



Claiming Compliance: What it Really Means

There is some misunderstanding about what it means to claim compliance with the Global Investment Performance Standards (GIPS®). We often see firms make reference to the GIPS standards incorrectly, or in the wrong places. Who can forget the full page ad in the *Wall Street Journal* in which a firm stated that they were GIPS compliant and their performance track record was “GIPS verified?” (Hint: a track record isn’t verified; only a firm is verified. And you can’t refer to the GIPS standards without including certain disclosures, as explained later.) While many firms adopt the “more is better” approach to claiming compliance and making references to the GIPS standards, this often results in a firm getting themselves into trouble. When a firm claims compliance and uses one of the two GIPS compliance statements, either the GIPS Advertising Guidelines compliance statement or the “regular” GIPS standards compliance statement, all appropriate disclosures must be included. However, a GIPS compliant firm does not have to prepare all marketing materials strictly in compliance with the GIPS standards. In fact, marketing materials can be prepared that make absolutely no mention of the GIPS standards. We will explain the different options for making reference to the GIPS standards, as well as what a claim of compliance means for your marketing efforts.

We claim compliance with the GIPS standards. How do we tell the world that we claim compliance?

A firm that meets all the requirements of the GIPS standards on a firm-wide basis can tell the world about its claim of compliance through the use of the GIPS compliance statement, which is: [Firm Name] has prepared and presented this report in compliance with the Global Investment Performance Standards (GIPS®). The claim of compliance may be included only on a composite presentation that includes all required disclosures. A compliant presentation includes data typically presented in a chart format, including annual returns for both the composite and the benchmark and a variety of other data about the composite, such as the number of portfolios as of year end. In addition, there are required disclosures that must accompany the chart data, such as a brief description of the composite’s strategy.

Sample compliant presentations are included in the GIPS Handbook, pp. 40-41.

If we want to claim compliance in an advertisement, do we need to include a fully compliant presentation?

No. A firm is allowed to follow the GIPS Advertising Guidelines when claiming compliance in an advertisement. These are essentially an abbreviated set of disclosures that allow firms to claim compliance in an advertisement without presenting a fully compliant presentation. When using the GIPS Advertising Guidelines, a firm must include:

- A description of the firm;
- How an interested party can obtain a presentation that complies with all the requirements of the GIPS standards and/or a list and description of all firm composites; and
- The GIPS Advertising Guidelines compliance statement: [Firm Name] claims compliance with the Global Investment Performance Standards (GIPS®).

If you are presenting performance you must also include:

- A description of the strategy;
- Period-to-date composite returns;
- 1-, 3-, and 5-year cumulative annualized composite returns or 5 years of annual composite returns, with the end-of-period date clearly identified;
- Whether performance is presented gross or net of investment management fees;
- Benchmark returns for the same period;
- Currency used to express returns;
- Description of the use and extent of leverage and derivatives if they are used as an active part of the investment strategy; and
- If presenting non-compliant performance information for periods prior to January 1, 2000, identify the period and the specific information that is not in compliance and provide the reason why the information is not in compliance.

(Continued on page 2)

Inside this issue:

Save the Dates	3
Break in Performance	4
VPS Survey Results to be Released Soon	4

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(Continued from page 1)

If we claim compliance with the GIPS standards, must we follow the GIPS Advertising Guidelines in an advertisement?

No. Claiming compliance with the GIPS Advertising Guidelines is voluntary. A GIPS-compliant firm that advertises has three options with respect to the GIPS standards:

- Include a fully compliant presentation in the advertisement;
- Prepare the advertisement in accordance with the GIPS Advertising Guidelines; or
- Make no mention of the GIPS standards.

Do we have to include a claim of compliance (via either the regular claim of compliance or following the GIPS Advertising Guidelines) in all of our marketing materials?

No. The only requirement that you have to meet is GIPS Provision O.A.11, which states that a firm must make every reasonable attempt to provide a fully compliant presentation to all prospective clients. As long as you have provided a compliant presentation to a prospective client within the past 12 months, this requirement is met. We often recommend to our clients that they include a fully compliant GIPS presentation in the back of every pitch book to ensure they meet this requirement. Don't forget that RFPs and consultant databases must be considered prospective clients, so at least once a year you must ensure you provide the appropriate compliant presentation to them as well.

Are we limited to providing only "GIPS compliant" composite presentations in our marketing materials?

No. As long as there is no reference to the GIPS standards you may include whatever information you wish, with one caveat: a GIPS-compliant firm may not present information that contradicts or conflicts with the GIPS standards. For example a compliant firm may not link (or join) performance of a model portfolio to the performance of a composite.

In our pitch books, we present performance through the most recent quarter-end. Our policy is to include a compliant presentation in our pitch books. If we're meeting with a prospective client in October, does the compliant presentation have to be updated through Q3?

No. There is no requirement to update the compliant presentation more frequently than

annually, but you may do so if you wish. The other materials in the pitch book can be updated with the most recent return information, but that does not have any impact on the compliant presentation. We typically recommend updating the compliant presentations annually to minimize the risk of error.

How should we answer GIPS-related questions that are asked in RFPs or in databases that are either out-of-date or inaccurate with respect to the GIPS standards? For example, we were asked if our composite returns are calculated in compliance with CFAI Standards and, if so, at what level? How should we respond?

If your firm claims compliance with the GIPS standards and you are providing returns derived from a GIPS-compliant composite, answer yes to the calculation question. As far as the "level" question, we assume they are referring to the outdated concept of two levels of verification that existed in the old AIMR-PPS[®] standards. We suggest you answer yes to this question, too. In an RFP there is typically space allowed to provide answers, and in a database there is usually a section for notes, so we recommend using this space to explain how the old standards were retired and replaced with the new GIPS standards and answer the questions as they should have been asked. Additionally, you should provide, or attempt to provide, a compliant presentation along with your proposal or information provided to the database.

Can we claim compliance only for our marketed composites?

No. A firm may claim compliance only on a firm-wide basis. Firms may not pick and choose composites or divisions of the firm (e.g. equity versus fixed income) they want to be compliant. Either you are compliant firm-wide, based on your firm definition, or you are not. You must be able to provide a fully compliant presentation for *any* composite on your list and description of composites upon request, and that list must include all composites, not just those you market. It is best practice to create compliant presentations for all of your composites and then update them once a year. That way if a prospective client, the SEC, or your verifier asks you for a GIPS compliant presentation for one of your non-marketed composites, you can hand it over with ease instead of scrambling to gather 10 years of composite data to create a compliant presentation.

(Continued on page 3)

"Firms must make every reasonable effort to provide a compliant presentation to all prospective clients."

GIPS Provision O.A.11

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(Continued from page 2)

Do we need to be verified before claiming compliance?

No. Verification is voluntary. While there has been much discussion over whether verification will be mandatory at some point, the current view from the Executive Committee (the committee that oversees the GIPS standards) is that verification will not be mandatory, at least not in the near future.

If our firm has been verified, do we have to disclose this in our compliant presentations?

No. Currently the GIPS standards encourage firms that have been verified to disclose in compliant presentations and advertisements that the firm has been verified, but this is not required. If you do choose to add this disclosure, you must disclose the periods of verification if the compliant presentation includes periods that have not been subject to firm-wide verification. However, the next draft of the GIPS standards will require a firm to disclose their verification status. Of course this is subject to change as a result of the public comment process, but we expect this disclosure change will happen. Note that the next version of the GIPS standards should be issued for public comment in early 2009, and it is expected that the effective date of the next version will be January 1, 2011.

GIPS Provision 5.A.1 states that a firm must present annual returns for all years in the compliant presentation. We started a new strategy as of June 30, 2007. Do we have to wait until De-

ember 31, 2008 to present an annual return for 2008 and claim compliance?

No. You are allowed to present performance for partial periods as long as the periods covered are clearly disclosed. In this instance you can report a year-to-date return for 2007 in the composite's compliant presentation. Please remember that returns for less than a year must not be annualized.

Are we required to provide a compliant presentation to our current clients?

The GIPS standards do not address client reporting. A compliant firm is not required to provide compliant presentations to current clients. Of course you may do so if you wish, but it is not required. If you are presenting a new strategy to an existing client, you should treat the current client as a prospective client for the new strategy and provide a fully compliant presentation for that strategy.

We prepare and distribute a newsletter quarterly and include performance information in accordance with the GIPS Advertising Guidelines. If someone hires us based on this information, are we still required to provide a compliant presentation to them?

Yes. Providing information to a prospective client that is prepared in accordance with the GIPS Advertising Guidelines does not relieve you of the requirement to make every reasonable effort to provide a fully compliant presentation to the prospective client.

"You are allowed to present performance for partial periods as long as the periods covered are clearly disclosed... Please remember that returns for less than a year must not be annualized."

Save the Dates

The next annual GIPS conference, sponsored by CFA Institute, will be held on September 25th and 26th, at the Westin Copley Place in Boston. This conference is the must attend event for many of us in the performance world. The day before the conference, on September 24th, a GIPS introduction workshop will also be held. This workshop is targeted to performance professionals who are new to the GIPS standards, or wish to have a thorough refresher on complying with the GIPS standards.

Registration information should be posted on the GIPS standards website www.gipsstandards.org in the next few

months. We recommend registering early as both the conference and the workshop sold out last year.

Additionally, early that same week the GIPS Executive Committee will be meeting in Boston. The public meeting should be on Tuesday, September 23rd.

Finally, we will be hosting a dinner for our clients on Wednesday, September 24th. If you are attending the conference or are in the Boston area please plan on attending. Dinner will be at Maggiano's, near the conference hotel. Details will be provided soon.

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Performance is all we do.



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Vincent Performance Services LLC provides consulting and verification services to firms that comply, or wish to comply, with the Global Investment Performance Standards (GIPS®). Our clients range in size from less than \$1 billion of assets under management to over \$500 billion and are located throughout the U.S.

Additional information about our services and expertise can be found at www.vincentperformance.com

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Break In Performance

What happens if, at some point in time, a composite loses all of its members? This could happen if all accounts within the composite terminate, or if they temporarily do not qualify for composite inclusion based on other factors, such as experiencing significant cash flows or falling below the composite minimum, resulting in a break in performance. How should you handle this break in the composite's compliant presentation? Recently a Q&A was posted to

the GIPS Database on this topic, under the Performance History/Track Record category, and states:

- Returns both before and after the break must be presented;
- Returns for the partial year must be presented; and
- Returns must not be linked across the break.

The Q&A also includes a sample presentation. See the Q&A database at www.gipsstandards.org/standards

VPS Survey Results to be Released Soon

We recently undertook a project to survey US and Canadian managers of institutional assets as reported by *Pensions & Investments*. We decided to conduct the survey for several reasons:

- We are frequently asked some variation on the following questions: What percentage of firms claim compliance? Do small firms claim compliance, or only large firms? What percentage of firms are verified? Do most firms have performance examinations done in addition to the verification? While we are happy to answer these questions as best as we can, we wanted hard facts to support our views.

- The GIPS standards include some changes with an effective date of 2010. The two significant changes are the prohibition against using carve-outs (with allocated cash) after that date, and the requirement to revalue portfolios for large cash flows. (Large can be defined for each composite, but this will effectively require the ability to price daily.) We want to know whether firms are ready for 2010.
- We want to learn what areas of the GIPS standards need additional clarification or guidance.

We will provide the survey results to any and all interested parties. Stay tuned for more information.