GIPS standards website (www.gipsstandards.org).