GLOBAL INVESTMENT PERFORMANCE STANDARDS™

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ASSOCIATION FOR INVESTMENT MANAGEMENT AND RESEARCH®

Setting a Higher Standard for Investment Professionals Worldwide™

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GLOBAL INVESTMENT PERFORMANCE STANDARDS

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GLOBAL INVESTMENT PERFORMANCE STANDARDS

I. INTRODUCTION

PREAMBLE: WHY IS A GLOBAL STANDARD NEEDED?

1. The financial markets and the investment management industry are becoming increasingly global in nature. Given the variety of financial entities and countries involved, this globalization of the investment process and the exponential growth of assets under management demonstrate the need to standardize the calculation and presentation of investment performance.

2. Prospective clients and asset managers will benefit from an established standard for investment performance measurement and presentation that is recognized worldwide. Investment practices, regulation, performance measurement, and reporting of performance results vary considerably from country to country. Some countries have guidelines that are widely accepted within their borders, and others have few recognized standards for presenting investment performance.

3. Requiring investment managers to adhere to performance presentation standards will help assure investors that the performance information is both complete and fairly presented. Firms in countries with minimal presentation standards will be able to compete for business on an equal footing with firms from countries that have more developed standards. Firms from countries with established practices will have more confidence of being fairly compared to "local" firms when competing for business in countries that have not previously adopted performance standards.

4. Both prospective and existing clients of investment firms will benefit from a global investment performance standard by having a greater degree of confidence in the performance numbers presented by the firms. Performance standards that are accepted in *all* countries enable all investment firms to measure and present their investment performance so that clients can readily compare investment performance among firms.

VISION STATEMENT

5. *A global investment performance standard leads to readily accepted presentations of investment performance that (1) present performance results that are readily comparable among investment managers, without regard to geographic location, and (2) facilitate a dialogue between investment managers and their prospective clients about the critical issues of how the manager achieved performance results and future investment strategies.*

OBJECTIVES

6. To obtain worldwide acceptance of a standard for the calculation and presentation of investment performance in a fair, comparable format that provides full disclosure.

7. To ensure accurate and consistent investment performance data for reporting, record keeping, marketing, and presentation.

8. To promote fair, global competition among investment firms for all markets without creating barriers to entry for new firms.

9. To foster the notion of industry self-regulation on a global basis.

OVERVIEW

10. The Global Investment Performance Standards (GIPS) have several key characteristics:

    a. GIPS are ethical standards for investment performance presentation to ensure fair representation and full disclosure of an investment firm's performance history.

    b. GIPS exist as a minimum worldwide standard where local or country-specific law, regulation, or industry standards may not exist for investment performance measurement and/or presentation.

    c. GIPS require managers to include all actual fee-paying discretionary portfolios in composites defined according to similar strategy and/or investment objective and require firms to show GIPS compliant history for a minimum of five years, or since inception of the firm or composite if in existence less than five years.

d. GIPS require firms to use certain calculation and presentation methods and to make certain disclosures along with the performance record.

e. GIPS rely on the integrity of input data. The accuracy of input data is critical to the accuracy of the performance presentation. For example, benchmarks and composites should be created/selected on an *ex ante* basis, not after the fact.

f. GIPS consist of guidelines that firms are required to follow in order to claim compliance. The adoption of other elements of GIPS is recommended for firms to achieve best practice in performance presentation.

g. GIPS apply to the presentation of investment performance of assets managed on behalf of a third party.

h. GIPS should be applied with the goal of full disclosure and fair representation of investment performance. Meeting the objective of full and fair disclosure is likely to require more than compliance with the minimum requirements of GIPS. If an investment firm applies GIPS in a performance situation that is not addressed specifically by the Standards or is open to interpretation, disclosures other than those required by GIPS may be necessary. To fully explain the performance included in a presentation, firms are encouraged to present all relevant supplemental information.

i. In cases in which applicable local or country-specific law or regulation conflicts with GIPS, the Standards require firms to comply with the local law or regulation and make full disclosure of the conflict.

j. GIPS do not address every aspect of performance measurement, valuation, attribution, or coverage of all asset classes. GIPS will evolve over time to address additional aspects of investment performance. Certain recommended elements in GIPS may become requirements in the future.

SCOPE

11. *Application of GIPS*. Investment management firms from any country may come into compliance with GIPS. Compliance with GIPS will facilitate a firm's participation in the investment management industry on a global level.

12. *Definition of a Firm*. GIPS must be applied on a firmwide basis. A firm may define itself as

    a. an entity registered with the appropriate national regulatory authority overseeing the entity's investment management activities; *or*

    b. an investment firm, subsidiary, or division held out to clients or potential clients as a distinct business unit (e.g., a subsidiary firm or distinct business unit managing private client assets may claim compliance for itself without its parent organization being in compliance);

    c. (until January 1, 2005), all assets managed to one or more base currencies (for firms managing global assets).

    When presenting investment performance in compliance with GIPS, an investment management firm must state how it defines itself as a "firm."

13. *Historical Performance Record*.

    a. A firm is required to present, at a minimum, five years of annual investment performance that is compliant with GIPS. If the firm or composite has been in existence less than five years, firms must present performance since the inception of the firm or composite.

    b. After a firm presents five years of compliant history, firms must present additional annual performance up to ten years. For example, after a firm presents five years of compliant history, the firm must add an additional year of performance each year so that after five years of claiming compliance, the firm presents a ten year performance record.

    c. A firm may link a non-GIPS-compliant performance record to their compliant history so long as no non-compliant performance is presented for periods after January 1, 2000, and the firm discloses the periods of non-compliance and explains how the presentation is not in compliance with GIPS.

Nothing in this section shall prevent firms from immediately presenting more than five years of performance results.

COMPLIANCE

14. *Requirements*. Firms must meet *all* the requirements set forth in GIPS to claim compliance with GIPS. Although GIPS requirements must be met immediately by a firm claiming compliance, the following requirements do not go into effect until a future date:

    a. Portfolios must be valued at least monthly for periods beginning January 1, 2001.

    b. Time-weighted rates of return adjusted for cash flows are required. Firms must use time-weighted rates of return *adjusted for daily-weighted* cash flows for periods beginning January 1, 2005.

    c. For periods beginning January 1, 2010, firms will likely be required to value portfolios on the date of any external cash flow.

    d. Firms must use trade-date accounting for periods beginning January 1, 2005.

    e. Accrual accounting must be used for dividends (as of the ex dividend date) for periods beginning January 1, 2005.

    Until these future requirements become effective, these provisions should be considered recommendations. Firms are encouraged to implement these requirements prior to their effective date. To ease compliance with GIPS when the future requirements take effect, firms should design performance software to incorporate these future requirements.

15. *Compliance Check*. Firms must take all steps necessary to ensure that they have satisfied all of the requirements of GIPS before claiming compliance with GIPS. Firms are strongly encouraged to perform periodic internal compliance checks and implement adequate business controls on all stages of the investment performance process—from data input to presentation material—to ensure the validity of compliance claims.

16. *Third-Party Performance Measurement and Composite Construction*. GIPS recognize the role of independent third-party performance measurers and the value they can add to the firm's performance-measurement activities. Where third-party performance measurement is an established practice or is available, firms are encouraged to use this service as it applies to the investment firm. Similarly, where the practice is to allow third parties to construct composites for investment firms, firms can use such composites in a GIPS-compliant presentation only if the composites comply with GIPS.

17. *Claim of Compliance*. Once a firm has met all of the required elements of GIPS, the firm may use the following "Compliance Statement" to indicate that the performance presentation is in compliance with GIPS:

    [Insert name of firm] has prepared and presented this report in compliance with the Global Investment Performance Standards (GIPS).

    If the performance presentation does not meet all of the requirements of GIPS, firms cannot represent that the performance presentation is "in compliance with the Global Investment Performance Standard *except for . . .*" Statements referring to the calculation methodology used in a presentation as being "*in accordance* (or compliance) with the Global Investment Performance Standards" are prohibited except when applied to the performance of a single, existing client.

18. *Sample Presentation*. A sample presentation, shown in Appendix A, provides an example of what a compliant performance presentation could look like, including disclosures.

RELATIONSHIP OF GIPS WITH COUNTRY-SPECIFIC LAWS, REGULATIONS, AND INDUSTRY STANDARDS

19. GIPS fill the void where no country standards exist. Regulators and investment organizations worldwide are strongly encouraged to recognize and adopt GIPS as the performance presentation standard applicable to their constituencies. If there is a need for country-

specific guidelines that go beyond GIPS, regulators and organizations are encouraged to develop and implement such guidelines to augment, but not conflict with, GIPS. Regulators are urged to supervise country compliance with GIPS and any country-specific standards that may exist.

20. Where existing laws, regulations, or industry standards already impose performance presentation standards, firms are strongly encouraged to comply with GIPS *in addition to* those local requirements. Compliance with applicable law or regulation does not necessarily lead to compliance with GIPS. When complying with GIPS and local law or regulation, firms must disclose any local laws and regulations that conflict with GIPS.

21. The establishment of GIPS will minimize the complexities that result with the existing contingent reciprocity agreements among organizations with their own standards. Organizations are encouraged to recognize GIPS rather than establish "country-to-country" reciprocity agreements for country-specific standards. When a country or group establishes local performance presentation standards, such standards should incorporate all of the required elements of the GIPS and state that compliance with GIPS is equivalent to compliance with the local standards.

II. THE GLOBAL INVESTMENT PERFORMANCE STANDARDS

GIPS is divided into five sections that reflect the basic elements involved in presenting performance information: Input Data, Calculation Methodology, Composite Construction, Disclosures, and Presentation and Reporting.

1. *Input Data*: Consistency of input data is critical to effective compliance with GIPS and establishes the foundation for full, fair, and comparable investment performance presentations. The Standards provide the blueprint for a firm to follow in constructing this foundation.
2. *Calculation Methodology*: Achieving comparability among investment management firms' performance presentations requires uniformity in methods used to calculate returns. The Standards mandate the use of certain calculation methodologies (e.g., performance must be calculated using a time-weighted total-rate-of-return method).
3. *Composite Construction*: A composite is an aggregation of a number of portfolios into a single group that represents a particular investment objective or strategy. The composite return is the asset-weighted average of the performance results of all the portfolios in the composite. Creating meaningful, asset-weighted composites is critical to the fair presentation, consistency, and comparability of results over time and among firms.
4. *Disclosures*: Disclosures allow firms to elaborate on the raw numbers provided in the presentation and give the end user of the presentation the proper context in which to understand the performance results. To comply with GIPS, firms must disclose certain information about their performance presentation and the calculation methodology adopted by the firm. Although some disclosures are required of all firms, others are specific to certain circumstances and thus may not be applicable in all situations.
5. *Presentation and Reporting*: After constructing the composites, gathering the input data, calculating returns, and determining the necessary disclosures, the firm must incorporate this information in presentations based on the guidelines set out in GIPS for presenting the investment performance results. No finite set of guidelines can cover all potential situations or anticipate future developments in investment industry structure, technology, products, or practices. When appropriate, firms have the responsibility to include in GIPS-compliant presentations information not covered by the Standards.

The Standards for each section are divided between requirements, listed first in each section, and recommended guidelines. Firms must follow the required elements of GIPS to claim compliance with GIPS. Firms are strongly encouraged to adopt and implement the recommendations to ensure that the firm fully adheres to the spirit and intent of GIPS. An example of a GIPS-compliant presentation for a single composite is included in Appendix A.

Although GIPS may be translated into many languages, if a discrepancy arises between the different versions of the standards, the English version of GIPS is controlling.

1. Input Data

1.A. *Requirements*

1.A.1. All data and information necessary to support a firm's performance presentation and to perform the required calculations must be captured and maintained.

1.A.2. Portfolio valuations must be based on market values (not cost basis or book values).

1.A.3. Portfolios must be valued at least quarterly. For periods beginning January 1, 2001, portfolios must be valued at least monthly. For periods beginning January 1, 2010, it is anticipated that firms will be required to value portfolios on the date of any external cash flow.

1.A.4. Firms must use trade-date accounting for periods beginning January 1, 2005.

1.A.5. Accrual accounting must be used for fixed-income securities and all other assets that accrue interest income.

1.A.6. Accrual accounting must be used for dividends (as of the ex dividend date) for periods beginning January 1, 2005.

1.B. *Recommendations*

1.B.1. Sources of exchange rates should be the same for the composite and the benchmark.

2. Calculation Methodology

2.A. *Requirements*

2.A.1. Total return, including realized and unrealized gains plus income, must be used.

2.A.2. Time-weighted rates of return that adjust for cash flows must be used. Periodic returns must be geometrically linked. Time-weighted rates of return that adjust for daily-weighted cash flows must be used for periods beginning January 1, 2005. Actual valuations at the time of external cash flows will likely be required for periods beginning January 1, 2010.

2.A.3. In both the numerator and the denominator, the market values of fixed-income securities must include accrued income.

2.A.4. Composites must be asset weighted using beginning-of-period weightings or another method that reflects both beginning market value and cash flows.

2.A.5. Returns from cash and cash equivalents held in portfolios must be included in total-return calculations.

2.A.6. Performance must be calculated after the deduction of all trading expenses.

2.A.7. If a firm sets a minimum asset level for portfolios to be included in a composite, no portfolios below that asset level can be included in the composite.

2.B. *Recommendations*

2.B.1. Returns should be calculated net of non-reclaimable withholding taxes on dividends, interest, and capital gains. Reclaimable withholding taxes should be accrued.

2.B.2. Performance adjustments for external cash flows should be treated in a consistent manner. Significant cash flows (i.e., 10 percent of the portfolio or greater) that distort performance (i.e., plus or minus 0.2 percent for the period) may require portfolio revaluation on the date of the cash flow (or after investment) and the geometric linking of subperiods. Actual valuations at the time of external cash flows will likely be required for periods beginning January 1, 2010.

3. Composite Construction

3.A. *Requirements*

3.A.1. All actual fee-paying discretionary portfolios must be included in at least one composite.

3.A.2. Firm composites must be defined according to similar investment objectives and/or strategies.

3.A.3. Composites must include new portfolios on a timely and consistent basis after the portfolio comes under management—unless specifically mandated by the client.

3.A.4. Terminated portfolios must be included in the historical record of the appropriate composites up to the last full measurement period that the portfolio was under management.

3.A.5. Portfolios must not be switched from one composite to another unless documented changes in client guidelines or the redefinition of the composite make switching appropriate. The historical record of the portfolio must remain with the appropriate composite.

3.A.6. Convertible and other hybrid securities must be treated consistently across time and within composites.

3.A.7. Carve-out returns excluding cash cannot be used to create a stand-alone composite. When a single asset class is carved out of a multiple-asset portfolio and the returns are presented as part of a single-asset composite, cash must be allocated to the carve-out returns and the allocation method must be disclosed. Beginning January 1, 2005, carve-out returns must not be included in single asset class composite returns unless the carve-outs are actually managed separately with their own cash allocations.

3.A.8. Composites must include only assets under management and may not link simulated or model portfolios with actual performance.

3.B. *Recommendations*

3.B.1. Separate composites should be created to reflect different levels of allowed asset exposure.

3.B.2. Unless the use of hedging is negligible, portfolios that allow the use of hedging should be included in different composites from those that do not.

4. Disclosures

4.A. *Requirements*

The following disclosures are *mandatory*:

4.A.1. The definition of "firm" used to determine the firm's total assets and firm-wide compliance.

4.A.2. Total firm assets for each period.

4.A.3. The availability of a complete list and description of all of the firm's composites.

4.A.4. If settlement-date valuation is used by the firm.

4.A.5. The minimum asset level, if any, below which portfolios are not included in a composite.

4.A.6. The currency used to express performance.

4.A.7. The presence, use and, extent of leverage or derivatives, including a description of the use, frequency and characteristics of the instruments sufficient to identify risks.

4.A.8. Whether performance results are calculated gross or net of investment management fees and other fees paid by the clients to the firm or to the firm's affiliates.

4.A.9. Relevant details of the treatment of withholding tax on dividends, interest income, and capital gains. If using indexes that are net of taxes, firms must disclose the tax basis of the composite (e.g., Luxembourg based or U.S. based) versus that of the benchmark.

4.A.10. For composites managed against specific benchmarks, the percentage of the composites invested in countries or regions not included in the benchmark.

4.A.11. Any known inconsistencies between the chosen source of exchange rates and those of the benchmark must be described and presented.

4.A.12. Whether the firm has included any non-fee-paying portfolios in composites and the percentage of composite assets that are non-fee-paying portfolios.

4.A.13. Whether the presentation conforms with local laws and regulations that differ from GIPS requirements and the manner in which the local standards conflict with GIPS.

4.A.14. For any performance presented for periods prior to January 1, 2000, that does not comply with GIPS, the period of noncompliance and how the presentation is not in compliance with GIPS.

4.A.15. When a single asset class is carved out of a multiple-asset portfolio and the returns are presented as part of a single-asset composite, the method used to allocate cash to the carve-out returns.

4.B. *Recommendations*

The following disclosures are *recommended*:

4.B.1. The portfolio valuation sources and methods used by the firm.

4.B.2. The calculation method used by the firm.

4.B.3. When gross-of-fee performance is presented, the firm's fee schedule(s) appropriate to the presentation.

4.B.4. When only net-of-fee performance is presented, the average weighted management and other applicable fees.

4.B.5. Any significant events within the firm (such as ownership or personnel changes) that would help a prospective client interpret the performance record.

5. Presentation and Reporting

5.A. *Requirements*

5.A.1. The following items must be reported:

(a) At least five years of performance (or a record for the period since firm inception, if inception is less than five years) that is GIPS compliant. After presenting five years of performance, firms must present additional annual performance up to 10 years. (For example, after a firm presents five years of compliant history, the firm must add an additional year of performance each year so that after five years of claiming compliance, the firm presents a 10-year performance record).

(b) Annual returns for all years.

(c) The number of portfolios and amount of assets in the composite and the percentage of the firm's total assets represented by the composite at the end of each period.

(d) A measure of the dispersion of individual component portfolio returns around the aggregate composite return.

(e) The standard Compliance Statement indicating firmwide compliance with GIPS.

(f) The composite creation date.

5.A.2. Firms may link non-GIPS-compliant performance to their compliant history so long as firms meet the disclosure requirements of Section 4 and no non-compliant performance is presented for periods after January 1, 2000. (For example, a firm that has been in existence since 1990 that wants to present its entire performance history *and* claim compliance as of January 1, 2000, must present performance history that meets the requirements of GIPS at least from January 1, 1995, and must meet the disclosure requirements of Section 4 for any non-compliant history prior to January 1, 1995.)

5.A.3. Performance for periods of less than one year must not be annualized.

5.A.4. Performance results of a past firm or affiliation can only be linked to or used to represent the historical record of a new firm or new affiliation if

(a) a change only in firm ownership or name occurs, or

(b) the firm has all of the supporting performance records to calculate the performance, substantially all the assets included in the composites transfer to the new firm, and the investment decision-making process remains substantially unchanged.

5.A.5. If a compliant firm acquires or is acquired by a non-compliant firm, the firms have one year to bring the non-compliant firm's acquired assets into compliance.

5.A.6. If a composite is formed using single-asset carve-outs from multiple asset class composites, the presentation must include the following:

(a) a list of the underlying composites from which the carve-out was drawn, *and*

(b) the percentage of each composite the carve-out represents.

5.A.7. The total return for the benchmark (or benchmarks) that reflects the investment strategy or mandate represented by the composite must be presented for the same periods for which the composite return is presented. If no benchmark is presented, the presentation must explain why no benchmark is disclosed. If the firm changes the benchmark that is used for a given composite in the performance presentation, the firm must disclose both the date and the reasons for the change. If a custom benchmark or combination of multiple benchmarks is used, the firm must describe the benchmark creation and rebalancing process.

5.B. *Recommendations*

5.B.1. The following items should be included in the composite presentation or disclosed as supplemental information:

(a) composite performance gross of investment management fees and custody fees and before taxes (except for non-reclaimable withholding taxes),

(b) cumulative returns for composite and benchmarks for all periods,

(c) equal-weighted means and median returns for each composite,

(d) volatility over time of the aggregate composite return, and

(e) inconsistencies among portfolios within a composite in the use of exchange rates.

5.B.2. Relevant risk measures—such as volatility, tracking error, beta, modified duration, etc.—should be presented along with total return for both benchmarks and composites.

III. VERIFICATION

The primary purpose of verification is to establish that a firm claiming compliance with GIPS has adhered to the standards. Verification will also increase the understanding and professionalism of performance-measurement teams and the consistency of presentation of performance results.

The verification procedures attempt to strike a balance between ensuring the quality, accuracy, and relevance of performance presentations and minimizing the cost to investment firms of independent review of performance results. Investment firms should assess the benefits of improved internal processes and procedures, which are as significant as the marketing advantages of verification.

The goal of the GIPS committee in drafting the verification procedures is to encourage broad acceptance of verification.

A. Scope and Purpose of Verification

1. Verification is the review of an investment management firm's performance-measurement processes and procedures by an independent third-party "verifier." Verification tests:
   A. Whether the investment firm has complied with all the composite construction requirements of GIPS on a firmwide basis, and
   B. Whether the firm's processes and procedures are designed to calculate and present performance results in compliance with the GIPS standards.

A single verification report is issued in respect to the whole firm; GIPS verification cannot be carried out for a single composite.

2. Third-party verification brings credibility to the claim of compliance and supports the overall guiding principles of full disclosure and fair representation of investment performance. Verification is *strongly encouraged* and is expected to become mandatory (but no earlier than 2005). Countries may require verification sooner through the establishment of local standards.
3. The initial minimum period for which verification can be performed is one year of a firm's presented performance. The recommended period over which verification is performed will be that part of the firm's track record for which GIPS compliance is claimed.
4. A verification report must confirm that
   A. the investment firm has complied with all the composite construction requirements of GIPS on a firmwide basis and
   B. the firm's processes and procedures are designed to calculate and present performance results in compliance with the GIPS standards.

Without such a report from the verifier, the firm cannot claim that its claim of compliance with GIPS has been verified.

5. After performing the verification, the verifier may conclude that the firm is not in compliance with GIPS or that the records of the firm cannot support a complete verification. In such situations, the verifier must issue a statement to the firm clarifying why a verification report was not possible.
6. A principal verifier may accept the work of a local or previous verifier as part of the basis for the principal verifier's opinion.
7. The minimum GIPS verification procedures are described in Section III(B), Required Verification Procedures.

B. Required Verification Procedures

The following are the *minimum* procedures that verifiers must follow when verifying an investment firm's compliance with GIPS. Verifiers must follow these procedures prior to issuing a verification report to the firm:

1. Pre-verification Procedures

A. *Knowledge of the Firm.* Verifiers must obtain selected samples of the firm's investment performance reports, and other available information regarding the firm, to ensure appropriate knowledge of the firm.

B. *Knowledge of GIPS.* Verifiers must understand the requirements and recommendations of GIPS, including any updates, reports, or clarifications of GIPS published by Investment Performance Council, the AIMR sponsored body responsible for oversight of the Global Investment Performance Standards.

C. *Knowledge of the Performance Standards*. Verifiers must be knowledgeable of country-specific performance standards, laws, and regulations applicable to the firm and must determine any differences between GIPS and the country-specific standards, laws, and regulations.

D. *Knowledge of Firm Policies*. Verifiers must determine the firm's assumptions and policies for establishing and maintaining compliance with all applicable requirements of GIPS. At minimum, verifiers must determine the firm's following policies and procedures of the firm:

- i. Policy with regard to investment discretion. The verifier must receive from the firm, in writing, the firm's definition of investment discretion and the firm's guidelines for determining whether accounts are fully discretionary.
- ii. Policy with regard to the definition of composites according to investment strategy. The verifier must obtain the firm's list of composite definitions with written criteria for including accounts in each composite;
- iii. Policy with regard to the timing of inclusion of new accounts in the composites.
- iv. Policy with regard to timing of exclusion of closed accounts in the composites.
- v. Policy with regard to the accrual of interest and dividend income.
- vi. Policy with regard to the market valuation of investment securities.
- vii. Method for computing time-weighted portfolio return.
- viii. Assumptions on the timing of capital inflows/outflows.
- ix. Method for computing composite returns.
- x. Policy with regard to the presentation of composite returns.
- xi. Policies regarding timing of implied taxes due on income and realized capital gains for reporting performance on an after-tax basis.
- xii. Policies regarding use of securities/countries not included in a composite's benchmark.
- xiii. Use of leverage and other derivatives.
- xiv. Any other policies and procedures relevant to performance presentation.

E. *Knowledge of Valuation Basis for Performance Calculations*. Verifiers must ensure that they understand the methods and policies used to record valuation information for performance calculation purposes. In particular, verifiers must determine that

- i. the firm's policy on classifying fund flows (e.g., injections, disbursements, dividends, interest, fees, taxes, etc. is consistent with the desired results and will give rise to accurate returns;
- ii. the firm's accounting treatment of income, interest, and dividend receipts is consistent with cash account and cash accruals definitions;
- iii. the firm's treatment of taxes, tax reclaims, and tax accruals is correct and the manner used is consistent with the desired method (i.e., gross- or net-of-tax return);
- iv. the firm's policies on recognizing purchases, sales, and the opening and closing of other positions are internally consistent and will produce accurate results; and
- v. the firm's accounting for investments and derivatives is consistent with GIPS.

2. Verification Procedures

A. *Definition of the Firm*. Verifiers must determine that the firm is, and has been, appropriately defined.

B. *Composite Construction*. Verifiers must be satisfied that

  i. the firm has defined and maintained composites according to reasonable guidelines in compliance with GIPS;

  ii. all of the firm's actual discretionary fee-paying portfolios are included in a composite;

  iii. the manager's definition of discretion has been consistently applied over time;

  iv. at all times, all accounts are included in their respective composites and no accounts that belong in a particular composite have been excluded;

  v. composite benchmarks are consistent with composite definitions and have been consistently applied over time;

  vi. the firm's guidelines for creating and maintaining composites have been consistently applied; and

  vii. the firm's list of composites is complete.

C. *Nondiscretionary Accounts.* Verifiers must obtain a listing of all firm portfolios and determine on a sampling basis whether the manager's classification of the account as discretionary or nondiscretionary is appropriate by referring to the account agreement and the manager's written guidelines for determining investment discretion.

D. *Sample Account Selection.* Verifiers must obtain a listing of open and closed accounts for all composites for the years under examination. Verifiers may check compliance with GIPS using a selected sample of a firm's accounts. Verifiers should consider the following criteria when selecting the sample accounts for examination:

  i. number of composites at the firm;

  ii. number of portfolios in each composite;

  iii. nature of the composite;

  iv. total assets under management;

  v. internal control structure at the firm (system of checks and balances in place);

  vi. number of years under examination; and

  vii. computer applications, software used in the construction and maintenance of composites, the use of external performance measurers, and the calculation of performance results.

  This list is not all inclusive and contains only the *minimum* criteria that should be used in the selection and evaluation of a sample for testing. For example, one potentially useful approach would be to choose a portfolio for the study sample that has the largest impact on composite performance because of its size or because of extremely good or bad performance. The lack of explicit record keeping or the presence of errors may warrant selecting a larger sample or applying additional verification procedures.

E. *Account Review*. For selected accounts, verifiers must determine

  i. whether the timing of the initial inclusion in the composite is in accordance with policies of the firm;

  ii. whether the timing of exclusion from the composite is in accordance with policies of the firm for closed accounts;

  iii. whether the objectives set forth in the account agreement are consistent with the manager's composite definition as indicated by the account agreement, portfolio summary, and composite definition;

  iv. the existence of the accounts by tracing selected accounts from account agreements to the composites;

  v. that all portfolios sharing the same guidelines are included in the same composite; and

  vi. that shifts from one composite to another are consistent with the guidelines set forth by the specific account agreement or with documented guidelines of the firm's clients.

F. *Performance-Measurement Calculation.* Verifiers must determine whether the firm has computed performance in accordance with the policies and assumptions adopted by the firm and disclosed in its presentations. In doing so, verifiers should

i. recalculate rates of return for a sample of accounts in the firm using an acceptable return formula as prescribed by GIPS (i.e., time-weighted rate of return) and

ii. take a reasonable sample of composite calculations to assure themselves of the accuracy of the asset weighting of returns, the geometric linking of returns to produce annual rates of returns, and the calculation of the dispersion of individual returns around the aggregate composite return.

G. *Disclosures.* Verifiers must review a sample of composite presentations to ensure that the presentations include the information and disclosures required by GIPS.

H. *Maintenance of Records*. The verifier must maintain sufficient information to support the verification report. The verifier must obtain a representation letter from the client firm confirming major policies and any other specific representations made to the verifier during the examination.

C. Detailed Examinations of Investment Performance Presentations

Separate from a GIPS verification, an investment management firm may choose to have a further, more extensive, specifically focused examination (or performance audit) of a specific composite presentation.

Firms cannot make any claim that a particular composite has been independently examined with respect to GIPS unless the verifier has also followed the GIPS verification procedures set forth in Section B. Firms cannot state that a particular composite presentation has been "GIPS verified" or make any claim to that effect. GIPS verification relates only to firmwide verification. Firms can make a claim of verification only after a verifier has issued a GIPS verification report.

To claim verification of a claim of compliance with the Standards, a detailed examination of a specific composite presentation is not required. Examinations of this type are *unlikely* to become a requirement of GIPS or become mandatory.

APPENDIX A.

SAMPLE PRESENTATION

XYZ Investment Firm Performance Results: Balanced Composite, January 1, 1995, through December 31, 1999

Year	Total Return (%)	Benchmark Return (%)	Number of Portfolios	Composite Dispersion (%)	Total Assets at End of Period (DM millions)	Percentage of Firm Assets	Total Firm Assets
1995	16.0	14.1	26	4.5	165	70	236
1996	2.2	1.8	32	2.0	235	68	346
1997	22.4	24.1	38	5.7	344	65	529
1998	7.1	6.0	45	2.8	445	64	695
1999	8.5	8.0	48	3.1	520	62	839

XYZ Investment Firm has prepared and presented this report in compliance with the Global Investment Performance Standards (GIPS).

Notes:

1. XYZ Investment Firm is a balanced portfolio investment manager that invests solely in German securities. XYZ Investment Firm is defined as an independent investment management firm that is not affiliated with any parent organization.
2. The benchmark: 30 percent DAX 100; 70 percent EFFAS Bund Index rebalanced monthly. Annualized compound composite return = 11.9 percent; annualized compound benchmark return = 11.4 percent.
3. Valuations are computed in German marks and from Reuters.
4. The dispersion of annual returns is measured by the standard deviation across asset-weighted portfolio returns represented within the composite for the full year.
5. Performance results are presented before management and custodial fees but after all trading commissions. The management fee schedule is attached.
6. This composite was created in February, 1995. No alteration of composites as presented here has occurred because of changes in personnel or other reasons at any time. A complete list of firm composites and performance results is available upon request.