VERIFICATION OVERVIEW
WEBINAR

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Agenda

Verification overview:
- What is verification?
- Benefits of verification
- Qualification requirements
- Verification procedures and reporting requirements

Performance examinations overview

Resources

Q&A
What is Verification?

• It’s the review of performance measurement policies and procedures by an independent third party, testing whether
  – The firm has complied with all the composite construction requirements on a firm-wide basis
  – The firm’s policies and procedures are designed to calculate and present performance in compliance with the GIPS standards

• Applies to the entire “firm”, not specific composites (does not ensure the accuracy of any composite presentation)
Verification

• The minimum period for which verification can be performed is one year
  – Or since the firm’s inception, if less than one year

• A firm may choose to have additional testing done on a specific composite’s results, which is referred to as a performance examination
Question #1

A verification is required in order for a firm to claim compliance with the GIPS standards?

a) True

b) False
Verification

• The GIPS standards recommend that firms be verified.
• The GIPS Executive Committee encourages firms to undergo verification and believes it represents best practice.
Question #2

What is the verification status of your investment management firm?

a) My firm claims compliance with the GIPS standards and is verified.

b) My firm claims compliance with the GIPS standards and is not verified.

c) My firm does not claim compliance with the GIPS standards.

d) I don’t know the compliance/verification status of my firm.

e) The GIPS standards do not apply to my employer.
Question #3

What percentage of firms that have notified CFA Institute that they are GIPS compliant have also been verified?

a) Less than 25%
b) Between 25% and 50%
c) Between 50% and 75%
d) Over 75%
1570 Firms Registered GIPS Compliance

- 86% Verified Firms
- 14% Non-Verified Firms

CFA Institute
Benefits of Verification

• Brings additional credibility to the compliance claim supports the overall guiding principles of the GIPS standards: fair representation and full disclosure

• May provide:
  – Increase in knowledge and quality of compliant presentations.
  – Improvement in internal processes and procedures
  – Additional confidence in your firm’s claim of compliance.
  – Marketing advantages

• “The Benefits of Verification” document available
What is an Independent Third Party?

- Guidance Statement on Verifier Independence
- Performs its service in an unbiased manner and is not performing any management function or verifying its own work
- The verification firm and the verification client must reach a conclusion regarding the verification firm’s independence
- Disclosure alone usually does not “cure” an independence issue
- Determining independence is the responsibility of both the verification client and the verification firm
Verifier Qualification Requirements

• Independent from investment management firm
• Knowledgeable of the GIPS standards
• Appropriate ability/experience and expertise regarding investment management practices, including performance and business processes.
• Knowledgeable of applicable laws/ regulations regarding calculation and presentation of performance
• Verifiers must follow currently accepted standards of practice within their industry (if applicable)
Selecting a Verifier

• “Suggested Questions to Ask Verification Firms” document available

• Firms should ensure communication throughout the year will be available (not just during the verification)

• Firms should use the verifier to assist when issues arise, instead of waiting until the verification

• CFA Institute does not conduct verifications
Compliance Statement for a Verified Firm

[Insert name of firm] claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. [Insert name of firm] has been independently verified for the periods [insert dates]. The verification report(s) is/are available upon request.

Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm’s policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. Verification does not ensure the accuracy of any specific composite presentation.
Compliance Statement for a Firm that Has Not Been Verified

[Insert name of firm] claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. [Insert name of firm] has not been independently verified.
Minimum Required Verification Procedures

• Pre-Verification Procedures
  – Knowledge of the GIPS standards
  – Knowledge of regulations
  – Knowledge of the firm
  – Knowledge of the firm’s policies and procedures
  – Knowledge of valuation basis and performance calculations
Verification of a firm requires the verifier to test every composite that the firm markets to prospective clients?

a) True

b) False
Minimum Required Verification Procedures

- The entire firm must be subject to the verification testing
- May use sampling; not required to test all portfolios or composites within the firm
- If errors are found, additional testing may be needed
- Verifiers must follow currently accepted standards of practice within their industry (if applicable)
Minimum Required Verification
Procedures

• Must perform sufficient procedures to determine that:
  – The firm is appropriately defined
  – All actual, fee-paying, discretionary portfolios are included in at least one composite
  – Definition of discretion is consistently applied
  – All portfolios are included in their respective composites for the correct time periods
  – Policies for ensuring the existence and ownership of client assets are appropriate and have been consistently applied
  – Policies for creating and maintaining composites have been consistently applied
  – List of composite descriptions is complete
  – Total firm assets are appropriately calculated
Minimum Required Verification Procedures

• Composite construction – must test:
  – Discretion status
  – Timing of composite inclusion and exclusion
  – Proper composite assignment based on contract, guidelines, etc.
  – Portfolios that change composites do so based only on changes to a portfolio’s guidelines (or a composite redefinition)
Minimum Required Verification Procedures

• Data review – must test:
  – Security purchases/sales, and valuation
  – Income and expense recognition
  – Treatment of cash receipts and disbursements: cash flow or not?
Minimum Required Verification Procedures

• Performance calculation – must test:
  – Portfolio-level returns
  – Composite-level returns
  – Custom benchmark calculations
  – All other required presentation items
    • Internal dispersion
    • Number of portfolios
    • Composite value
  – 3 year annualized ex-post standard deviation
Minimum Required Verification Procedures

• Compliant presentations
  – Must test for completeness and accuracy of disclosures

• Maintenance of records
  – Verifier must maintain sufficient documentation supporting their work including all significant judgments and conclusions

• Management representation letter
  – From the firm to the verifier
  – Must confirm that the firm complies with the GIPS standards and policies and procedures utilized are as described in policies and procedures document(s)
Verification Report

- Based on the procedures performed, the verifier will express an opinion on whether the firm has:
  - Complied with all the composite construction requirements of the GIPS standards on a firm-wide basis (over a period), and
  - Designed its policies and procedures to calculate and present performance in compliance with the GIPS standards

- If the verifier concludes the firm is not in compliance or the records of the firm cannot support a verification, they must issue a statement to the firm clarifying why a verification report could not be issued

- Guidance Statement on Verification contains listing of required items to include in the verification report
Question  #5

A verification report must indicate that the firm has prepared and presented its composite presentation in compliance with the GIPS standards?

a) True

b) False
Composite-Specific Performance Examination

- A performance examination is a detailed examination of a specific composite’s compliant presentation by an independent verifier. Typically performed by same firm that has performed verification.
- Optional— but must be done after or along with a firm-wide verification.
Composite-Specific Performance Examination

• Verifier determines scope, procedures, etc.
• Verifier must accumulate sufficient evidence and perform sufficient procedures so that risk of not detecting errors during the exam is mitigated to an acceptably low level.
• The verifier must maintain sufficient documentation to support their work including all significant judgments and conclusions.
Performance Examination Report

• Issued after a Performance Examination has been performed & opines for particular composite firm has:
  – Constructed the composite and calculated the composite performance in compliance with the GIPS standards; and
  – Prepared and presented the composite presentation in compliance with the GIPS standards.

• Report must not be issued when verifier knows firm is not in compliance with the Standards, presentation doesn’t comply with the Standards, or firm’s records cannot support the examination of the composite and its associated presentation.

• See Guidance Statement on Performance Examinations for further information.
Minimum Required Performance Examination Procedures

• Performance Examinations Guidance Statement provides minimum procedures verifiers must follow regarding the following:
  – Timing of inclusion/exclusion of portfolios
  – Portfolio classification
  – External cash flows
  – Portfolio: income/expenses, purchases & sales, and valuation
  – Existence and ownership of client assets
  – Performance calculations
  – Composite compliant presentation
Compliance Statement for a Verified Firm for an Examined Composite

[Insert name of firm] claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. [Insert name of firm] has been independently verified for the periods [insert dates].

Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm’s policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. The [insert name of composite] composite has been examined for the periods [insert dates]. The verification and performance examination reports are available upon request.
Summary

• Verification is the review of performance measurement policies and procedures of GIPS compliant firms
• Performed by an independent third party
• Additional verifier qualification requirements
• Not required by the GIPS standards
• Adds credibility to a firm’s compliance claim
• Firm-wide but can use sample testing
• Minimum required verification testing procedures
• Not a performance examination of a specific composite
Additional Questions?
Resources

• The gipsstandards.org website:
  – Complete list of Guidance Statements
  – New Q&A database
  – Brochures and webcasts
  – Newsletter archive

• The GIPS Handbook

• Helpdesk (gips@cfainstitute.org)

• Firm notification requirement (gipscompliance@cfainstitute.org)

• GIPS newsletter (http://www.gipsstandards.org/news/Pages/newsletter.aspx)

• Twitter: @GIPS

• Certificate in Investment Performance Measurement (CIPM): cfainstitute.org/cipm
Upcoming Events

16 September 2015
- GIPS Interactive Workshop – San Diego, California, US
- Fundamentals of Performance Measurement & Attribution Workshop – San Diego, California, US

17-18 September 2015
- GIPS Annual Conference – San Diego, California, US

28 October 2015
- Fundamentals of GIPS Compliance Webinar