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## *SEC Issues Updated FAQ on Marketing Rule*

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Recently published guidance by the SEC staff from the Division of Investment Management (the "Staff") is likely to have a significant impact on marketing materials prepared by investment advisers marketing new private funds. The link to the guidance, which appeared in updated FAQs (the "FAQ") by the Staff, is linked here: <https://www.sec.gov/investment/marketing-faq>.

The FAQ clarifies the SEC's perspective that prior performance of a single investment in a private fund (commonly referred to in the industry as "deal by deal returns") is an example of "extracted performance" under the new Marketing Rule, meaning that an adviser may not show gross performance of a single investment without also showing the net performance of that single investment. The FAQ references performance of single investments in a private fund but does not clarify whether the SEC's views extend to managed accounts, single-investment funds or other types of investment vehicles/accounts.

This guidance is at odds with the preliminary understanding of many industry participants, including many law firms, that the performance of single investments was not intended to be treated as "extracted performance" and thus, while subject to the "fair and balanced" requirement of the new Marketing Rule, would not be subject to the requirement to show net performance alongside the gross equivalent.

Prior to the FAQ, many industry participants believed that showing gross performance for single investments (deal by deal returns) would be acceptable under the Marketing Rule if the impact on performance of fund level fees (including management fees), expenses and carried interest/other performance compensation was clearly included elsewhere in the applicable document or presentation. This was often accomplished by presenting the gross and net performance of the applicable fund (commonly referred to in the industry as "fund level returns") in the same presentation. The FAQ instead requires investment advisers to present the net performance for deal by deal returns even if the track record presentation separately demonstrates the effect of fund level fees, expenses and carried interest on fund level investor returns. This effectively requires advisers to apply model fees and expenses to individual investments (and, therefore, disclose details regarding the assumptions underlying such model fees and expenses).

While the Staff's guidance is not binding on the Commission, and should not be considered as having the same force and effect as an SEC rule adopted under the Administrative Procedures Act, the guidance does provide insight as to how the Staff will interpret and enforce the Marketing Rule. The Paul Hastings investment funds team is actively working with clients to address this new guidance. As a reminder, compliance with the Marketing Rule was required beginning November 4, 2022.



*If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings New York lawyers:*

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