

# KIRKLAND & ELLIS

Kirkland AIM

## SEC Releases Marketing Rule FAQ on Private Fund Net Performance

12 January 2023

More than two months after the effective date of the SEC's amended Marketing Rule, the Staff of the Division of Investment Management released on January 11, 2023, a [Frequently Asked Question](#) regarding the presentation of gross and net performance in advertisements governed by the Marketing Rule.

The FAQ, reproduced in its entirety below, states the view of the Staff that an SEC-registered 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. The FAQ cites the example of showing a gross return in a case study, which the Staff indicated would also require a net return as extracted performance. While the new guidance did not specifically refer to the standalone presentation of realized or unrealized investment performance, presentation of such performance would be expected to present similar issues.

The FAQ did not directly address interpretive questions regarding performance in traditional private fund investment tables, in which gross performance of all individual transactions within a private fund, rather than a subset or group of investments, is presented directly above fund-level gross and net performance. Despite the remaining interpretive gaps, SEC-registered advisers should take note of the SEC's restatement of its focus in the area when presenting gross performance results. Please reach out to your usual Kirkland regulatory contact with any questions.

The full text of the FAQ 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.<sup>[1]</sup> 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.<sup>[2]</sup> 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.<sup>[3]</sup>

*[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.*

*[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).*

*[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).*

## Related Professionals

Norm Champ, P.C.

Partner / New York

Scott A. Moehrke, P.C.

Partner / Chicago

Diane Blizzard

Partner / Washington, D.C.

Michael Chu

Partner / Chicago

Matthew Cohen

Partner / Bay Area – San Francisco / Los Angeles – Century City

Melissa S. Gainor

Partner / Washington, D.C.

Phil Vincent Giglio

Partner / Chicago

Nicholas A. Hemmingsen

Partner / Chicago

Xiao-Hong Jing

Partner / New York

Daniel Kahl

Partner / Washington, D.C.

Alpa Patel, P.C.

Partner / Washington, D.C.

Eric L. Perelman

Partner / New York

Noah Qiao

Partner / New York

John T. Reinert

Partner / Chicago

Nabil Sabki, P.C.

Partner / Chicago

Reed T. Schuster

Partner / Austin / Chicago

Christopher J. Scully

Partner / Chicago

Ryan P. Swan

Partner / Chicago

Josh Westerholm, P.C.

Partner / Chicago

Jina K. Yun

Partner / Chicago

# Related Services

## Practices

- Investment Funds

## Suggested Reading

- 12 December 2022 Kirkland AIM SEC Continues Enforcement Scrutiny of ESG Claims by Investment Advisers
- 15 November 2022 Kirkland AIM SEC Proposes New Rules on Adviser Oversight of Service Providers
- 03 June 2022 Kirkland AIM SEC Proposes Enhanced Disclosure by Certain Advisers on ESG Investment Practices

This publication is distributed with the understanding that the author, publisher and distributor of this publication and/or any linked publication are not rendering legal, accounting, or other professional advice or opinions on specific facts or matters and, accordingly, assume no liability whatsoever in connection with its use. Pursuant to applicable rules of professional conduct, portions of this publication may constitute Attorney Advertising.

© 2023 Kirkland & Ellis LLP.