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February 10, 2020

Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

*Via Electronic Filing*

Re: Proposed Commission Amendments to Rule 206(4)-1 and Form ADV; Request for Comment on Enhancing Investment Adviser Regulation; Rel. No. IA- 5407; File No. S7-21-19

Dear Ms. Countryman:

Ropes & Gray, LLP appreciates the opportunity to provide these comments to the Commission on the above-referenced matters.

Our firm represents the interests of many asset management firms that are registered with the Commission as investment advisers, including a wide range and significant number of investment management, hedge and private equity firms. The proposed amendments to Rule 206(4)-1 (the "Advertising Rule") addresses certain principles, prohibitions, limitations and requirements for investment advisers in the creation and distribution of marketing materials and thus would directly apply to our investment advisory clients. Given this fact, we are writing to provide our views on aspects of the proposed Advertising Rule. The comments expressed herein reflect the views of the undersigned, as practitioners with many years of experience in providing legal counsel to a wide variety of asset management firms. These comments and opinions are not intended to represent the views of our clients.

1. The "Principles-Based" Approach to the Advertising Rule Is Beneficial to Investment Advisers and Their Prospective Clients and Investors and Should Be Further Expanded

We strongly agree with the Commission that a shift towards a "principles-based approach" to the advertising requirements would be beneficial to investment advisers and allow investment advisers to tailor advertisements more appropriately to their business, their investment products and their prospective clients and investors. In the proposing release, the Commission accurately recognizes that due to the evolution of the asset management industry since the adoption of the current Advertising Rule (including, for instance, changes in methods of communication and technology, the expectation of investors utilizing investment advisory services, and the nature of the investment advisory industry), a principles-based approach to the advertising requirements would allow

investment advisers to provide more useful and valuable information to investors.[1] We further agree that the breadth of the current Advertising Rule's *per se* violations and lack of clear guidance relating to presentation of performance in particular has presented compliance challenges and can have a limiting effect on investment adviser transparency and communications with investors.[2]

Thus, while we strongly endorse the principles-based approach introduced by the Commission, we would respectfully suggest that the proposed Advertising Rule could be further improved by removing or revising several of the more technical and rigid requirements included therein (in particular, in instances where it could have the effect of chilling communications and transparency to investors), and further focusing the Advertising Rule on general principles to guide investment advisers' practices. We have highlighted several of these instances below.

*a. The Requirement to "Clearly and Prominently" Disclose Material Risks and Other Limitations in All Advertising Materials Should Be Removed*

The proposed Advertising Rule sets forth a number of general prohibitions on certain advertising practices in order to prevent fraudulent, deceptive or manipulative acts, including a prohibition on "[A]dvertisements that discuss or imply any potential benefits connected with or resulting from the investment adviser's services or methods of operation *without clearly and prominently* discussing associated material risks or other limitations associated with the potential benefits."[3] In the proposing release, the Commission further notes that, for instance, a hyperlink to relevant disclosures would be unacceptable because it may not be viewed or acknowledged by investors and, as a result, investors may not receive all information necessary to make an informed investment decision.[4]

While we agree that the material risks involved with utilizing an investment adviser's services are important and necessary for evaluating and making informed investment decisions, we would respectfully suggest that the requirement in the proposed Advertising Rule goes beyond what is necessary or helpful for prospective investors. Instead, we would suggest that so long as a prospective investor receives all relevant disclosures at some point prior to entering into a contract with the investment adviser or making an investment in a private fund, then the investor has received all information necessary to make an informed investment decision. Indeed, the practice of including material risks in all advertising

[1] *See* Proposed Rules for Investment Adviser Advertisements; Compensation for Solicitations, 84 Fed. Reg. 67518, 67520 (proposed Dec. 10, 2019)("Proposed Rules") (to be codified at 17 C.F.R. Pts. 275, 279).
[2] *See id.* at 67520.
[3] *Id*. at 67533-34 (footnotes omitted)(emphasis added).
[4] *See id*. at 67534.

materials would likely result in a prospective investor receiving a substantial amount of duplicative information and would represent a potential departure from industry practice.

The disclosure of material risks and other limitations associated with making an investment in a private fund is common practice in certain advertising materials (for instance, private placement memoranda and due diligence questionnaires). However, inclusion of this sort of lengthy disclosure would be less useful for investors and more burdensome for investment advisers in other contexts (e.g., shorter marketing communications that would be transformed into long and unwieldy documents).

Further, we would note this requirement would be redundant of other obligations of investment advisers. In particular, the Commission requires in Item 8 of Form ADV Part 2A that investment advisers specifically disclose the risk of loss and material risks.[5] Item 8 requires, among other things, that investment advisers (i) disclose that investing in securities involves risk of loss that clients should be prepared to bear, (ii) for each investment strategy or method of analysis, explain the material risks involved, and (iii) describe the material risks involved with a particular security.[6] Form ADV Part 2A is required to be delivered to clients prior to entering into a contract with the investment adviser or making an investment in a private fund. In addition, investors in private funds generally receive the Form ADV Part 2A prior to making an investment and/or receive a private placement memorandum with such risks described.

We would respectfully recommend that the Commission remove this requirement altogether or alternatively, revise this requirement such that a prospective investor must receive clear and prominent disclosure of any associated material risks or other limitations associated with the potential benefits of an investment adviser's services or methods of operation *at any point* prior to entering into a contract with the investment adviser or making an investment in a private fund (clarifying that such disclosure need not be attached to every advertisement distributed to a prospective investor). If the Commission is reluctant to adopt this standard for all investors, we would respectfully request the Commission consider this more flexible requirement with respect to "Non-Retail Persons," as these investors have the sophistication and resources necessary to understand that shorter marketing materials do not disclose all material risks associated with utilizing an investment adviser's investment advisory services and are more able to evaluate an investment product based on the fulsome materials it receives and reviews prior to entering into a contract with the investment adviser or making an investment in a private fund.

[5] *See* Instructions for Part 2A of Form ADV.
[6] *See id.*

*b. The Proposed Prohibition of Showing Time-Based Performance Results in Retail Advertisements Should Be Removed*

The proposed Advertising Rule provides that, for advertisements provided to "Retail Persons," investment advisers would be prohibited from showing performance results for a particular fund/portfolio, unless the performance results for the same fund/portfolio for 1-, 5-, and 10-year periods were each shown with equal prominence and ending on the most recent practicable date (with an exception for portfolios not in existence during that particular period).[7] While the Commission notes that it currently requires average annual total returns for the same periods of time in advertisements with respect to securities of certain registered investment companies and business development companies,[8] the proposed Advertising Rule fails to take into consideration other financial metrics used by many investment advisers for which such time-based calculations are not easily determinable. For instance, internal rates of return (or "IRR") used by private equity managers and many other private fund managers, unlike many other performance calculations, have a "time-based" component, essentially allowing investors to understand how much capital is returned and how quickly that capital is returned. By way of example, two investments can reflect the same "multiple on invested capital," yet can have two different IRRs depending on the speed at which the capital was returned to an investor. The faster capital was returned to an investor would be reflected in a higher IRR.

For illiquid, closed-end funds with a diverse portfolio (like private equity funds) that do not offer periodic distributions or redemption rights, this time-based component to the calculation is innately valuable and more useful to investors than other financial performance. In addition, IRRs is the performance metric that general partners typically present and investors expect to see in order to appropriately evaluate an investment. IRR is just one example of alternative forms of performance measurements that investment advisers use instead of a 1-, 5-, and 10-year track record that provides valuable information to their potential clients. As a result, this requirement could create confusion to investors and introduces questions for investment advisers who have historically presented financial metrics that would fail to comply with the proposed Advertising Rule (i.e., would an investment adviser be required to calculate returns on another basis that it has determined to be less meaningful and relevant just to comply with this requirement?). If this aspect of the Advertising Rule is adopted as proposed, we foresee that many investment advisers may elect to present both time-based performance metrics and traditional metrics (e.g., IRR and multiples of invested capital), which could result in greater confusion for investors.

[7] *See* proposed rule 206(4)-1(c)(2)(ii).
[8] *See* 17 C.F.R. §230.482(d)(3).

While we agree with the Commission that this time-based requirement does prevent investment advisers from including in Retail Advertisements only recent performance results, or cherry picking strong performance years,[9] we would respectfully suggest that this stringent requirement is unnecessary in light of the general principles of the proposed Advertising Rule, specifically the principle that investment advisers show investments in a "fair and balanced" manner designed to give prospective investors a complete picture of a fund/portfolio. This principle inherently extends to the presentation of performance information. In fact, the Commission explicitly notes that the prohibitions in paragraph (a) of the proposed Advertising Rule (e.g., to present performance time period in a manner that is not fair an balanced)[10] would still apply to presentaton of performance across the required time periods.[11] Thus, even absent this time period requirement, we believe there are many forms in which performance information can be presented while still being "fair and balanced."

Relying on general principles and permitting investment advisers to determine how best to present performance information in a "fair and balanced" way allows investment advisers to continue calculating investment performance in a manner they determine to be most relevant and useful, which provides appropriate information to investors and does not unduly burden investment advisers. Therefore, in lieu of a prescriptive requirement with which it would be burdensome for many investment advisers to comply, we would suggest the Commission instead highlight various examples to provide guidance as to what it believes would satisfy the "fair and balanced" criteria (for instance, the time period requirement, or presentation of all investment performance in a fund/portfolio, etc.).

*c. The Requirement to Show All "Related Performance" Should Be Removed*

The proposed Advertising Rule prohibits the inclusion of any "related performance" (i.e., performance results of any other funds/portfolios managed by an investment adviser with substantially similar investment policies, objectives, and strategies as those of the funds/services being offered or promoted) in an advertisement without inclusion of the performance of *all* related funds/portfolios.[12] While the Commission notes that this restriction is "intended to prevent investment advisers from including only related portfolios having favorable performance results or otherwise "cherry-picking[.],"[13] we would respectfully suggest that this constraint is unnecessary in light of the proposed Advertising

[9] *See* Proposed Rules, 84. Fed. Reg. at 67553.
[10] *See* proposed rule 206(4)-1(a)(6).
[11] *See* Proposed Rules, 84 Fed. Reg. at 67553.
[12] *See* proposed rule 206(4)-1(c)(1)(iii); *id*. At 67556.
[13] Proposed Rules, 84 Fed. Reg. at 67556

Rule's principles-based restriction requiring investment adviser present specific investment advice in a manner that is "fair and balanced."[14]

Indeed, removal of this fixed requirement would instead allow investment advisers the flexibility to tailor the way they present specific investment advice (including performance thereof) in a manner that satisfies the "fair and balanced" test, and would be more consistent with the principles-based approach. For instance, investment advisers to multiple successor funds with sophisticated investors often choose to present only the performance information of more recent funds/portfolio, as they find it to be more relevant and helpful for investors (due to investment professional turnover from early funds/portfolios and/or changed market conditions, such older fund/portfolio performance may be less relevant than those of the later funds/portfolios). By way of a specific example, an investment adviser fundraising for "Fund XV" may only provide performance for Funds V-XIV, determining the performance information for much earlier vintages (e.g., Funds I-IV) to be less relevant to prospective investors (and, in fact, may be misleading if there have been significant changes in investment personnel or investment focus). With the "fair and balanced" standard to guide them, investment advisers are in a better position to determine what performance information is relevant to evaluate an investment in a private fund and appropriately disclose any differences or explanation that would help an investor better understand how and why the information may (or may not) be relevant.

Furthermore, we believe that removing the requirement to present all "related performance" would not, in and of itself, permit an investment adviser to present only the best or most favorable performance to prospective investors, because the proposed Advertising Rule contains other safeguards that prevent investment advisers from showing information in an imbalanced and misleading manner. In fact, as the Commission appropriately notes in the proposing release, the principles-based approach "allow[s] investment advisers to better tailor the information that they include in advertisements that contain references to specific investment advice in a manner that does not mislead investors." [15] We further agree with the Commission's additional explanation as to how "fair and balanced" should be determined, noting that "[I]nstead of including a requirement for a particular presentation, advisers, when determining how to present this information in a fair and balanced manner, should consider the facts and circumstances of the advertisement, including the nature and sophistication of the audience."[16]

Therefore, we would respectfully suggest that so long as an investment adviser is presenting performance information in a manner that is "fair and balanced" consistent with the general

[14] *See* proposed rule 206(4)-1(a)(6); *id*. at 67534.
[15] Proposed Rules, 84 Fed. Reg. at 67534.
[16] *Id*. at 67535.

principles of the proposed Advertising Rule and the advertisement contains appropriate and clear disclosure about the funds/portfolios that are excluded, an investment adviser should not be required to present *all* related funds/portfolio in the advertisement.

*d. The Requirement to Adopt Policies and Procedures "Reasonably Designed to Ensure that Hypothetical Performance is Relevant" Should Be Removed*

The proposed Advertising Rule provides that an investment adviser may present hypothetical performance (which includes targeted returns and projections) subject to certain conditions, including (among other things) that the investment adviser adopts and implements policies and procedures that are "reasonably designed to ensure that hypothetical performance is relevant to the financial situation and investment objectives" of the recipient.[17] We believe this requirement would unjustifiably burden investment advisers of private funds, as private fund advisers are often not equipped with detailed information about investors' financial situation and investment objectives, especially prior to submitting subscription documentation. Although private fund investors are typically subject to certain wealth and/or income standards,[18] a private fund adviser often has no visibility into, or knowledge of, such investor's overall financial situation and investment objectives. Further, investors may be unwilling to provide such information prior to receiving the materials it deems necessary to evaluate an investment in the private fund. As a result, this restriction would prohibit private fund advisers from providing useful and valuable information to prospective investors that would assist them in their evaluation of a fund investment.

In the proposing release, the Commission recognizes that hypothetical performance is a useful tool to prospective investors, allowing them to more fully evaluate an investment adviser's strategies, services, and investment process and understand how investments may perform under differing market conditions.[19] In addition, targeted returns and projections prepared in a "fair and balanced" manner that are properly disclosed can assist a prospective investor in evaluating its own portfolio and diversification needs.

Removal of this specific requirement would not result in investment advisers' carte blanche ability to show hypothetical performance in an unrestrained manner, because investment advisers would still have to adhere to other conditions and safeguards, which would prevent the information from being presented in a misleading manner. In fact, the proposed Advertising Rule includes two additional requirements, including the requirement to provide sufficient information to enable the recipient to understand how the hypothetical

[17] *Id*. at 67562.
[18] *See* 17 C.F.R. §230.501(a) (defining "accredited investor");17 C.F.R. §275.205-3 (defining "qualified client"); 15 U.S.C. §80a-2(a)(51) (defining "qualified purchaser").
[19] *See* Proposed Rules, 84 Fed. Reg. at 67560.

performance was calculated (such as the various criteria and assumptions used) and the requirement to provide (or in the case of a Non-Retail Person, offer to provide promptly) a description of the risks and limitations in using hypothetical performance, both of which we believe provide sufficient protection and information to investors and are more consistent with the principles-based approach.[20] Therefore, we would respectfully request the Commission remove the requirement to adopt these policies and procedures and instead, consistent with the principles-based approach, rely on the additional two requirements set out in the proposed Advertising Rule, which allow investment advisers more flexibility in determining what information is necessary in order to present hypothetical performance in a "fair and balanced" manner, taking into account a prospective investor's sophistication and resources to analyze such information.

2. The Definition of "Advertising" Should Not Include Reports to Current Investors That Include the Adviser's Own Market Commentary or Discussion of an Adviser's Investing Thesis

The Commission has generally taken the position that "[W]ritten communications by advisers to their existing clients about the performance of the securities in their accounts are not offers of investment advisory services but are part of the adviser's advisory services."[21] Consistent with this guidance, we believe that many investment advisers have historically not treated normal-course, periodic investor reports (e.g., quarterly and annual investor reports) as "Advertising." However, under the proposed Advertising Rule, reporting to current investors is more likely to be "Advertising." While the Commission notes that usual communications to an existing investor relating to specific information about an investor's account would not generally be for promoting the adviser's services or to retain investors, the Commission goes on to say that "[A] communication to existing investors that includes the adviser's own market commentary or a discussion of the adviser's investing thesis may be considered to be "offering or promoting" the adviser's services depending on the facts and circumstances of the relevant communication."[22] We believe this clarification would require investment advisers to subject periodic investor reporting that includes the adviser's own market commentary or discussion of an adviser's investment thesis to "Advertising" review and compliance, which would likely result in investment advisers removing valuable information from their periodic reports.

Investment advisers routinely include market information and commentary, as well as information about their investment theses, in communications to existing investors for a variety of reasons, which are generally deemed to be beneficial and useful by investors. This type of information provides market and industry context and can assist investors in understanding financial and economic conditions more generally (and changes therein), industry analyses, as well as

[20] *See id*. at 67564.
[21] *See* Investment Counsel Association of America, Inc., SEC Staff No-Action Letter (Mar. 1, 2004)
[22] Proposed Rules, 84 Fed. Reg. at 67526.

information about their own portfolio investments (for instance, portfolio concentration, holding periods, etc.). This information is generally not intended by investment advisers to "promote" their services, but instead is offered as a benefit to investors, to educate them and provide valuable insight into certain areas in which the investment adviser has expertise and provide context for investment performance over time. We believe the expansion of the definition of "Advertising" would inhibit these communications and disadvantage existing investors because investment advisers may be more reluctant to share such valuable information with existing investors, which would ultimately result in less transparent communications to investors.

Due to the benefits such information can provide to investors, we would respectfully suggest the Commission clarify that ordinary-course, periodic reports provided to existing investors that include the adviser's own market commentary or discussion of an adviser's investing thesis are not designed to obtain or retain investors and, therefore, are exempted from the definition of "Advertising."[23]

3. The Definition of "Advertising" Should Not Include Reports Required by Publicly Traded Investment Advisers

The proposed Advertising Rule accurately exempts from the definition of "Advertising" "[a]ny information required to be contained in a statutory or regulatory notice, filing, or other communication."[24] While the Commission notes that this exemption reflects its belief that communications that are prepared as a requirement of statutes or regulations should not be viewed as "Advertisements," the Commission goes on to provide that extraneous information provided by an investment adviser (i.e., information that is "… neither required under applicable law nor required by the proposed rule"), *would be* an "Advertisement."[25]

The proposed Advertising Rule, however, raises questions as to what information is "required" in certain regulatory notices or other filings, particularly in the context of certain periodic Commission filings required to be made by publicly traded registered investment advisers (including, among others, 8-Ks and 10-Ks that are filed and publicly available on the Commission's Edgar website). For instance, Form 10-K requires "a narrative explanation of the financial statements and other statistical data that the registrant believes will enhance a readers' understanding of its financial condition, changes in financial condition and results of operation," which disclosure should not be generic and "boilerplate" and instead, should be tailored to reflect the specific facts and

[23] While the risks inherent in these types of materials are low in general, we believe they are particularly low for closed-end private fund advisers that do not offer periodic redemption or withdrawal rights.
[24] Proposed rule 206(4)-1(e)(1)(iv).
[25] *See* Proposed Rules, 84 Fed. Reg. at 67531.

circumstances specific to a registrant.[26] For registered investment advisers, this information often includes fund performance (even though the Form does not specifically require such information). Publicly traded investment advisers typically make a determination to include fund performance, as it drives the cash flow and earnings of an investment adviser, and thus is consistent with the overall objectives of the Form. In particular, investment advisers provide this information as they deem it to be relevant to the shareholders of the investment adviser (as opposed to their clients and fund investors) to ascertain and evaluate the financial strength of a company and the likelihood that past performance is indicative of future results.

Periodic filings for publicly traded investors are aimed to a different audience than "Advertisements" (i.e., their shareholders, as opposed to prospective clients and fund investors). Therefore, while in other contexts performance disclosure should be deemed to be "Advertising," we believe that where the purpose of a required statutory or regulatory notice, filing or other communication is not to gather new investors but instead to satisfy the notice, filing or other communication's requirements in a manner the investment adviser determines is appropriate, such disclosure should be exempt from the definition of "Advertising."

We would respectfully request the Commission clarify that "Advertising" does not include any information contained in a statutory or regulatory notice, filing or other communication, so long as such information is reasonably designed to satisfy the requirements of such notice, filing or other communication and is not for the purpose of obtaining new fund investors or clients.

4. Appropriate Disclosure Should Satisfy the "Fair and Balanced" Requirement with Respect to Endorsements

We support the Commission's view that there should not be a blanket prohibition against the use of endorsements and further agree that there should be certain tailored restrictions and conditions around the use of endorsements.[27] However, we do not believe that the "fair and balanced" concept is necessarily workable in the context of endorsements, and instead we would respectfully suggest that an investment adviser be permitted to use endorsements in advertising so long as any such endorsements are accompanied by appropriate disclosure.

The proposed Advertising Rule defines "endorsements" as "any statement by *a person other than a client or investor indicating approval, support, or recommendation* of the investment adviser or its advisory affiliates…"[28] In the proposing release, the Commission clarifies that endorsements could include statements that "indirectly implicate the expertise or capabilities of the adviser or its

[26] *See* DIV. OF CORP. FIN., U.S. SEC. AND EXCH. COMM'N, FINANCIAL REPORTING MANUAL 295 (2008).
[27] *See* Proposed Rules, 84 Fed. Reg. at 67538.
[28] Proposed rule 206(4)-1(e)(2) (emphasis added).

advisory affiliates, such as their trustworthiness, diligence or judgment."[29] This definition and accompanying clarification cast a wide net over the types of statements that could be deemed endorsements, and, in an investment advisory context, would capture opinions and statements made by service providers and joint venture partners. In the context of a private equity fund manager, the definition would appear to include statements by portfolio company management, which can be valuable resources to other management teams and business owners in choosing to partner with an investment adviser.

While the Commission recognizes that endorsements are useful tools for investors in evaluating investment advisers,[30] the Commission further notes that the use of endorsements in an advertisement would be subject to the general prohibitions on certain advertising practices, including the prohibition on cherry-picking, specifically noting that "… cherry-picking testimonials, or otherwise selectively only using the most positive testimonials available to an adviser, would not be consistent with the general prohibition in the proposed rule."[31] [32]

Because the definition of an endorsement is so broad and may come from *any person* other than a client or an investor, we would respectfully suggest it is nearly impossible for an investment adviser to comply with the "fair and balanced" requirement, which overly burdens the investment adviser in determining the group of persons from which it would need to solicit statements. In addition, endorsements include, by definition, only statements indicative of approval or support, or a recommendation of an investment adviser, and thus, it is unclear how an investment adviser could present an endorsement (or multiple endorsements) in an advertisement in a manner that complies with the "fair and balanced" requirement, as the concept of endorsements does not contemplate negative statements or opinions. We believe the challenges relating to presenting endorsements in a "fair and balanced" manner is distinct from "testimonials," which come from a finite group of persons (e.g., investors and clients), and relate to *any* statement made about their experience with the investment adviser.[33] We therefore believe it is easier for investment advisers to comply with a "fair and balanced" test as it relates to testimonials, as opposed to endorsements.

As the concept of "fair and balanced" is impractical in the context of endorsements, we would respectfully request this be replaced with a requirement for investment advisers utilizing endorsements to instead be required to disclose the inherent limitations in providing an endorsement

[29] Proposed Rules, 84 Fed. Reg. at 67538.
[30] *See id.*
[31] *Id.* at 67540.
[32] We note that we believe the Commission would take the same position with respect to endorsements.
[33] *See* proposed rule 206(4)-1(e)(15).

(e.g., that it may not represent all opinions about the investment adviser and that the investment adviser may not have solicited opinions from all possible parties) to ensure it is not misleading.[34]

5. The Definition of "Non-Retail Persons" Should Also Include "Accredited Investors," "Affiliates" of Investment Advisers and Their "Knowledgeable Employees"

With respect to the presentation of certain performance information in advertisements, the Commission proposes to distinguish between advertisements disseminated solely to "Retail Persons" and "Non-Retail Persons."[35] The proposed Advertising Rule includes as "Non-Retail Persons" only "qualified purchasers"[36] and "knowledgeable employees."[37] In a private fund context, this definition would thus limit the benefits and flexibilities for "Non-Retail Advertisements" solely to a fund that would be an investment company but for the exclusion provided by section 3(c)(7) of the Investment Company Act of 1940, as amended (the "Investment Company Act").

We believe the universe of "Non-Retail Persons" is too narrow and should be broadened and would respectfully request that the Commission include as "Non-Retail Persons" accredited investors, affiliates of the investment adviser and any such affiliates' "knowledgeable employees."

The Commission adopted a standard of net worth to define "accredited investors," deeming such persons as being "capable of evaluating the merits and risks of [a] prospective investment" and thus, not requiring the protections afforded under the Securities Act of 1933, as amended.[38] Further, in adopting the net worth standard for accredited investors, the Commission agreed that accredited investors are "persons who can bear the economic risk of an investment in unregistered securities, including the ability to hold unregistered (and therefore less liquid) securities for an indefinite period and, if necessary, to afford a complete loss of such investment."[39] In doing so, we would suggest that the Commission effectively adopted a standard of investor sophistication under the Advisers Act that has served as a well-known and long-understood concept in the private fund industry for private offerings. The Commission has subsequently reiterated the point that "the accredited investor concept in Regulation D was designed to identify, with bright-line standards, a

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[34] *See* proposed rule 206(4)-1(a)(1) (prohibiting an investment adviser from omitting any material fact necessary to make a statement not misleading).
[35] *See* Proposed Rules, 84 Fed. Reg. at 67546.
[36] Proposed rule 206(4)-1(e)(8)(i); *see* 15 U.S.C. §80a-2(a)(51).
[37] Proposed rule 206(4)-1(e)(8)(ii); s*ee* Rule 3c-5 under the Investment Company Act of 1940, as amended.
[38] *See* 17 C.F.R. §230.506(b)(2)(ii) (requiring that if securities are sold to an investor that does not meet the "accredited investor" standard, specific information requirements and protections apply).
[39] *See* U.S. SEC. AND EXCH. COMM'N, REPORT ON THE REVIEW OF THE DEFINITION OF ''ACCREDITED INVESTOR'' 88 (2015).

category of investors whose financial sophistication and ability to sustain the risk of loss of investment or ability to fend for themselves render the protections of registration unnecessary."[40] However, in the proposing release, the Commission inconsistently assessed "accredited investor status" - stating that it did not necessarily mean that such a person does not have access to the extensive and specialized resources or expertise needed to evaluate and understand the performance information that would be provided in a "Non-Retail Advertisement."[41] We would respectfully suggest that this inconsistency creates multiple "investor sophistication" standards, which could cause confusion with investment advisers and would require them to make multiple "sophistication" determinations for each prospective investor. Therefore, we believe that where the Commission has previously determined that "accredited investors" have the necessary sophistication to evaluate the risks and merits of a prospective investment in an unregistered security, such clients should also be determined to have the necessary sophistication, with appropriate disclosure, to understand and evaluate the performance information in "Non-Retail Advertisements."[42]

We would further note that "Non-Retail Advertisements" are not without their own level of defenses and safeguards, and therefore, accredited investors receiving these advertisements would not be without a level of protection. Under the proposed Advertising Rule, "Non-Retail Advertisements" are still subject to various restrictions relating to the presentation of performance net and gross of fees and such advertisements must comply with various general prohibitions and principles. We believe these prohibitions and requirements sufficiently protect, and address concerns relating to, accredited investors as "Non-Retail Persons."

While the proposed Advertising Rule does not address inclusion of affiliates of the investment adviser and/or their "knowledgeable employees" as "Non-Retail Persons," we would respectfully suggest the Commission broaden the definition to include such persons. "Knowledgeable employees" are, by definition, sophisticated and educated, having a sufficient understanding and

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[40] *See* Report on the Review of the Definition of ''Accredited Investor'' (Dec. 18, 2015), available at https:// www.sec.gov/corpfin/reportspubs/special-studies/ review-definition-of-accredited-investor-12-18- 2015.pdf, at 88.

[41] *See* Proposed Rules, 84 Fed. Reg at 67549.

[42] Should the Commission be uncomfortable with broadening the definition of "Non-Retail Persons" to include "accredited investors" we would propose that, at a minimum, the Commission should broaden the definition to include "qualified clients", as this is the investor sophistication standard previously adopted by the Commission under Section 205(e) of the Advisers Act. *See* 15 U.S.C. §80b-5(e) (permitting the Commission to make a determination of investor sophistication based on various factors, including "financial sophistication, net worth, knowledge of and experience in financial matters, amount of assets under management, relationship with a registered investment adviser and such other factors as the Commission determines are consistent with [section 205].").

experience in an investment advisory context.[43] Such individuals do not require the protections afforded to less sophisticated "Retail Persons." With the expansion and evolution of the asset management industry, investment advisory firms and their structure are growing in size and complexity. For instance, within a single organization, multiple investment advisers are often created to address different business segments (e.g., private equity and credit), with appropriate investment professionals employed by each such investment adviser. These entities are generally under common control with one another, may be "relying advisers," share resources and personnel and often invest, or permit their employees to invest in an affiliate's fund. With respect to these types of affiliated entities, we do not believe there should be a distinction among "knowledgeable employees," especially where the separation of the entities is purely structural.

If the Commission were to retain the more narrow definition of "Non-Retail Persons," it would create challenges and complications for investment advisers of private funds. While the Commission suggests that a pooled investment vehicle with both "Retail Persons" and "Non-Retail Persons" could either (i) provide different advertisements to each group of prospective investors or (ii) provide the same advertisements to all prospective investors that comply with the conditions for "Retail Advertisements," we disagree that these are practical solutions. In providing different advertisements and offering materials to investors in the same (or in parallel) vehicles, investment advisers would first need to consider securities offering issues associated with providing differing information to investors in the same parallel offering and consider whether this practice would be inconsistent with an investment adviser's fiduciary duty to it investors. We would further suggest that proposed solution (i) would be onerous for investment advisers in that it would require them to prepare multiple versions of the same document and examine the disclosure in each to make sure it is appropriately tailored to the different groups of investors. This proposed solution would undoubtedly result in additional costs and expenses to the funds and their investors with little to no added benefits. Further, proposed solution (ii) above (requiring investment advisers to provide "Retail Advertisements" to all investors) may prevent sophisticated investors from getting information they would find valuable and necessary in making an informed investment decision given their resources and knowledge, and would have the effect of steering the proposed Advertising Rule away from its overall goals shaped by a "principles-based approach."

We would further note that these requirements imply that an investment adviser would know whether the recipient of a particular advertisement qualifies as a "Non-Retail Person" at the time or prior to providing the materials, which is inconsistent with industry practice and does not advance the cause of investor protection. In the private fund context, this information may not be verified until the time an investor submits a subscription document, at which time the fund and the investment adviser can determine whether it is a "qualified purchaser" (or "knowledgeable employee") and can invest in a fund relying on section 3(c)(7) of the Investment Company Act, or the investor is an accredited investor and would invest through a fund relying on section 3(c)(1) of

[43] *See* Rule 3c-5 of the Investment Company Act of 1940, as amended.

the Investment Company Act. Accordingly, investment advisers seeking to present performance information in accordance with "Non-Retail Advertisement" requirements would need to adopt and implement policies and procedures to ensure that any such advertisements are distributed only to "qualified purchasers" or "knowledgeable employees," which would impede the fundraising process, add unnecessary costs to investors and cause timing delays in getting investors the information they desire.

6. The Requirement for a Designated Employee Review of Advertisements Should Be Removed

The proposed Advertising Rule includes a requirement that all advertisements be reviewed by a designated employee (or group of employees) at an investment adviser.[44] While the Commission does not prescribe who this person should be, it clarifies that it would be inappropriate for the person creating an advertisement to subsequently be responsible for its review and approval.[45]

We would respectfully suggest that this requirement could create additional compliance, administrative and recordkeeping burdens on already-stretched chief compliance officers. In particular, this would disproportionately burden small and newly established investment advisers that often have few employees, with employees serving in multiple roles (for instance, it is not uncommon for the Chief Financial Officer and Chief Compliance Officer to be the same individual). This requirement would effectively prohibit an individual from creating performance tables for an advertisement in their capacity as "Chief Financial Officer," and subsequently approving the advertisements in their capacity as "Chief Compliance Officer." This requirement would be inconsistent with the Commission's previous acknowledgement that the compliance function can be tailored to the size, scope and business of an investment adviser.[46]

Therefore, we would respectfully request the Commission remove the requirement for investment advisers to designate specific individuals to review and approve advertisements and instead rely on investment advisers to tailor their advertising procedures and processes as best suits their organization and structure. Specifically, we would suggest that any marginal benefit received by this requirement in terms of investor protections is outweighed by the administrative and compliance burden that would be placed on firm personnel. If the Commission would prefer to not remove the requirement entirely, we would respectfully suggest the Commission revise this requirement so as to not prohibit the same individual creating the advertisement from reviewing and approving it, as that would unduly burden small and newly established investment advisers. Instead, we would suggest the Commission clarify that a reviewing and approving individual must

[44] *See* proposed rule 206(4)-1(d); . Proposed Rules, 84 Fed. Reg. at 67568.
[45] *See* Proposed Rules, 84 Fed. Reg. at 67569.
[46] *See* 17 C.F.R. §275.206(4)-7; *see also* Compliance Programs of Investment Companies and Investment Advisers, Release No. IA-2204, 68 Fed. Reg. 74714 (December 24, 2003).

be qualified, knowledgeable and competent in the requirements of the Advertising Rule, without prescribing further guidance as to who, at a particular organization, should serve in this role.

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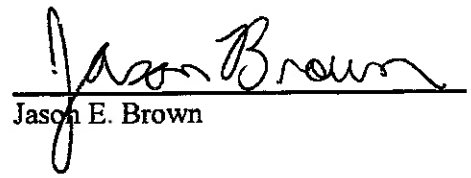
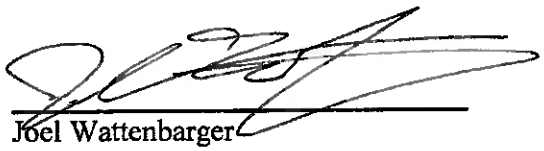
Again, we thank you for the opportunity to provide these comments. We stand ready to provide additional comments or to answer any questions you may have.

Very truly yours,



Jason E. Brown



Joel Wattenbarger