



Legal Risk Management Tip June 2006

Performance Advertising

This is the second of five risk management tips addressing the process of building Internal Controls. As regulators review supervisory controls and annual review reports of broker-dealers and investment advisers during routine examinations, particular focus is given on whether the firm has identified risks (and possible risks) and connected them to its policies and procedures.

A common area that is frequently overlooked is enforcement of policies and procedures related to **performance advertising**. Has your firm created an inventory of risks associated with performance advertising and mapped those risks to firm policies and procedures? Moreover, has your firm conducted any tests to ensure that controls are in place to ensure accurate reporting of performance figures?

One simple way to test your internal controls is to request back-up documentation from the marketing department. Before going to print on any materials, check to see that performance numbers, NAVs and the like are properly calculated (if applicable) and transposed to firm marketing materials.

For those advisory firms who claim compliance with GIPS®, consider assessing these areas to help ensure you are satisfying the Gold GIPS requirements for compliant presentations.

1. How is the firm striving to make reasonable efforts to provide a compliant presentation to its prospective clients?
2. Can the firm supply within 24-hours (i.e., reasonable time) a complete list and description of all the firm's composites?
3. Does the firm have a current list and description of all composites that have been discontinued for at least five years after discontinuation?
4. Does the firm have available a compliant presentation for each of its composites listed?

Conducting in-depth analyses such as these will help to identify "gaps" that may exist in the compliance program and will validate that the firm is capturing the necessary internal control information.

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