



FEBRUARY 10, 2023

For more information,
contact:

Conrad C. Axelrod
caxelrod@kslaw.com

Douglas J. Elsbeck
delsbeck@kslaw.com

Kathryn M. Furman
kfurman@kslaw.com

C. Spencer Johnson III
csjohnson@kslaw.com

Jennifer M. Morgan
jmorgan@kslaw.com

John D. Wilson
jdwilson@kslaw.com

Russell D. Sacks
rsacks@kslaw.com

Steven R. Blau
sblau@kslaw.com

P. Sean Kelly
sean.kelly@kslaw.com

Steve Zavodnick
szavodnick@kslaw.com

KING & SPALDING

Atlanta
1180 Peachtree Street, NE
Atlanta, Georgia 30309-3521

New York
1185 Avenue of the Americas
New York, New York
10036-4003

SEC Staff Addresses Net Performance Presentation Requirements for Single Investments Under Marketing Rule

On January 11, 2023, the SEC Staff published a question-and-answer in its Marketing Compliance FAQs¹ that addresses whether an advertisement that includes gross performance information for a single investment (or group of investments) must also present net performance for such investment(s). The guidance addresses a question on which there had been a diversity of views, and represents the SEC Staff's first addition to its Marketing Rule FAQs since the Marketing Rule's November 4, 2022 compliance date.²

THE FAQ'S GUIDANCE RE NET PERFORMANCE REQUIREMENTS FOR SINGLE INVESTMENTS/GROUP OF INVESTMENTS

The addition to the FAQs is as follows:

“Q: *When an adviser displays the gross performance of one investment (e.g., a case study) or a group of investments from a private fund, must the adviser show the net performance of the single investment and the group of investments?*

A. *Yes. The staff believes that displaying the performance of one investment or a group of investments in a private fund is an example of extracted performance under the new marketing rule.³ Because the extracted performance provision was intended, in part, to address the risk that advisers would present misleadingly selective profitable performance with the benefit of hindsight, the staff believes the provision should be read to apply to a subset of investments (i.e., one or more). Accordingly, an adviser may not show gross performance of one investment or a group of investments without also showing the net performance of that single investment or group of investments, respectively.⁴ In addition, the adviser must satisfy the other tailored disclosure requirements as well as the*



*general prohibitions, including the general prohibition against specific investment advice not presented in a fair and balanced manner, when showing extracted performance.*⁵

With the addition of this question-and-answer to the FAQs, the market now has the SEC Staff’s formal view with respect to whether, if an advertisement presents gross performance information for a single investment, net performance information must also be presented.

However, the SEC Staff did not take the opportunity to provide guidance with respect to the *calculation* of net performance information for a single investment or a group of investments, including what methodologies are acceptable to SEC Staff. Advisers will need to address the considerable questions presented by calculation of net performance of specific investments, including how to apply to a single investment the carried interest or other incentive compensation that is often applied at the fund level.

CONCLUSION

This guidance represents the SEC Staff’s first addition to the Marketing Rule FAQs since the compliance date, and reflects the SEC Staff’s attention to Marketing Rule implementation, including through the examination process. While the SEC Staff addressed one question that had been on the marketplace’s mind, many others remain.

In addition to the Marketing Rule, there are many other items of interest to private fund advisers on the SEC’s Regulatory Flexibility Agenda, including amendments to Form PF and the proposed Private Fund Adviser rulemaking,⁶ both slated in the Agenda for final action by April 2023.

Should you have any questions regarding this alert, please feel free to contact your King & Spalding contact or any of the authors.

ABOUT KING & SPALDING

Celebrating more than 130 years of service, King & Spalding is an international law firm that represents a broad array of clients, including half of the Fortune Global 100, with 1,200 lawyers in 23 offices in the United States, Europe, the Middle East and Asia. The firm has handled matters in over 160 countries on six continents and is consistently recognized for the results it obtains, uncompromising commitment to quality, and dedication to understanding the business and culture of its clients.

This alert provides a general summary of recent legal developments. It is not intended to be and should not be relied upon as legal advice. In some jurisdictions, this may be considered “Attorney Advertising.” View our [Privacy Notice](#).

ABU DHABI	ABU DHABI	ABU DHABI	ABU DHABI	ABU DHABI	ABU DHABI
ATLANTA	ATLANTA	ATLANTA	ATLANTA	ATLANTA	ATLANTA
AUSTIN	AUSTIN	AUSTIN	AUSTIN	AUSTIN	AUSTIN
BRUSSELS	BRUSSELS	BRUSSELS	BRUSSELS	BRUSSELS	BRUSSELS



¹ The FAQs are available at <https://www.sec.gov/investment/marketing-faq>.

² For an in-depth analysis of the obligations imposed on RIAs by the Marketing Rule, please refer to the [King & Spalding Client Alert](#) that was published on March 22, 2022.

³ The footnote to the FAQ is as follows: “[1] Extracted performance means “the performance results of a subset of investments extracted from a *portfolio*.” Rule 206(4)-1(e)(6). See section II.E.5 of the adopting release.”

⁴ The footnote to the FAQ is as follows: “[2] The rule prohibits any presentation of gross performance in an advertisement unless the advertisement also presents net performance. See section II.E.1 of the adopting release. The gross and net performance requirement applies to not only an entire portfolio but also to any portion of a portfolio that is included in extracted performance. See sections II.E.1(a) and (b) and the definitions of gross and net performance in rule 206(4)-1(e)(7) and (10) (“*Net performance* means the performance results of a *portfolio* (or portions of a portfolio that are included in *extracted performance*...”). The adopting release also states that the rule requires that advisers that show extracted performance must show net and gross performance for the applicable subset of investments extracted from a portfolio. See section II.E.1.a. of the adopting release (discussing gross performance).”

⁵ The footnote to the FAQ is as follows: “[3] The adopting release states that “advisers should evaluate the particular facts and circumstances that may be relevant to investors, including the assumptions, factors, and conditions that contributed to the performance, and include appropriate disclosures or other information such that the advertisement does not violate the general prohibitions...or other applicable law.” See section II.E.1 of the adopting release (discussing the net performance requirement). In addition, it would be considered “misleading under the final rule to present extracted performance in an advertisement without disclosing whether it reflects an allocation of the cash held by the entire portfolio and the effect of such cash allocation, or of the absence of such an allocation, on the results portrayed.” See section II.E.5 of the adopting release (discussing extracted performance).”

⁶ For more information on the proposed Private Fund Adviser rule, please refer to the [King & Spalding Client Alert](#) that was published on February 24, 2022.