

Navigating the SEC Marketing Rule: Common Pitfalls & Best Practices

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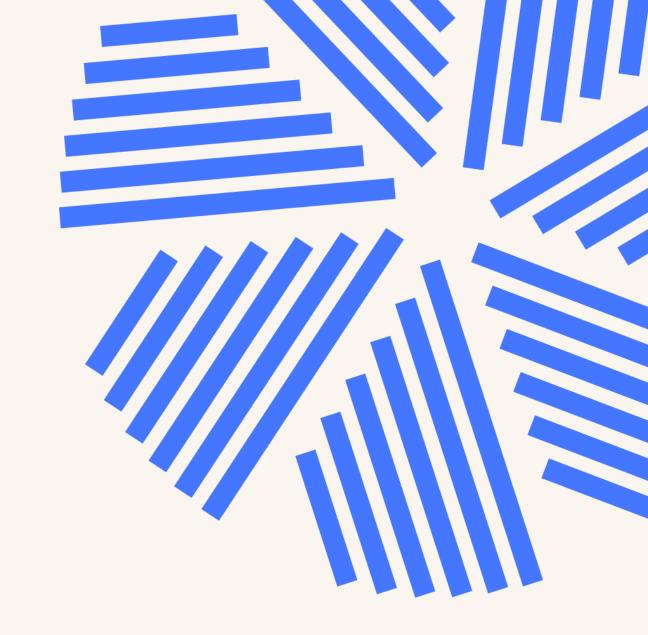
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Agenda

- Where We Stand Today
- Net Performance: When & How
 - New Marketing Rule FAQs
 - FN 590
- Comparing the Marketing Rule and the GIPS standards
 - Carve Outs/Extracted Performance
 - Performance Portability



Where We Stand Today

Dec. 22, 2020 SEC Adopts the Marketing Rule May 4, 2021 Marketing Rule becomes Effective Sept. 19, 2022 EXAMS Risk Alert highlighting Marketing Rule focus areas Feb. 6, 2024
SEC Staff FAQ
Issued:
Subscription
Lines of Credit

March 19, 2025 SEC Staff FAQs Issued: Extracts & Portfolio Characteristics

Jan. 1, 2020 Effective Date for 2020 Edition of the GIPS Standards Nov. 4, 2021 Marketing Rule Compliance Date

Aug. 21, 2023
First Marketing
Rule enforcement
action

April 17, 2024
EXAMS Risk
Alert sharing
Marketing Rule
observations































Question: When is Net Performance Required?

Answer: Any time Gross Performance is included in an advertisement!

Key requirements when including net performance:

- Presentation
- Calculation
- Time Period

This applies to any presentation of any type of gross performance in an advertisement, except...



New Marketing Rule FAQs

Extracted performance may be shown on a gross only basis *if*:

- The extract is clearly identified as gross of fees;
- The performance of the portfolio or composite from which the extract was derived is also presented:
 - Consistent with the requirements of the Marketing Rule;
 - On a gross and net basis, to demonstrate the effect of fees;
 - With at least equal prominence to and in a manner designed to facilitate comparison with the extract; and
 - Over a period of time that includes the entire period over which the extract is calculated.

Portfolio or investment characteristics may be shown on a gross only basis *if*:

- The characteristic is clearly identified as gross of fees;
- The performance of the portfolio or composite from which the characteristic was derived is also presented:
 - Consistent with the requirements of the Marketing Rule;
 - On a gross and net basis, to demonstrate the effect of fees;
 - With at least equal prominence to and in a manner designed to facilitate comparison with the characteristic; and
 - Over a period of time that includes the entire period over which the characteristic is calculated.

New Marketing Rule FAQs: Challenging Scenarios

Can extracts or characteristics of hypothetical performance be presented on a gross-only basis?

- Clearly, some hypothetical performance can be; see footnote 1.
- Does it play out differently for different types of hypothetical performance?
 - Backtests
 - Projections
 - Models
 - Composites of Extracts and Extracts of Composites
- Considerations
 - What does the Commission/Staff care about?
 - Is what is shown meaningful?

Can extracts or characteristics of predecessor performance be shown on a gross-only basis?

- Are you also in compliance with the predecessor performance requirements?
- Potential overlap with hypothetical performance
- Considerations
 - Higher-risk presentations?
 - What does the Commission/Staff care about?

Net Performance: Actual vs. Model Fees

Net performance may be calculated by deducting:

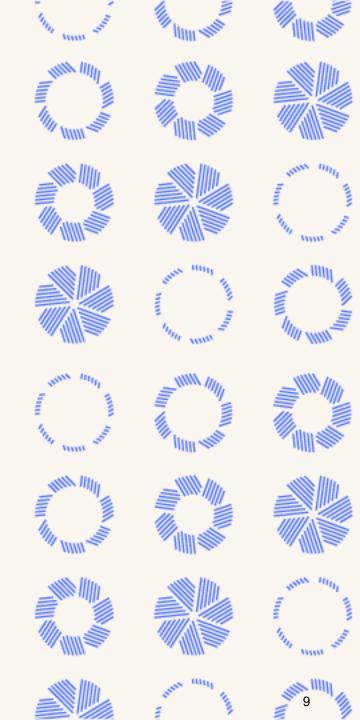
- The actual fees a client or investor has paid or would have paid; or
- A model fee if:
 - Doing so would result in performance figures that are no higher than if the actual fee had been deducted; or
 - Equal to the highest fee charged to the intended audience to whom the advertisement is disseminated



Net Performance: Footnote 590

Adopting Release FN 590

"If the fee to be charged to the intended audience is anticipated to be higher than the actual fees charged, the adviser <u>must</u> use a model fee that reflects the anticipated fee to be charged in order not to violate the rule's general prohibitions."



Carve-Outs and Extracted Performance

MARKETING RULE

- Extracted performance can be a subset of any investments from a portfolio
- Must present (or for private fund advertisements, offer to provide) performance of the total portfolio the extracted performance is pulled from
- A composite of carve outs is treated as hypothetical performance

GIPS STANDARDS

- Carve-outs must be representative of a distinct investment strategy
- Do not need to present performance of the total portfolio that carve-out performance is taken from
- A composite may include carve-outs



Marketing Rule: Performance Portability

Predecessor performance may be shown provided that:

- Person(s) primarily responsible for achieving prior performance results continue to manage accounts at the advertising adviser
- Accounts managed at predecessor adviser are sufficiently similar to accounts managed at advertising adviser
- All accounts managed in a substantially similar manner are advertised unless
 exclusion of any account would not result in materially higher performance or alter the
 presentation of any prescribed time periods
- Advertisement clearly and prominently includes all relevant disclosures and indicates performance results were from accounts managed at another entity



GIPS Standards: Performance Portability

Prior firm performance may be used and linked to the acquired firm's performance if:

- Substantially all of the investment decision makers are employed by the new or acquiring firm
- The decision-making process is substantially intact and independent within the new or acquiring firm
- The new or acquiring firm has records to support the performance
- There is no break in the track record between the past firm or affiliation and the new or acquiring firm



Marketing Rule vs. GIPS Standards

MARKETING RULE

If the portability tests are no longer met because the person(s) primarily responsible for achieving the prior performance no longer manage accounts, the ported performance should not be used

GIPS STANDARDS

Once the portability tests are met, the prior performance becomes the performance of the new or acquiring firm and can always be used











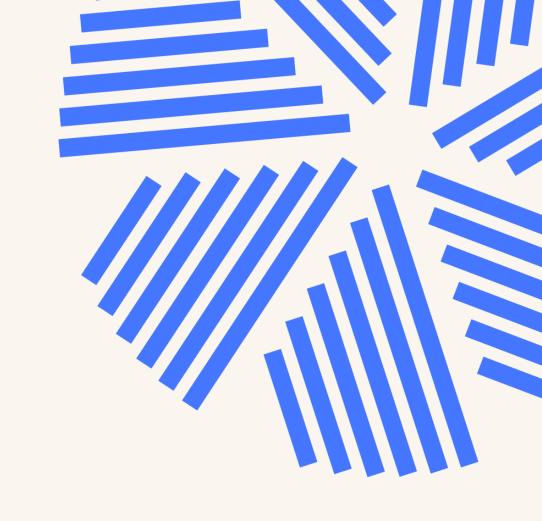








Questions?



Thank you!

