CFA Institute

915 East High Street
Charlottesville, VA
22902-4868 USA

+1 (434) 951 5499 tel
+1 (434) 951 5262 fax
info@cfainstitute.org
www.cfainstitute.org

24 February 2020

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

Re: Investment Adviser Advertisements; Compensation for Solicitations

File No. S7-21-19

Dear Ms. Countryman:

CFA Institute[1] appreciates the opportunity to comment to the Securities and Exchange Commission's ("SEC" or the "Commission") request for comment on its proposed rule, *Investment Adviser Advertisements; Compensation for Solicitations* (the "Proposal"). CFA Institute represents the views of those investment professionals who are its members before standard setters, regulatory authorities, and legislative bodies worldwide about issues affecting the practice of financial analysis and investment management, education and licensing requirements for investment professionals, and on issues affecting the efficiency, integrity and accountability of global financial markets.

Executive Summary

CFA Institute supports efforts to ensure investment advisers (hereinafter referred to as "Advisers") provide to investors a fair, accurate, complete, and timely representation of the kind and quality of advisory services they can provide to current and potential investment clients. False advertising about how an Adviser has performed in the past and will operate in the future can cause significant harm to individuals and their financial circumstances. It therefore warrants SEC attention.

Moreover, rules covering Adviser advertising were due for revision. When created, there was no worldwide web on which investors could find information about investment providers, and

[1] CFA Institute is a global, not-for-profit professional association of nearly 179,000 investment analysts, advisers, portfolio managers, and other investment professionals in 165 countries, of whom more than 172,000 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 158 member societies in 73 countries and territories.

investment services providers could market their offerings directly to investors. We support the SEC's updating of these rules to make them applicable to modern communications systems.

This area of regulation is by its nature complex due to the myriad ways in which Advisers can and do promote their services to clients. Consequently, development, application, and enforcement of regulation in this area requires nuance and care. At the same time, sophisticated institutional investors (as compared with less-sophisticated institutional investors such as trustees for small endowments) are capable of comprehending nuance in presentations from Advisers and consequently have less need for complex regulations to cover their interactions and dealings. Retail investors, on the other hand, need greater regulatory protection because they often are less capable of comprehending the complexity within adviser advertising, and therefore most likely victims of false, incomplete, and/or fraudulent advertising.

In reaching this goal, the Commission must at once avoid too much complexity in the rules it creates to deal with sophisticated investors, while also providing ample protection for less-sophisticated retail investors. The Proposal is the Commission's recommendations for addressing this different and often conflicting needs.

With these matters in mind, we provide the following summarized comments on the Proposal:

- Definition of an advertisement: While we appreciate the goal of creating rules applicable to a significant percentage of investment communications, we are concerned nevertheless about having the same requirements that apply to a one-on-one presentation with a sophisticated institutional investor also apply for a social media campaign to a broad retail audience. We believe this approach could lead to insufficient disclosures and information for marketing materials that are broadly distributed, while limiting the information institutional investors will receive in one-on-one presentations. We do not see this as helpful.

  Instead, we would prefer prescriptive requirements for broadly distributed advertisements to retail clients, and less prescriptive requirements for one-on-one presentations to sophisticated institutional and retail clients.

  We also are concerned that the redefining of the term, "advertisement," within the Proposal would include as advertisements, inaccurately we believe, performance and market updates that Advisers provide to their clients on a regular basis. Rather than increase information flow to existing investors, we believe the Proposal will lead to a reduction in information existing clients receive from their advisers, due in large part to the compliance difficulties and costs associated with the proposed re-definition of advertising.

  While we support the Proposal's effort to ensure adviser advertisements provide timely, relevant, complete, and accurate information to prospective customers, we also believe the Commission should amend its Proposals with regard to existing advisory customers. We believe the Commission could achieve this by defining an advertisement to cover materials distributed to one or more potential clients, while excluding one-on-one presentations and client reporting. The Commission should stipulate that to benefit from this definition and its implied exemption, the adviser would have to forego including adviser advertisements in such presentations and client reporting.

- Disclosure: To protect retail investors, we believe that broadly distributed retail advertisements should be provided in clear language and should not contain potentially

confusing financial terms that a retail investor may not understand. Disclosures addressing the following items should be required for retail advertisements containing performance:

- A statement alerting customers to the fact that past performance neither guarantees nor predicts future results, and it is possible the client may lose money.
- The type of fees (actual or model) that were used to calculate net-of-fee returns.
- Fees a retail client should expect to pay.
- Whether the net returns reflect different fees from those a retail client would pay (e.g., if a client will pay .80% in fees but the fees used to calculate advertised net returns are actual fees paid by other clients that may differ from what the retail client will pay).
- If a retail client should expect to pay any fees or expenses beyond the fees utilized in the calculation or presented in the fee schedule.
- A description of the investment strategy, including key risks (e.g., significant use of leverage or derivatives, or lack of liquidity).
- The effect of material market or economic conditions on the results portrayed, which can be achieved by presenting an appropriate market benchmark, if available. If no benchmark is shown, then the effect of material market or economic conditions must be disclosed.
- If an index or benchmark is presented, the material facts relevant to any comparison must be provided.

- Benchmarks: Benchmarks are an important component of fairly representing performance. While the Proposal addresses the presentation of performance earned by an Adviser, it does not require a comparison of this performance to a benchmark. Without providing an appropriate benchmark, an advertisement cannot illustrate whether or not an adviser has succeeded in managing clients' financial assets.

  Therefore, we believe an adviser should have to show returns of an appropriate benchmark for the same periods as presented for the adviser's performance. We suggest limiting this requirement to the situation where the adviser has benchmark performance available. An appropriate benchmark is one that reflects the investment mandate, objective, or strategy of the adviser's performance that is presented. For non-retail advertisements, the presentation of benchmark performance should be encouraged. We propose a definition for representative portfolio later in this letter in the relevant section.

- Exclusion of accounts from composites: We do not agree with the expansion of the conceptual basis for the Horizon no-action letter to the proposed rule. Whereas the Horizon letter permits presentation of performance of all accounts managed in a substantially similar manner from a prior entity, the adviser would have to calculate performance including all related portfolios – that is, it must calculate proper composite performance – to determine whether the results are "no higher than if all related portfolios had been included." We believe this proper composite performance is what an advertisement should present.

  Additionally, implementing the test to ensure results are "no higher than" the proper composite for each period included in the track record would be extremely difficult. We tried to imagine the procedures an adviser would need to ensure this test was met and believe that

clear guidance is needed for how an adviser can make this assessment. We note a number of questions this raises in the discussion below.

- Representative portfolios: The proposed rule requires that related performance must include all related portfolios and be presented on a portfolio-by-portfolio basis or as one or more composite aggregations. While we agree with the Proposal's call for presentation of composite performance and hope the adopting release encourages Advisers to present composite performance in advertisements when marketing a separate account, we appreciate that some Advisers who manage separate accounts may not maintain composites that cover all portfolios managed to a specific strategy. In such cases, flexibility is needed, and we believe Advisers should be allowed to use other types of related performance, including performance of a single representative portfolio. Please see our detailed comments in the sections below for details on what we mean by a representative portfolio.

- Performance of pooled investment vehicles: The scope of the Proposal includes both separate accounts and private pooled investment vehicles. However, there is no mention of the type of performance an Adviser should present when selling participation in a specific pooled investment vehicle. We believe an Adviser should be permitted to utilize pooled investment vehicle performance when marketing a pooled investment vehicle.

  We also believe related performance should be allowed. Related performance demonstrates an Adviser's experience managing other accounts in the same strategy as the pooled investment vehicle. This information can be very helpful to a prospective investor.

  Lastly, we believe that pooled fund net returns should be distinguished from net returns for related performance. When clients invest in a pooled fund, they cannot opt out of custody and other administrative fees. Therefore, we believe that when an Adviser is selling participation in a specific fund, net performance for that fund should be net of all fees an investor would pay, subject to issues raised in the Fee Disclosures discussion below.

- Fee disclosures: We do not believe it is feasible for an Adviser that presents gross returns to "provide promptly a schedule of the specific fees and expenses (presented in percentage terms) deducted to calculate net performance." This is because fees used to calculate performance can change over time, and if actual fees are used the fees can differ based on the constituents of the composite. Assuming the intended disclosure is the effective fee rate, we believe that this should be reconsidered. The effective fee rate of the composite can change every period as composite members change. If the fees change each year or each quarter, this becomes impossible to disclose.

  Rather than focusing on the effective fee rate of the calculation, we believe an investor would be more interested in the following items, which are included in the "Disclosure" bullet point above as we recommend requiring for all retail advertisements.

  - The type of fees (actual or model) that were used to calculate net-of-fee returns.
  - Fees the prospective client should expect to pay.
  - Whether the fees used to calculate net returns differ from what the prospective client should expect to pay.
  - If they should expect to pay other fees or expenses beyond those used in any net returns

or reflected in the fee schedule.

- Time-period requirements: While we support the Proposal's standardized presentation of performance, we nevertheless believe the Commission should contemplate the presentations of Advisers who claim compliance with the Global Investment Performance Standards (GIPS®). Advisers who claim compliance with the GIPS standards must present annual returns in their GIPS Reports as of the most recent annual period end. GIPS Reports are used through the year, and the requirement to present 1-, 5-, and 10-year returns as of the "most recent practicable date" in retail advertisements will force Advisers who distribute GIPS Reports to a retail audience to continuously update these reports throughout the year in a similar manner. We provide possible solutions to this compliance challenge in our response to question 18 on page 16 of this letter, under "Prescribed Time Periods."

  We also believe the Proposal needs to allow for money-weighted returns. As written, it appears to contemplate only time-weighted returns. When an Adviser controls external cash flows, however, we believe money-weighted returns may be more meaningful than time-weighted returns. We specifically recommend requiring disclosure of an annualized since-inception money-weighted return. While we recognize that the time-period requirement is only proposed for retail advertisements, and that private funds with capital call structures would most likely be advertised to non-retail prospective investors, in the spirit of making the rule timeless we believe the SEC should address the concept of time-weighted and money-weighted returns in the final rule.

- Extracted performance: The proposed definition of extracted performance is "the performance results of a subset of investments extracted from a portfolio." This is similar to a concept in the GIPS standards, referred to as carve-out performance. A carve-out under the GIPS standards is a portion of a portfolio that is representative of a distinct investment strategy. It can be included in a composite as long as it includes cash and can be used to create a track record for a standalone strategy, similar to any other portfolio.

  We believe the rule should distinguish between extracted performance advertised as a standalone strategy (equivalent to a GIPS-compliant composite that includes carve-outs) and extracted performance advertised as a segment of a strategy (large-cap equity performance excluding cash, for example). When extracted or carve-out performance is used to advertise a standalone strategy, it needs to be held to a higher standard because it will be held out as being managed as a distinct investment strategy. In such cases, we believe the final rule should have three requirements.

  - First, an Adviser needs a fundamental belief that the extraction represents a strategy that could be managed as a standalone portfolio. An Adviser should not be able to extract one or two securities from a portfolio and market it as a strategy. We believe advertising performance based on such a small number of investments that is not representative of a standalone portfolio would be misleading.
  - Second, we believe extracted performance should be based on a composite of all related portfolio extracts.
  - Third, we believe this extracted performance should have to include an allocation of cash. When extracted performance is not advertised as a standalone strategy (e.g., segment performance), we do not believe that cash needs to be allocated.

- Targeted and projected returns: We believe that targeted returns should be removed from the current definition of hypothetical performance for any portfolio or to the investment services offered or promoted in the advertisement. At the same time, we believe projected performance should be considered hypothetical performance. Targeted returns, such as those used as a benchmark or to describe the investment objective of a strategy, are not hypothetical but rather used to define or measure the success of a strategy. Projected performance, on the other hand, should be considered hypothetical because in this case an Adviser is taking historical data and applying assumptions to that data to predict what will happen in the future.

- Blurring of distinctions between Advisers and broker-dealers. We are troubled about the application of the definition of Adviser advertisement to cover investors in pooled investment vehicles. This further blurring of the distinction of what Advisers do under the Investment Advisers Act and what others, such as broker-dealers or other solicitors will likely impose greater restrictions on capital-raising activities on behalf of corporate issuers. This would be to the detriment of investors and the economy, in general.

  We have argued against blurring these distinctions in other matters[2] for other reasons. In this case, our concern is that the blurring may ultimately subject broker-dealers' capital-raising activities to provisions of the Advisers Act that are more appropriately addressed by the Securities Exchange Act which are intended to cover such activities. By handling matters in this way, we are concerned the Proposal will not only create regulatory confusion for broker-dealers and private capital issuers, but also create potential conflicts with existing interpretations of the Securities Acts, conflicts that could force broker-dealers operating in this space to have to register as Advisers. Ultimately, this blurring could dissuade broker-dealers from engaging in capital raising for such private funds, thereby depriving venture capital, private equity, and other investment vehicles of funding for economic growth and efficiency.

Definition of "Advertisement" – Section 275.206(4)-1

Proposed Subsection: (e)(1) – Definitions (p472). The Proposal would define "advertisement" as "any communication, disseminated by any means, by or on behalf of an Adviser, that offers or promotes the Adviser's investment advisory services or that seeks to obtain or retain one or more investment advisory clients or investors in any pooled investment vehicle advised by the

[2] See: 10 Jan 2018 Letter to SEC Chairman Jay Clayton on control of titles used by broker-dealers when interacting with retail investors, found at http://www.cfainstitute.org/-/media/documents/comment-letter/2015-2019/20180110.ashx; 29 March 2018 Letter to SEC Staff responding to questions raised in in-person meeting on 10 January 2018 letter, found at http://www.cfainstitute.org/-/media/documents/comment-letter/2015-2019/20180329.ashx; 7 August 2018 Letter to SEC on Proposed Regulation Best Interest, found at http://www.cfainstitute.org/-/media/documents/comment-letter/2015-2019/20180807-3.ashx; 7 August 2018 Letter to SEC on Proposed Interpretation of Standard of Conduct for Investment Advisers, found at http://www.cfainstitute.org/-/media/documents/comment-letter/2015-2019/20180807-2.ashx; 7 August 2018 Letter to SEC on Proposed Form CRS and Titles Control, found at http://www.cfainstitute.org/-/media/documents/comment-letter/2015-2019/20180807-1.ashx; and 16 May 2019 Letter to SEC on Investor Testing of Form CRS Relationship Summary, found at http://www.cfainstitute.org/-/media/documents/comment-letter/2015-2019/20190516.ashx.

Adviser." The Commission notes that this definition is intended to be flexible enough to remain relevant regardless of technological changes or evolving investment practices.

The Proposal would not include the following as advertisements:

- Live oral communications not broadcast on radio, TV, the internet, or similar media;
- Communication that does no more than respond to an unsolicited request for information about the Adviser or its services, excepting:
    - Any communication to a retail person that includes performance results; or
    - Any communication that includes hypothetical performance;
- Any advertisement, other than sales material, or sales literature that is about a registered investment company or a business development company and is within rule 482 or rule 156 of the Securities Act; or
- Any information required to be contained in a statutory or regulatory notice, filing, or other communication.

CFA Institute Response: Our primary concern with the re-definition of advertisement in this way is its breadth, covering "any communication," including by inference any communication with existing investment advisory clients. We disagree with this specific aspect of the Proposal because, whether intended or not, this phrasing will ultimately subject any communication with existing clients to the complicated and complex rules incorporated within the Proposal.

We believe this is wrong because Advisers' principal communications with existing clients are intended to update their clients for reasons other than business solicitation, including: a) how their investment portfolios have fared in recent months; b) the current state of their investment portfolios; c) how current and anticipated macro- and micro-economic and geopolitical events may affect investment strategies and tactics, and investment performance in the near future; and d) whether any change in strategy or holdings is warranted given the foregoing.

For example, prudent Advisers will wish to communicate with their existing clients on how the current coronavirus that began in Asia will affect not only supply lines for many companies whose securities are held in client portfolios but also its potential affect on revenues, costs, liabilities, and the value of intangibles, among other things, for portfolio companies. Under the Proposal as written, however, we are concerned such communications would be deemed advertisements and, therefore, subject to the Proposals rules.

These communications also are important and useful to clients in helping them assess their Advisers' value and performance, and ultimately hold those Advisers accountable. By defining such communications so broadly to ensure coverage by the Proposal's advertising rules, whether by intention or inadvertent interpretation, the Proposal is likely to reduce communication between Adviser and client, together with fewer communications that might be more accurately construed as advertisements.

Specific Phrases

Dissemination by any means. The Proposal would expand the scope of its coverage beyond the written communications and radio or television announcements in the current rule to "encompass

all promotional communications regardless of how they are disseminated," with limited exceptions. The rule would cover electronic communications and presentations, videos, films, podcasts, blogs, billboards, and all types of social media. The Commission notes that its use of "by any means" is intended to focus "the proposed rule on the goal of the communication, and not its method of delivery" in the hope of ensuring the definition will "remain evergreen" with evolving technologies.

CFA Institute Response: In general, CFA Institute supports the SEC's efforts to capture all means of delivering advertising to potential clients. There is a significant need to update the rule to address new technologies Advisers may use to deliver advertisements to potential clients.

Our concern is the potential all-encompassing nature of the rule, and particularly how that will affect communications with clients. We noted these concerns in our comments in the immediately preceding question within this section.

Proposed Subsection: (a) - General Prohibitions (p468). The re-definition of advertisement would include a list of seven general prohibitions for advertisements, including:

- Any untrue statement of a material fact, or omission of a material fact needed to make the statement, in relevant circumstances, not misleading
- Unsubstantiated material claim or statement
- Untrue or misleading implication about a material fact about the Adviser, or that would likely create an untrue or misleading inference about the Adviser
- Discusses or implies potential benefits of the Adviser's services or methods without clearly and prominently commenting on risks or limitations of the potential benefits
- Unfair and unbalanced presentation of specific investment advice given by the Adviser
- Performance presentation that unfairly includes/excludes certain results or time periods
- Otherwise materially misleading information

CFA Institute Response: In general, CFA Institute sees these as appropriate intended targets for false advertising. The Commission should have little difficulty proving to a court whether a statement of fact provided by an Adviser is untrue, or that an omitted material fact was needed to accurately present an Adviser's approach, performance, history, or other material information.

Likewise, we recognize the value and importance of ensuring that performance presentations are not unbalanced or include or exclude certain periods to make results look better than they would be if appropriately presented. The SEC can obtain sufficient and relevant data to prove such faulty, "unbalanced," and "unfair" performance.

Others of these prohibitions, however, seem difficult to enforce. In particular, proving that an advertisement falsely or misleadingly "implied" something about an Adviser appears difficult. While we support efforts to prevent false advertising to investors and enforce such prohibitions, we worry that the Commission's enforcement division will have difficulty proving to juries that inferences or implications of material facts or potential benefits constitute regulatory violations or fraud. While the Commission is likely to find a friendly jurist in administrative law courts, the

trend for investors and investment practitioners to seek jury trials is likely ultimately to make such options mute.

For these reasons, we recommend the elimination of the third prohibition above with greater reliance on the first prohibition. Likewise, we recommend removal of "or implies" in the fourth bulleted item above.

Compensation for the Solicitation of Existing and Prospective Investors (p 210). As part of the Proposal, the Commission proposes to amend the Advisers Act cash solicitation rule, Rule 206(4)-3, to expand its reach to cover solicitations of existing and prospective private fund investors. The Commission notes this expansion is intended to further protect private fund investors by alerting them to a solicitor's conflicted interests. It also would prohibit an Adviser from using the services of disqualified solicitors who have disciplinary events barring them from association with an Adviser.

The Commission notes that the expanded application of the solicitation rule to private fund investors and not just an Adviser's clients – i.e., the persons or firms hired to solicit funds from the private fund investors – would be consistent with the Proposal on Adviser advertising. Solicitations of existing and prospective investors in registered investment companies ("RICs") and business development companies ("BDCs") would be exempt from the Proposal's expansion because, the Commission contends, broker-dealers and other financial intermediaries already provide conflict disclosures related to selling interests in RICs and BDCs. The Proposal also notes the Commission's expectation that RIC and BDC investors are sought through advertisements or investment advice which are subject to other regulatory requirements. Finally, the Commission expressed its view that harmonizing the scope of the solicitation rule with the advertising rule should ease compliance burdens.

CFA Institute Response: In general, CFA Institute supports the disclosure of conflicts of interest to investors to ensure they are aware of agents who may not be acting in their best interests. We concur with the statement within the Proposal (see page 221, paragraph 2) that "it is important for investors to understand whether they will bear any additional costs as a result of the solicitation."

At the same time, investors in private funds are deemed sophisticated, in part, because they have experience investing in such vehicles and therefore likely either to comprehend the potential for conflicted interests of solicitors for such funds or have access to investment and legal counsel to help make them aware of these potentialities. A first line of defense in ensuring all investors, sophisticated or not, is to ensure the agents soliciting from them use titles that convey the roles they play in the solicitation. If they are working as brokers, they should use the broker title. Only those agents who must adhere to a higher, fiduciary standard of care and must put clients' interests ahead of their own, and not just on an equal basis, should be able to use the "Adviser" title in any form.

Furthermore, it appears this proposed expansion of Rule 206(4)-3 would reinterpret *Goldstein, et al. v. Securities and Exchange Commission* decided by the U.S. Court of Appeals for the District

of Columbia Circuit in 2006. That decision served as the basis for the Commission's 2008 Mayer Brown LLP Interpretive Letter[3] which recognized that

> "for purposes of Section 206 of the Advisers Act, ***investors in a pooled investment vehicle are not "clients" of the investment adviser of the pool***. Similarly, we believe that the references to ***"client" and "prospective client" in Rule 206(4)-3 under the Advisers Act should not be interpreted to include investors in investment pools or prospective investors*** in investment pools." [emphasis added]

The Commission notes that it intends to revisit its Mayer Brown Interpretative Letter as part of this Proposal.

We are concerned that with this provision, the Commission would further blur the differences between Advisers and broker-dealers already blurred by Regulation Best Interest and Form Customer Relationship Summary (collectively, "Reg BI"). We did not support the blurring of standards of conduct in Reg BI because we believed it left retail investors, and unsophisticated investors in particular, unaware of the different roles and legal standards for these two groups of investment professionals.

In regard to the Proposal, however, we are less concerned with the protection of sophisticated investors considering investments in private funds and more concerned how the blurring of the roles and obligations of Advisers and solicitors for private fund activities could weaken the ability of investment funds to raise capital for emerging growth companies, for example, or to supply the ongoing capital needs of companies in various industries.

Consequently, we do not support this provision of the Proposal.

5. Performance Advertising

a. Application of the General Prohibitions to Performance Advertising (p. 102)

Questions beginning on p. 105

1. *The proposed rule addresses some disclosures by reference to the prohibitions in paragraph (a). As an alternative, should we require in rule text any specific disclosures or other information to be included in performance advertising? Why or why not? Should we require any of the disclosures described above? For example, should we require disclosure of the material conditions, objectives, and investment strategies used to obtain the results portrayed; whether and to what extent the results portrayed reflect the reinvestment of dividends and other earnings; the effect of material market or economic conditions on the results portrayed; the possibility of loss; or the material facts relevant to any comparison made to the results of an index or other benchmark? Why or why not?*

CFA Institute Response: To protect retail investors, we believe that broadly distributed retail advertisements should be required to include certain disclosures. The required disclosures should be in clear language and not contain potentially confusing financial terms so that a retail investor would likely be able to understand them. We also believe that retail investors should receive

[3] See: Mayer Brown LLP — Interpretive Letter, July 28, 2008, https://www.sec.gov/divisions/investment/noaction/2008/mayerbrown072808-206.htm

benchmark returns or other information about the effect of market or economic conditions. Without providing an appropriate benchmark, an advertisement cannot illustrate whether an Adviser is successful in managing financial assets. (Please also see our comment about the use of benchmarks in the response to question 2 under "General request for comment on performance advertising" on page 52 of this letter.) We believe disclosures addressing the following items should be required for retail advertisements:

- Past performance neither guarantees nor predicts future results, and it is possible that the client may lose money.
- The type of fees (actual or model) that were used to calculate net of fee returns.
- Fees a retail client should expect to pay.
- If the net returns reflect different fees from those that a retail client should expect to pay (e.g., if a retail client will pay .80% in fees and the fees used to calculate net returns are actual fees of other clients that differ from the .80% the retail client will pay).
- If a retail client should expect to pay any other fees or expenses beyond the fees utilized in the calculation or presented in the fee schedule.
- A description of the investment strategy, including key risks of the investment strategy (e.g., significant use of leverage or derivatives).
- The effect of material market or economic conditions on the results portrayed. (This can be met by presenting an appropriate market benchmark, if available, and if no benchmark is shown, then the effect of material market or economic conditions must be disclosed.)
- If an index or benchmark is presented, the material facts relevant to any comparison.

We also believe it would be helpful to provide in the adopting release principles for Advisers to consider when determining which disclosures to include in all advertisements, such as the following (some of which are taken from the proposed release):

- Properly tailor disclosures to the relevant services being offered, the performance being presented, and whether the recipient is a retail or non-retail investor. For retail advertisements, clear language must be used for describing the investment strategy and fees charged to ensure that terms are disclosed in a meaningful way so investors can compare financial products more readily and knowledgeably.
- Have disclosures that strike the right balance between providing enough information so the advertisement is not misleading but does not overwhelm the investor with so many disclosures that it renders the advertisement ineffective.
- Evaluate the particular facts and circumstances of the advertised performance, 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 prohibitions in paragraph (a) of the proposed rule or other applicable law.

We also recommend providing a non-exhaustive list of items that Advisers should consider disclosing in all advertisements. It would be helpful to have all disclosures currently found in various no-action letters included in one place, such as in the adopting release. We also

recommend that the adopting release explicitly state that this should not be treated as a checklist – that is, an Adviser must exercise judgement to determine which disclosures should be included in a specific advertisement, and the wording of the disclosures should be left to the Adviser. Based on the overarching principles above, Advisers would need to tailor, add, or exclude disclosures based on relevance and to ensure they comply with paragraph (a).

In addition to the disclosures we suggest requiring in retail advertisements above, we believe you should include the following disclosures for consideration in the adopting release:

- Information about the share classes or series used to calculate performance, if applicable.
- If the results portrayed do not reflect income. (We believe this disclosure should be required only when income is not reflected in returns. Industry convention is to include income in returns. Please note that we believe the currently required disclosure – to disclose whether and to what extent the results portrayed reflect the reinvestment of dividends and other earnings – is confusing and not necessary.)

[End of prior question] Should our disclosure requirements differ based on the intended audience for the performance advertising?

CFA Institute Response: We believe, as stated above, there needs to be specific requirements for retail advertisements. Similar to other regulations that protect consumers, there should be specific disclosures required to protect retail investors who are less knowledgeable about investment performance.

4. *If we adopt a rule that requires specific disclosures, should we specify how those disclosures are presented? For example, should we specify the proximity of the disclosure to the claim it qualifies or other relevant information? Should we specify how prominent such disclosure should be – e.g., with respect to size, color, or use of graphics – in order to increase the likelihood that a prospective investor reviews the disclosure? Would specifying such characteristics impede investment advisers from using non-paper media for advertising? Are there other elements of presentation that we should consider if we adopt a rule requiring specific disclosures?*

CFA Institute Response: We do not believe that there should be specific requirements on proximity, size, or color. However, to increase the likelihood that an investor reads and is able to understand the disclosures, we believe the adopting release should specify that the disclosures need to be legible and they must be provided in close proximity to the performance information.

5. *Are there specific disclosures that investment advisers include in their advertisements in order to comply with the current rule that they believe would be unnecessary in order to comply with the proposed rule?*

CFA Institute Response: As discussed in our response to question 1, we believe the disclosure "whether and to what extent the results portrayed reflect the reinvestment of dividends and other earnings" in the Clover Capital no-action letter is confusing and unnecessary.

Additionally, we believe the disclosure "if applicable, that the Adviser's clients had investment results materially different from the results portrayed in the model" included in the Clover Capital no-action letter is also unnecessary. It is expected that an Adviser's clients could and should have investment results that differ from the results portrayed in the model, due to unique client requirements. We instead suggest that when an Adviser presents model results that it should be encouraged to also present actual results of portfolios invested following the model, if such results exist.

6. *Have investment advisers experienced any specific compliance challenges in preparing and presenting appropriate disclosures for performance advertising? What types of compliance challenges and how might we address them in the proposed rule?*

CFA Institute Response: We believe that all critical compliance challenges faced by Advisers when preparing advertisements are addressed by the proposed rule and our comments.

7. *Are there specific disclosures that should be required in presenting the performance results of separate accounts but not pooled investment vehicles? Or in presenting the performance results of pooled investment vehicles but not separate accounts?*

CFA Institute Response: Our responses above contemplate both separate accounts and pooled investment vehicles.

What sorts of issues do investment advisers face in advertising performance results of pooled investment vehicles that they do not face in advertising performance results of separate accounts? Should the proposed rule address those issues? And if so, how?

CFA Institute Response: Advisers face the following issues when advertising performance results of pooled investment vehicles that they do not face when advertising performance results of separate accounts. We believe these issues should be addressed as follows:

- Determining which share class or series to use for performance. This item can be addressed through disclosure of the share class or series used for performance.
- Use of money-weighted returns (MWRs) versus time-weighted returns. Many private funds use money-weighted returns instead of time-weighted returns. We believe Advisers should be allowed to use money-weighted returns versus time-weighted returns when they control the timing of external cash flows to and from clients. If an Adviser qualifies to and chooses to present money-weighted returns instead of time-weighted returns, we believe they should be required to present an annualized since inception money-weighted return.
- Use of a fund's track record when the strategy changes. Advisers may be required to use history of a fund even if the strategy has changed. We believe this can be addressed by disclosing the date and change of the strategy.

- Potential inability to use related performance in fund marketing materials. We believe that related performance is relevant to all investors, and the inability to use related performance in certain situations withholds important information from investors. In our opinion, an investor who is deciding whether or not to purchase a pooled investment vehicle would want to see an Adviser's experience in managing accounts to the same strategy. We believe Advisers should be allowed to present fund performance and/or related performance when advertising a fund. If an Adviser chooses to show related performance when advertising a fund, any differences between the accounts included in the related performance and the fund, including differences in fees and costs, should be clearly disclosed.

Are there similar or other issues that would apply to presenting the performance results of other investment structures, for example side pockets of illiquid investments?

CFA Institute Response: Side pockets present a unique issue. We believe that, following the principles of fair representation and full disclosure, performance of a fund that includes the effect of any side pockets should be presented. However, an Adviser should be allowed to also show performance excluding the effect of any side pockets.

Another issue that continues to draw attention is the use of subscription lines of credit. These can shorten the time period for which the money-weighted return is calculated and have a significant effect on performance. We believe that returns calculated both with and without the effect of the subscription line of credit should be presented. If the subscription line of credit was short term in nature and was not used to fund distributions, we recommend not requiring returns without the effect of the subscription line of credit. We believe that the adopting release should specifically address this issue and state that if a subscription line of credit is in use, it would be misleading if appropriate disclosures about the use and effect of the line of credit are not included.

b. Requirements for Gross and Net Performance

Questions beginning on p. 133

1. *Is our belief accurate that analyzing certain performance information requires access to more specialized and extensive analytical and other resources than would be required to evaluate the merits and risks of an investment?*

CFA Institute Response: We agree.

Should we require additional disclosures based on the type of audience to which performance advertising is disseminated as proposed?

CFA Institute Response: We believe certain disclosures should be required for retail advertisements. See our response to question 1 under "Performance Advertising and Portability of Performance: Application of the General Prohibitions to Performance Advertising" on page 10 above for suggestions on differentiating the disclosures for retail and non-retail advertisements.

2. *Would such an approach place Retail Persons at an informational disadvantage?*

CFA Institute Response: We do not believe that requiring clear, standardized disclosures for a retail audience would put Retail Persons at an information disadvantage.

> *Should we instead impose on all advertisements the same requirements for presenting performance results that the proposed rule would impose only on Retail Advertisements? Would such an approach create difficulties where different audiences may need different amounts and types of disclosures to ensure that the performance information is not false or misleading?*

CFA Institute Response: We do not believe the same requirements should apply to retail and non-retail clients. There is value in being more flexible for advertisements created for non-retail clients, and there is a greater need to protect retail clients.

> *For instance, would the amount or type of disclosure necessary to make a Retail Advertisement not misleading overwhelm the disclosure and render it ineffective?*

CFA Institute Response: As mentioned above, we believe that requiring clear, standardized disclosures for retail clients is the best approach. We agree that if there is too much disclosure it can overwhelm and make the disclosures ineffective.

> *Would treating all advertisements presenting performance results the same way make it harder for Non-Retail Persons to obtain information they find valuable?*

CFA Institute Response: As mentioned above, we do not think all advertisements should be held to the retail advertising requirements. We agree with the proposed rule that enables Advisers to show only gross returns in non-retail advertisements but requires net returns in retail advertisements.

3. *Instead of our approach to performance presentations, should we simply rely on an overarching prohibition against misleading advertisements? Would such an overarching prohibition achieve our objective in a less burdensome and more effective way than the approach we are proposing? Why or why not?*

CFA Institute Response: We believe the industry will benefit from having some additional guidance for determining what would be considered misleading. Without guidance, Advisers that are trying to do the right thing might unknowingly provide the wrong type of information to prospective investors. Advisers would also welcome having consolidated disclosures that are currently included in numerous no-action letters

4. *If we do not include additional disclosure requirements for Retail Advertisements, should we require that advertisements directed to general audiences include more comprehensive disclosure than those directed to more financially sophisticated audiences?*

CFA Institute Response: Assuming the definition of an advertisement in the proposed rule is the same in the final rule, we believe that requiring standardized, clear disclosures for retail advertisements is the best approach. Alternatively, and what we believe is a better approach, is to keep the current definition of an advertisement – that is, materials distributed to more than one

party and excluding one-on-one presentations and client reporting. In that case, the disclosures that we proposed for retail advertisements could be applied to all advertisements since they would be broadly distributed.

> *If so, should we consider providing guidance or promulgating disclosure requirements for how an adviser's disclosure may differ based on the investor's financial sophistication or scope of mandate? What guidance should we provide or disclosure should we require?*

CFA Institute Response: Please see our response above**.**

> *Would there be any types of performance presentations whose risks or limits could not be disclosed effectively to some audiences?*

CFA Institute Response: We do not believe there are any such types of performance presentations.

Presentation of Gross and Net Performance

i. Prescribed Time Periods (p.130)

18. *(Bullet point 3 on p. 138) Do Advisers to pooled investment vehicles other than Section 3(c)(7) Companies, including private funds that rely on section 3(c)(1) of the Investment Company Act, or investment advisers to separate accounts currently provide the kinds of performance information in advertisements that we propose to require in Retail Advertisements?*

CFA Institute Response: We believe that it is common for Advisers to provide performance for standardized time periods, often following the periods required to be presented for '40 Act funds. However, the requirement to present 1-, 5-, and 10-year returns will put a burden on Advisers claiming compliance with the GIPS standards that present annual returns in their GIPS-compliant reports as required by the GIPS standards, if the GIPS Reports will be distributed to retail investors. This will force Advisers that present GIPS Reports to retail investors to add the annualized returns to their current GIPS Reports. Because GIPS Reports are used throughout the year, Advisers will be forced to continuously update their GIPS Reports provided to retail clients throughout the year, to include updated 1-, 5-, and 10-year returns. We also believe that the annual returns included in GIPS Reports are much more informative than only 1-, 5-, and 10-year annualized returns, and allow for greater comparability between Advisers. We believe the following are possible solutions to address these issues:

- Align the rule with the GIPS standards by allowing Advisers to present annual returns for the past 10 years (or since inception if the track record exists for less than 10 years) as of the most recent calendar year end, instead of 1-, 5-, and 10-year annualized returns.
- Assuming you do not allow the substitution of annual returns for 1-, 5-, and 10-year annualized returns, allow "the most recent practicable date" for GIPS Reports to be as of the last calendar year end. Firms that comply with the GIPS standards would calculate and present the 1-, 5-, and 10-year annualized returns through the most recent annual year end in GIPS Reports.

- Allow the 1-, 5-, and 10-year annualized returns as of the most recent practicable date to be presented separately from the GIPS Report.
- Remove "and ending on the most recent practicable date" from the Rule, and instead discuss timeliness in the Adopting Release, without specifying a specific period.

Additionally, Advisers typically present a 3-year return in addition to the 1-, 5-, and 10-year returns. In the industry, 3 years is typically considered the minimum period when an investor is looking for an established track record. We suggest adding the 3-year time period as an additional required annualized return.

Lastly, when Advisers control cash flows (e.g., private funds with a capital call structure), they typically provide a single since-inception money-weighted return. They do not provide multiple money-weighted returns. We believe you should allow a money weighted return for those portfolios/strategies for which the Adviser controls the cash flows. If an advisor chooses to present a money-weighted return, we recommend requiring an annualized since inception money-weighted return.

> *Would the proposed rule create unique compliance difficulties for Advisers to pooled investment vehicles other than Section 3(c)(7) Companies? What types of difficulties and how should we address them?*

CFA Institute Response: As discussed above, pooled funds for which the Adviser controls the cash flows typically present money-weighted returns, and often do not provide time-weighted returns because time-weighted returns do not capture the effect of the timing and size of the cash flows. We recommend allowing a money weighted return for portfolios or composites where an advisor controls the cash flows. In such cases, we recommend requiring a single since-inception money-weighted return to be presented.

19. *(p. 138) Will requiring Retail Advertisements that present gross performance also to present net performance be effective in demonstrating the effect that fees and expenses had on past performance and may have on future performance?*

CFA Institute Response: Presenting both gross and net returns is an effective way to demonstrate the effect that fees and expenses will have on future performance, but this is true only when the fees that will be charged to the retail client are consistent with the fees that were used to calculate net returns. When the historical fees are not consistent with the fees that the retail client will pay, or the fees have changed over time, it becomes more challenging to understand this effect.

We also do not believe it is feasible to disclose "a schedule of the specific fees and expenses deducted to calculate net performance." Both model and actual fees may change over time, and actual fees can differ by client and by the amount of assets in an account. Determining a schedule of fees would get particularly challenging when composite performance is presented. We believe that retail clients would be better served if the following disclosures are required:

- The type of fees (actual or model) that were used to calculate net of fee returns.

- Fees a retail investor should expect to pay.
- If the net returns reflect different fees from those fees that a retail client should expect to pay.
- If a retail client should expect to pay any other fees or expenses beyond the fees utilized in the calculation or presented in the fee schedule.

Is there an alternative approach that would better demonstrate this effect?

CFA Institute Response: We think the effect of fees on performance is best demonstrated by showing both gross and net returns. However, when only net returns are shown, the effect of fees will be difficult, if not impossible, to address through disclosure. We therefore recommend requiring retail advertisements that present only net returns to include an example of the effect of fees over time. The example should be required to reflect the highest fee that the retail client could be charged for the respective strategy. We have seen Advisers use the same fee schedule for this example all strategies, regardless of the fee schedule that is appropriate to the strategy. We do not believe that presenting the effect of a 0.50% fee is helpful to a retail client who would be paying a 1.00% fee.

20. *(p. 138) Are there any instances when presenting net performance in accordance with the proposed rule would not be feasible or appropriate in a Retail Advertisement? Are there any exceptions to this requirement that we should consider?*

CFA Institute Response: When a portfolio pays no investment management fee, or a very small fee, a net return calculated by deducting actual fees will not appropriately demonstrate the effect that fees and expenses had on past performance and may have on future performance. This could happen when the assets included in performance are proprietary assets, employee assets, or there is a special fee waiver. The GIPS standards do not require an Adviser to apply a model fee to non-fee-paying portfolios. Instead, the GIPS standards require Advisers that include non-fee-paying portfolios in a composite and calculate net returns using actual investment management fees to disclose the percentage of assets represented by non-fee-paying portfolios as of each calendar year end. This allows a reader to understand the potential effect of the non-fee-paying portfolios on the net returns. We recommend taking the same approach and allow an Adviser to disclose the fact that non-fee-paying assets are included in the performance, as long as they also offer to provide information about the effect of such non-fee-paying assets on the returns.

21. *(p. 139) Is there additional information that we should require advisers to disclose when presenting gross performance?*

CFA Institute Response: The proposed rule addresses the use of gross returns. We recommend also addressing the use of what the GIPS standards refer to as "pure" gross returns. A pure gross return is a return on investments that does not reflect the deduction of transactions costs. Pure gross returns are commonly used when transaction costs are bundled with investment management fees, such as in a wrap fee arrangement. We believe that Advisers should be

required to identify pure gross returns as such and disclose that pure gross returns do not reflect the deduction of transaction costs.

We also believe that the rule should address whether returns of accounts that pay zero commissions are gross returns or pure gross returns. We believe that if actual transaction costs are zero, as is common in this zero-commission era, the return reflecting zero transaction costs is still considered to be "net of transaction costs" – the transaction costs are just zero.

22. *(p. 139) Should we clarify any specific criteria for "equal prominence"?*

CFA Institute Response: As mentioned in the discussion of the proposed rule, the concept of "equal prominence" is included in the GIPS Advertising Guidelines. While debating this concept, and creating interpretation of this requirement, we have had multiple debates about what "equal prominence" means. It was abundantly clear to us that there were too many considerations, and we eventually decided to not define what equal prominence means. We instead will remind firms that they must not present any performance that is false and misleading and must review each advertisement to be certain that the layout of the information is not misleading. We recommend taking the same approach.

> *Should we clarify any criteria for determining if net performance is presented "in a format designed to facilitate comparison"?*

CFA Institute Response: We do not believe that you should clarify criteria for determining if net performance is presented in a format designed to facilitate comparison. We recommend taking the same approach as we describe above with regard to defining "equal prominence."

23. *(p. 139) Should we provide further guidance or specify requirements in the proposed rule on how to calculate gross performance or net performance? If so, what guidance or requirements* should we provide?

CFA Institute Response: We believe that further guidance for calculating gross and net returns should be included, including the following:

- Specify what must be deducted when calculating "pure" gross returns, gross returns, and net returns;
- Specify that net returns for advisory clients must reflect the deduction of transaction costs and investment advisory fees (including any performance-based fees or carried interest);
- Specify that net returns for pooled funds must reflect the deduction of transaction costs, investment advisory fees (including any performance-based fees or carried interest), and any other fees or costs charged to fund investors;
- Require the use of total returns for both portfolios and benchmarks;
- Assuming money-weighted returns are allowed, require an annualized since inception money-weighted return;

- Specify that returns for the 1-, (3-), 5-, and 10-year periods are annualized returns; and
- Prohibit annualizing returns for periods of less than one year.

Should we look to the Global Investment Performance Standards adopted by the CFA Institute ("GIPS") or other standards?

CFA Institute Response: Compliance with the GIPS standards is demanded by the investment community, particularly by non-retail investors, who are knowledgeable about the complexities and nuances of performance information. The GIPS standards are viewed as the best practice for performance presentations and are often used as a resource for firms that do not comply with the GIPS standards.

Firms that adopt the GIPS standards are required to establish policies and procedures for complying with all applicable requirements of the GIPS standards. All investors, including retail investors, benefit from having an Adviser that claims compliance with the GIPS standards because the Adviser has voluntarily committed to establishing robust policies and procedures for calculating and presenting performance.

Should we require investment advisers to adopt policies and procedures prescribing specific methodologies for calculating gross performance and net performance? Why or why not?

CFA Institute Response: We believe Advisers should be required to adopt policies and procedures for calculating performance in accordance with their selected methodology. Even more important, however, is the population of portfolios that is included in the return calculation. We strongly believe that you should recommend that Advisers use composite performance that includes all portfolios managed to a specific strategy. Determining which portfolios are included in return calculations requires the establishment of robust policies and procedures, to prevent cherry picking and to fairly represent performance.

24. *(p. 139) Are the proposed definitions of "gross performance," "net performance," and "portfolio" clear? Should we modify any of those proposed definitions?*

CFA Institute Response: We have divided the answer into 4 sections: "Pure" Gross Performance, Gross Performance, Net Performance, and Portfolio.

a) "Pure" Gross Performance

We recommend adding a definition that defines pure gross performance as the performance results of a portfolio before the deduction of actual transaction costs incurred during the period when actual transaction costs could be deducted.

b) Gross Performance

SEC Proposed Definition: Gross performance means the performance results of a portfolio before the deduction of all fees and expenses that a client or investor has paid or would have paid in connection with the investment adviser's investment advisory services to the relevant portfolio.

GIPS Standards Definition:

- *Composite gross-of-fees return: The return on investments reduced by any transaction costs.*
- *Pooled fund gross return: The return on investments reduced by any transaction costs.*

We have the following comments on the term gross performance:

- "Advisory fees paid to underlying investment vehicles" is listed as a fee deducted from net performance, but this should also be deducted for gross performance.
- The proposed definition does not state that gross returns must reflect the deduction of transaction costs. We believe gross returns should be required to reflect the deduction of transaction costs, if any exist.
- The proposed definition refers to the performance results "of a portfolio." We recommend clarifying that this applies to any portfolios or portions of portfolios included in performance. This would then capture all types of relevant performance, including related performance and extracted performance.

c) <u>Net Performance</u>

SEC Proposed Definition:

Net performance means the performance results of a portfolio after the deduction of all fees and expenses that a client or investor has paid or would have paid in connection with the investment adviser's investment advisory services to the relevant portfolio, including, if applicable, advisory fees, advisory fees paid to underlying investment vehicles, and payments by the investment adviser for which the client or investor reimburses the investment adviser. For purposes of this rule, net performance may reflect one or more of the following

(i) The deduction of a model fee when doing so would result in performance figures that are no higher than if the actual fee had been deducted;

(ii) The deduction of a model fee that is equal to the highest fee charged to the relevant audience of the advertisement; and

(iii) The exclusion of custodian fees paid to a bank or other third-party organization for safekeeping funds and securities.

GIPS Standards Definitions:

- *Composite net-of-fees return: The gross-of-fees return reduced by investment management fees*
- *Pooled fund net return: The pooled fund gross return reduced by all fees and expenses, including investment management fees, administrative fees, and other costs.*

We have the following comments on the term net performance:

- The proposed definition does not state that net returns must reflect the deduction of transaction costs. We believe net returns should be required to reflect the deduction of transaction costs, if any exist.
- We believe that pooled fund net returns should be a separate term and should be distinguished from composite/account/extracted net performance. When a client invests in a pooled fund, they cannot opt out of the custody and other administrative fees. These fees and expenses are not paid to the Adviser, so would not qualify as fees and expenses that a client or investor has paid or would have paid in connection with the Adviser's investment advisory services. Even though the term "portfolio" includes pooled investments vehicles, these fees and expenses are not captured by the proposed definition. We believe that when an Adviser is selling participation in a specific fund, and is presenting performance of that fund, net performance for that fund should be net of all fees that an investor would pay. If a pooled fund is included in a composite, or related performance, we believe that net returns should follow the requirements of any other portfolio, and not be required to reflect the deduction of other fees and expenses. In this instance, the pooled fund is simply a portfolio included in the composite, just like any other portfolio managed by the Adviser.
- We do not understand this part of the net performance definition, so recommend clarifying this language: "and payments by the Adviser for which the client or investor reimburses the investment adviser."
- The proposed definition refers to the performance results "of a portfolio." We recommend clarifying that this applies to any portfolios or portions of portfolios included in performance. This would then capture all types of relevant performance, including related performance and extracted performance.
- In (ii) the proposed rule states that the "highest fee charged" may be used as a model fee. We recommend changing this to "the highest fee charged or would be charged" because the Adviser may not yet manage an actual account similar to the relevant audience. For example, an advertisement might include performance of a seed account and the Adviser applies a model fee consistent with the proposed fee schedule that a client would pay.
- In (ii) the proposed rule refers to the "relevant audience." In other parts of the rule, the audience is referred to as "the person to whom the advertisement is disseminated." We recommend using similar language here or, if there is an intended difference, explaining the difference.

d) Portfolio

SEC Proposed Definition: Portfolio means a group of investments managed by the investment adviser. A portfolio may be an account or a pooled investment vehicle.

> *GIPS Standards Definition: An individually managed group of investments. A portfolio may be a segregated account or a pooled fund, including assets managed by a sub-advisor for which the firm has discretion over the selection of the sub-advisor.*
>
> We agree with the proposed definition.

Do we need to define any other terms?

CFA Institute Response: As noted above, we believe you should define "pure gross return" and "pooled fund net return."

25. *(p. 139) For the proposed definition of "portfolio," should we modify the term "managed by the investment adviser" – e.g., to specify how this term addresses sub-advisory relationships or other relationships? If so, how should we modify the term?*

CFA Institute Response: We believe that language could be added but it is not necessary.

26. *(p. 139) For the proposed definition of "net performance," should we add or remove any item from the non-exhaustive list of fees and expenses to be considered? If so, which item and why?*

CFA Institute Response: As stated above, we recommend adding transaction costs to make it clear that net returns must reflect the deduction of transaction costs.

Are there particular items that might not be considered a "fee" or an "expense" that should nonetheless be deducted in calculating net performance? If so, which item and why?

CFA Institute Response: We do not believe there are other items that should be deducted, however, just to be clear, we believe that sales loads and charges should not be required to be deducted when calculating net returns for pooled funds.

27. *(p. 140) Are the proposed modifications to "net performance" appropriate?*

CFA Institute Response: We believe that the proposed modifications are appropriate.

Are there particular changes to the proposed modifications that we should make?

CFA Institute Response: Please see our comments above for proposed changes to the definitions. Also, if a term for pooled fund net returns is created, the concept of choosing a single share class or series, or limited partner fee schedule versus a client fee schedule, will need to be included.

Should we include any other permitted deductions?

CFA Institute Response: We do not believe there should be any other permitted deductions.

28. (*p. 140) Are there instances in which we should expressly require that "net performance" be*

calculated to reflect the deduction of a custodial fee – for example, in all circumstances other than where an advisory client selects its own custodian and directly negotiates the custodial fee?

CFA Institute Response: For advisory clients, we do not believe that net returns should be required to reflect the deduction of custody fees. As stated above, we believe that net returns for pooled investment vehicles, where clients cannot "opt out" of custody or other administrative costs, should be required to reflect the deduction of all of these fees and costs, when the Adviser is presenting net returns of a specific fund.

Are we correct in our understanding that if advisory clients select and pay directly their custodians, investment advisers may not know the amount of custodial fees?

CFA Institute Response: That is correct. Because the client selects the custodian, we do not believe the Adviser should be required to reflect the deduction of custodial fees. If this approach is taken, whether the Adviser knows the amount of custodial fees or not is irrelevant.

Are there other types of fees or expenses that investment advisers would be unable to deduct in calculating net performance and that the proposed rule should treat similarly to custodial fees?

CFA Institute Response: There are no other fees or expenses that we believe should be deducted when calculating net performance for advisory clients or need to be treated similar to custodial fees.

29. *(p. 140) Are there circumstances under which investment advisers might seek to calculate gross performance and net performance using different types of returns or methodologies or to use different types of returns or methodologies for different portions of a presented period? What are those circumstances? Should we take those circumstances into account? If so, why and how?*

CFA Institute Response: We agree that any comparison between gross performance and net performance should only be attributable to the effect of fees and expenses that are required to be deducted and believe that it would be helpful to have this explanation included in the adopting release.

Advisers will use different methodologies over time, and this should be allowed. As technology has improved over the decades, more and more firms are moving from a monthly calculation to a daily calculation. It should be clear that different methodologies can be used for different portions of a presented period. The key is that any contrast between gross performance and net performance should demonstrate the effect of fees and expenses.

30. *(p. 140) Should the proposed rule include different or additional criteria for Retail Advertisements in order to enable Retail Persons to compare performance between investment advisers? If so, what criteria and why?*

CFA Institute Response: As discussed above, we believe any retail advertisement should include information about the fees that a retail client will pay. This is different from the proposed disclosure about fees that were used to calculate net returns. Those fees could differ from the fees that the client will pay. Requiring disclosure of proposed fees will allow a retail client to compare expected future fees between Advisers.

31. *(p. 140) Instead of requiring Retail Advertisements presenting gross performance to provide or offer to provide promptly a schedule of fees and expenses, should we require that Retail Advertisements include disclosure about fees and expenses (i.e., without an itemized schedule)? What information about fees should the proposed rule require to be included in Retail Advertisements?*

CFA Institute Response: Even though a Retail Advertisement that includes gross performance would also include net performance, we believe that the following items should be required disclosures in any retail advertisement:

- The type of fees (actual or model) that were used to calculate net of fee returns.
- Fees a retail investor should expect to pay.
- If the net returns reflect different fees from those fees that a retail client should expect to pay.
- If a retail client should expect to pay any other fees or expenses beyond the fees utilized in the calculation or presented in the fee schedule.

32. *(p. 141) Should the proposed requirement to provide or offer a schedule of fees and expenses apply differently to different types of fees and expenses (e.g., custodial fees or other administrative fees as opposed to advisory fees)? Should the proposed requirement to provide or offer a schedule of fees and expenses apply differently to advertisements presenting the performance of pooled investment vehicles and advertisements presenting the performance of separate accounts? If so, why and how?*

CFA Institute Response: We believe the requirements should be different for pooled fund advertisements versus advertisements targeted for separate accounts. For separate accounts, we believe that the management fee details should be spelled out. For pooled funds, we suggest requiring disclosure of the pooled fund's current expense ratio, versus listing individual fees and costs as a percentage of assets under management.

33. *(p. 141) Should we take the position that an investment adviser would "provide" the schedule of fees and expenses if the advertisement includes a hyperlink that enables the audience to obtain and review the schedule?*

CFA Institute Response: We believe that if the medium allows for disclosure of the schedule of fees and expenses, or the expense ratio, then the fee schedule or expense ratio should be required

to be included in the advertisement. We do not find a hyperlink to be helpful, particularly for a retail client. Using a hyperlink would place the burden on the client to obtain the information. We believe that an Adviser should be required to provide any necessary information.

34. *(p. 141) As proposed, the schedule of fees and expenses would need to be presented in percentage terms and on the basis of assets under management in calculating net performance. Should we allow it to be presented in other formats as well?*

CFA Institute Response: There are rare instances where investment advisory fees are not charged based on a percentage of assets under managements, e.g., management fees are a flat fee of $xxx per year. The requirement could be modified to state that the fee schedule can be presented in percentage terms or as otherwise charged. Alternatively, in the spirit of remaining timeless, you could remove "presented in percentage terms" from the rule since different types of fee schedules are emerging in the industry. We do not believe that a format needs to be specified in the rule.

When presenting performance of a specific pooled fund, we suggest requiring disclosure of the pooled fund's current expense ratio, versus listing individual fees and costs as a percentage of assets under management.

Alternatively, should we require the schedule to be presented in another format? For example, should advisers be required to present the schedule in terms of the actual dollar amount paid or borne on a portfolio of a specific size, or the actual dollar amount paid or borne on the actual portfolio being managed and advertised?

CFA Institute Response: We do not believe that a fee schedule in terms of the actual dollar amount paid is helpful when fees and expenses are charged relative to the size of the portfolio. Without having detailed information about the size of the assets against which the expenses were charged, a prospect would have no idea what the impact of any fees would be, and this approach would not lend itself to comparability across Advisers.

Are there other formats that would work better than dollar or percentage terms?

CFA Institute Response: We generally believe that investment management fee schedules should be based in percentage terms and total pooled fund expenses should be disclosed through a current expense ratio. However, in the spirit of remaining timeless, we do not believe that a format needs to be specified in the rule because different types of fee schedules are emerging in the industry.

Would allowing an alternative presentation format, in addition to a format using percentage terms, be confusing or misleading?

CFA Institute Response: We generally believe that investment management fee schedules should be based in percentage terms and total pooled fund expenses should be disclosed through a current expense ratio. We believe that other formats could be confusing. However, in the spirit of remaining timeless, we do not believe that a format needs to be specified in the rule because different types of fee schedules are emerging in the industry.

Is it clear how an adviser would calculate net performance if it does not charge asset-based fees?

CFA Institute Response: For performance-based fees, which are typically used for a non-retail audience, the calculation can be quite complex. However, most non-retail investors who agree to a performance-based fee calculation understand the nuances and complexities, and often provide the formula that must be used to calculate the performance-based fee. If you are asking about calculating net returns using model fees or fixed fees, we do not believe you should specify how returns must be calculated. There is no single correct way to do these calculations. However, we believe that you should include, in the adopting release, a recommendation for Advisers to accrue fees and to reflect the effect of fees in the period for which the fee was earned.

35. *(p. 142) Are there any compliance challenges that investment advisers might face in preparing a schedule such as the type proposed?*

CFA Institute Response: We have no additional comments.

Under current law, have investment advisers included in their advertisements similar offers to provide schedules or other breakdowns of fees and expenses, or have investment advisers provided the fee and expense information?

CFA Institute Response: Advisers that comply with the GIPS standards are required to disclose the relevant fee schedule in a GIPS Report. Referring to another document that contains the fee information, such as an ADV, is not allowed. However, Advisers are not required to include a fee schedule in an advertisement that is prepared following the GIPS Advertising Guidelines. We recommend not requiring a fee schedule to be disclosed in non-retail advertisements, but instead suggest requiring that an Adviser either include the fee schedule in the non-retail advertisement or subsequently provide it. We do not believe that an offer to provide a fee schedule suffices. We believe that all prospective clients should receive a detailed fee schedule.

Are there types of fees and expenses for which providing a schedule would be particularly difficult?

CFA Institute Response: It may be difficult to determine a precise amount for fees and expenses other than investment management fees as a percentage of assets under management. This is particularly true when assets of a pooled fund are volatile. This would only be applicable for pooled funds. As mentioned previously, we instead recommend requiring disclosure of the current expense ratio when presenting performance of a specific pooled fund.

Do advisers expect that they would need to account for estimated, rather than actual, fees and expenses in certain cases?

CFA Institute Response: As mentioned above, it may be difficult to determine a precise amount for fees and expenses other than investment management fees. Advisers should be allowed to make reasonable estimates of the percentage of other fees and expenses, or of the expense ratio.

36. *(p. 142) Would there be circumstances in which investment advisers might have to provide proprietary or sensitive information to comply with this proposed requirement? Should we take those circumstances into account? If so, how?*

CFA Institute Response: Some Advisers consider fee schedules to be sensitive information and are reluctant to disclose this information. However, we believe that a client should understand the fees and expenses that they will pay, and the need for transparency is more important than protecting the Adviser's information. Because an Adviser would not be required to include the fee schedule in the advertisement (although we propose requiring a fee schedule in retail advertisements), we do not think you need to take these circumstances into account.

37. *(p. 142) Should we prescribe specific time periods as proposed? Are one, five, and ten years the right periods to be used? Instead, for example, should we require that performance always be presented since inception of a portfolio?*

CFA Institute Response: As previously stated, we generally support prescribing specific time periods. Please see our response to question 18 on page 16 of this letter under "Prescribed Time Periods.". We do not believe you should require since inception performance. Some Advisers have performance that goes back decades, and this performance will not promote comparability.

38. *(p. 142) Are there other time periods for which we should require the presentation of performance results?*

CFA Institute Response: As mentioned above, we recommend requiring 3-year annualized returns in addition to 1-, 5-, and 10-year annualized returns. We also believe you should allow money-weighted returns instead of time-weighted returns when the Adviser controls the cash flows. In such cases, when an Adviser chooses to present a money-weighted return, we suggest requiring Advisers to instead present only one return, an annualized since inception money-weighted return

Are there any specific compliance issues that an investment adviser would face in generating and presenting performance results for the required time periods?

CFA Institute Response: As mentioned above, the 1-, 5-, and 10-year requirement would not make sense for Advisers that use money-weighted returns. Also, the requirement to present 1-, 5-, and 10-year returns will put a burden on Advisers claiming compliance with the GIPS standards that present annual returns in their GIPS-compliant reports as required by the GIPS standards, if the GIPS reports will be distributed to retail investors. Please see our response to question 18 on page 16 of this letter, under "Prescribed Time Periods" for our suggestions on how to address this issue.

39. *(p. 143) Should we require an adviser without any performance results available for a particular period required in Retail Advertisements to disclose specifically that the adviser does not have those results? For example, should an adviser having a track record of only*

eight years for a portfolio be required to disclose that it does not have performance results for the required 10-year period?

CFA Institute Response: We agree with the proposed rule that requires a since inception annualized return for Advisers that do not have a 10-year history. We believe that presenting a since-inception return and properly labelling it with the inception date would inform the prospect of the inception date and why the Adviser does not present the required 10-year return. We believe you should explain in the adopting release that a since inception return needs to be properly labelled or disclosed.

40. *(p. 143) Should we impose any additional requirements for presentation of the time periods proposed? For example, beyond the proposed rule's requirement that the specified time periods end "on the most recent practicable date," should we require that performance results be current as of a particular date? For example, should we require that the specified time periods end on a date no greater than 90 days prior to dissemination of the* advertisement? Would some period other than 90 days be appropriate?

CFA Institute Response: To allow for GIPS Reports to be standardized and used throughout the year, we suggest that you reconsider the requirement to present performance as of "the most recent practicable date," or provide guidance specific to GIPS Reports. Please see our response to question 18 on page 16 of this letter, under "Prescribed Time Periods" for our suggestions on how to address this issue.

Should we provide guidance about the term "most recent practicable date"? If so, what guidance should we provide?

CFA Institute Response: Please see our response to question 18 on page 16 of this letter, under "Prescribed Time Periods" for our comments regarding GIPS Reports. Other than GIPS Reports, we do not believe it is possible to provide further guidance about the term "most recent practicable date" that is appropriate for all Advisers and strategies. Even if flexibility was provided to Advisers such that they were able to create their own policies and procedures by strategy, it would be a challenge to adhere to these policies since there will be exceptions (e.g., if the Adviser found an error and is in the process of correcting it, the Adviser will not be able to update performance per their policy).

c. ***Additional Requirements for Presentations of Performance in All Advertisements (p. 143)***

1. *(p. 145) Are there types of statements that would be prohibited under the proposed approval prohibition, but that commenters believe should be allowed in performance advertising? What types of statements and why should they be allowed?*

CFA Institute Response: We agree with the proposed prohibition.

2. *(p. 145) Instead of including a specific approval prohibition, should we take the view that a statement that would otherwise violate this prohibition is addressed through paragraph (a) of the proposed rule?*

CFA Institute Response: We believe it is helpful to include the specific approval prohibition.

ii. Related Performance (p. 145)

1. *(p. 150) Are the proposed definitions of "related performance" and "related portfolio" clear? Should we modify these proposed definitions?*

SEC Proposed Definitions:

> *Related performance* means the performance results of one or more *related portfolios*, either on a *portfolio*-by-*portfolio* basis or as one or more composite aggregations of all *portfolios* falling within stated criteria.
>
> *Related portfolio means a portfolio with substantially similar investment policies, objectives, and strategies as those of the services being offered or promoted in the advertisement. Related portfolio includes, but is not limited to, a portfolio for the account of the investment adviser or its advisory affiliate, as defined in the Form ADV Glossary of Terms.*

CFA Institute Response:

We believe that the definition of related performance should be modified, to allow for the use of representative portfolios. It is unclear if a representative portfolio is considered under the proposed definitions of related portfolio or related performance. The definition of related performance refers to "one or more related portfolios." "One" would seem to indicate a representative portfolio. However, the definition provides only two options for presenting performance: on a portfolio-by-portfolio basis or as one or more composite aggregations. We believe representative portfolio performance should be clearly presented as an option in the definition of related performance in the Rule. We also recommend including a definition of representative portfolio. It could be defined as "a related portfolio that is determined by the Adviser to be most representative of a specific strategy." Please also see our response to question 3 below on page 31, which addresses the concept of reporting performance on a portfolio-by-portfolio basis.

We also recommend defining the term "composite." The term "composite" is used multiple times within the proposed rule and definitions, including within the definition of related performance. We believe composite could be defined as an aggregation of all portfolios falling within stated criteria for a specific strategy.

Should we provide further guidance as to what constitutes a "related portfolio"?

CFA Institute Response: Please see our comments to the prior question. We agree with the guidance you provided for determining what qualifies as a related portfolio.

2. *(p. 151) Should we modify the proposed definition of "related portfolio" by changing the "substantially similar" criterion? If so, how and why?*

CFA Institute Response: We believe that the substantially similar criterion is appropriate.

> *Should we modify the proposed definition by specifying how an adviser should account for portfolios that are non-discretionary accounts? Should we modify the proposed definition of "related portfolio" to take into account how client-specific constraints may have affected the performance of portfolios that otherwise have "substantially similar" policies, objectives, and strategies?*

CFA Institute Response: We do not believe that you should modify the proposed definition of related portfolio to address non-discretionary accounts or portfolios with client-specific constraints. If a portfolio has a substantially similar investment policy, objective, or strategy as those of the services being offered, the Adviser should be allowed to present that performance. We believe that It would be helpful to include an example in the adopting release that would illustrate why it might be appropriate to advertise the performance of a portfolio that is considered a non-discretionary account for composite assignment purposes. For example, a fixed income portfolio restricts the use of futures to adjust duration, which is part of the Adviser's mandate, and the portfolio is considered non-discretionary for composite assignment purposes. If the Adviser decides to offer a fixed income strategy that does not include the use of futures, it might be appropriate to advertise the performance of this non-discretionary account.

> *Would investment advisers consider portfolios having such client- specific constraints to be portfolios that have policies, objectives, and strategies that are not "substantially similar"?*

CFA Institute Response: We believe that each Adviser must determine for itself whether portfolios having client-specific constraints would be considered "substantially similar." There are many variations on mandates and constraints.

3. *(p. 151) Would the proposed rule's approach of allowing related performance to be presented on a portfolio-by-portfolio basis or as one or more composites have the intended effect of illustrating the differences in performance achieved in managing related portfolios?*

CFA Institute Response:

We believe that presenting performance on a portfolio-by-portfolio basis would be helpful in very limited situations. As mentioned in your discussion, it would only be realistic to use portfolio-by-portfolio performance when an Adviser has a few accounts. When there are many accounts it may be unwieldy and difficult to comprehend portfolio-by-portfolio performance. Additionally, we believe there would be limited value in seeing performance for each portfolio. If each of the portfolios is a related portfolio, the range of returns between the portfolios should be quite small. We believe a composite that includes all portfolios managed in a specific strategy is the best way to show related performance. We do not believe the portfolio-by-portfolio option is practical or realistic for many managers. If an Adviser wishes to show a range of individual

portfolio returns, such as high-low, it could present this metric alongside the composite returns. Additionally, if a prospective client has a specific customization request and the Adviser manages an account with that same customization, an Adviser could provide that related portfolio's performance either by itself or along with composite performance.

The discussion of the proposed rule states:

> *To the extent that an investment adviser excludes portfolios from a composite that is constructed for GIPS purposes, the proposed rule would allow those portfolios to be included in a separate composite. That is, "related performance" could be presented through more than one composite aggregation of all portfolios falling within the stated criteria.*

We believe that Advisers should be allowed to present one or more composites in an advertisement. However, we are unclear how there can be more than one composite aggregation within the stated criteria. For any specific strategy, which we assume is what "stated criteria" refers to, we believe there should be one appropriate composite, or group of related portfolios. Advisers can certainly have closely related composites, but they should represent different strategies. Portfolios can also be included in more than one composite. This would happen when there is broadly defined composite that includes a larger set of accounts, and then a more narrowly defined composite that includes a subset of accounts. For example, an Adviser could create a broad composite that includes all fixed income portfolios managed to an intermediate-duration benchmark. The Adviser might also create narrow sub-composites based on the specific benchmarks. The Adviser can show the prospective investor the performance for the broad intermediate duration strategy and the performance relative to a specific benchmark. However, the two composites would each have their own stated criteria.

> *Are there other better approaches, including approaches that investment advisers use currently that we should consider? What approaches and why?*

CFA Institute Response: As previously mentioned, we strongly believe that composite performance is the most appropriate performance to represent an Adviser's history managing a specific strategy. Using composite performance eliminates many of the concerns about how portfolios were selected. Within the adopting release, we request that you add language that encourages the use of composite performance when marketing advisory services.

4. *(p. 151) Would the proposed rule's approach of allowing related performance to be presented in "one or more composite aggregations" be appropriate or should we require that related performance be presented in only one such composite? Why or why not?*

CFA Institute Response: Please see our response to question 3 on page 31 above.

5. *(p. 151) Rather than allowing related performance to exclude related portfolios as long as the advertised performance results are no higher than if all related portfolios had been included, should we require inclusion of all related portfolios? Why or why not?*

CFA Institute Response: The Horizon no-action letter allows for the presentation of performance of all accounts managed in a substantially similar manner from a prior entity, unless the exclusion of any such account would not result in materially higher performance. This concept, whereby an advertisement can include performance that excludes one or more related portfolios, so long as the advertised performance results are no higher than if all related portfolios had been included, is appropriate when considering performance from a prior entity, because it may not be possible to gather the information for all related portfolios from a prior entity. However, we do not agree with the expansion of this concept to the proposed rule. To determine if the results are "no higher than if all related portfolios had been included," the Adviser would be required to calculate performance including all related portfolios – that is, it must calculate proper composite performance. We believe that this proper composite performance should be used in an advertisement. Additionally, it would be extremely challenging to implement the test to ensure that results are "no higher than" the proper composite for each period that is included in the track record. We tried to imagine the procedures that an Adviser would need to implement to ensure this test was met and believe that clear guidance would need to be provided for how an Adviser can make this assessment. For example, would this test need to be met for each individual period? Should the test be conducted for both gross and net returns if both are included in the advertisement, or only for one set of returns? Could the Adviser switch between asset-weighted and equal-weighted composite returns, if the test is met using one method but not the other? Would the Adviser be required to conduct this test and pass this test for each period presented in the advertisement? Would it be appropriate for the Adviser to change the accounts that are included in the calculation each period, leading to different accounts being included in each period's return calculation? We suggest that these exceptions be removed from the rule and be allowed only for portability situations.

Also, we recommend including in the Adopting Release the concept that using composite performance is always preferred to using the performance of selected accounts. Using "proper" composite performance eliminates many of the concerns about how portfolios were selected. Within the adopting release, we request that you add language that encourages the use of composite performance when marketing advisory services.

We appreciate, however, that some Advisers that manage separate accounts may not maintain composites that include all portfolios managed in a specific strategy, and that flexibility as to the performance that may be included in an advertisement is needed. In such cases, we believe that Advisers should be allowed to use related performance, including performance of a single representative portfolio.

> *Alternatively, should we permit exclusion of related portfolios as long as the advertised results are not "materially" higher than if all related portfolios had been included? Why or why not?*

CFA Institute Response: We believe that Advisers should not be allowed to exclude portfolios on the basis that the returns were not "materially" higher, for the same reasons we stated above. In addition, this option could lead to "cherry picking."

As an alternative to any of those approaches, should we allow related performance without limitation and instead rely on the prohibitions in the rest of the proposed rule to ensure that performance of related portfolios is presented in a fair and balanced manner?

CFA Institute Response: We believe that having limitations on the information that can be presented is very helpful. Using a composite should be encouraged since it is presenting performance in a fair and balanced manner. We also believe that Advisers should be allowed to use performance of a pooled vehicle when marketing a specific pooled vehicle, if performance for that pooled vehicle exists.

6. *(p. 152) Rather than requiring that the exclusion of any related portfolio does not alter the presentation of time periods prescribed for Retail Advertisements, should we allow the exclusion to alter such presentation? Why or why not? Should we provide additional guidance regarding this requirement? If so, what additional guidance should we provide?*

CFA Institute Response: As discussed above, we do not believe the exclusion of any related portfolios from related performance should be allowed.

7. *(p. 152) Are there particular disclosures we should require when an advertisement presents related performance?*

CFA Institute Response: We believe retail advertisements should include required disclosures. Please see our response to question 1.

Should we require that an advertisement offer to provide additional information about the related performance? For example, if the investment adviser presents related performance as a composite, should the adviser be required to offer to provide the performance of the individual portfolios used to calculate that composite?

CFA Institute Response: We do not believe this would be practical or helpful. Sometimes a composite will contain hundreds, if not thousands, of portfolios. If the composite is defined appropriately, the performance of the composite will represent the overall strategy.

8. *(p. 152) Should we consider adopting FINRA's approach and prohibit the presentation of related performance in Retail Advertisements? Why or why not? If we do not adopt FINRA's approach, would it cause confusion for advisers or investors?*

CFA Institute Response: We do not believe you should adopt FINRA's approach and prohibit the presentation of related performance in retail or non-retail advertisements. As stated previously, we believe that the ability to use related performance in all advertisements is very meaningful and relevant to all investors, and the inability to use related performance in certain situations withholds important information from investors. In our opinion, an investor who is deciding whether or not to purchase a pooled investment vehicle would want to see an Adviser's experience in managing accounts to the same strategy. We believe Advisers should be allowed to present fund performance and/or related performance when advertising a specific fund. If an

Adviser chooses to show related performance when advertising a fund, any differences between the accounts included in the related performance and the fund, including differences in fees and costs, should be made clear through disclosure.

9. *(p. 152) Would investment advisers that seek to comply with GIPS face any compliance challenges in complying with the proposed rule's related performance provision? If so, what challenges and how would such advisers seek to address them?*

CFA Institute Response: Advisers that comply with the 2020 edition of the GIPS standards would face the following compliance challenges:

- The requirement for Advisers to show related performance to pooled fund investors would not be consistent with the GIPS standards. The GIPS standards permit Advisers to present performance of the specific fund for which the Adviser is selling participation.
- Requiring 1-, 5-, and 10-year performance through the most recent practicable date would differ from the GIPS standards in several ways:
    - The GIPS standards require Advisers to show annual performance when using time-weighted returns.
    - The GIPS standards allow an Adviser to select the end date of the annual period. Most Advisers present annual periods through the prior calendar year end. The end date would therefore differ from the most recent practicable date for much of the year. The Adviser would then need to update GIPS Reports throughout the year, to include the updated 1-, 5-, and 10-year annualized returns.
    - The rule does not contemplate the use of money-weighted returns versus time-weighted returns. It is not clear how these standardized time periods would apply to money-weighted returns. If a composite or pooled investment vehicle meets specified criteria and the Adviser chooses to present money-weighted returns, the GIPS standards require a single annualized since-inception money-weighted return. Advisers typically present returns in GIPS Reports through the most recent calendar year end. The end date would therefore differ from the most recent practicable date for much of the year. The Adviser would then need to update GIPS Reports throughout the year, to include returns through the most recent practicable date.
- In most instances an Adviser may present either gross or net returns in GIPS Reports. Under the proposed rule, net returns would be required in GIPS Reports that are used for retail clients. However, it is common practice for Advisers that are SEC registrants to include net returns in all GIPS Reports in accordance with the Clover Capital no-action letter.
- When selling participation in a specific pooled fund, and presenting the performance of that fund, the GIPS standards require net returns that reflect the deduction of all fees and expenses, including administrative fees. The proposed rule requires net returns that reflect

the deduction of only fees and expenses in connection with the Adviser's investment advisory services.

- The GIPS standards require composites to include all portfolios that are managed in the composite's strategy. Advisers are not allowed to exclude from the composite portfolios meeting the composite definition even if the exclusion generates results that are no higher than if all portfolios had been included.
- The GIPS standards permit the use of a model investment management fee. However, net returns calculated using the model investment management must be equal to or lower than returns calculated using actual investment management fees. The GIPS standards do not permit the application of a model investment management that generates net returns that are higher than returns calculated using actual investment management fees. However, we support the new proposal to allow for the use of model fees that are applicable to the prospect. In a GIPS Report this information can be presented as supplemental information.
- The GIPS standards do not consider targeted returns to be hypothetical performance.
- The GIPS standards do not require the application of a model fee to non-fee-paying portfolios when net returns are calculated. While it is common for institutional Advisers to use model fees for composite performance, this is not the case for all Advisers. Requiring the application of a model fee to non-fee-paying portfolios may result in many Advisers being required to restate historical performance.

Should we take those challenges into account and, if so, how?

CFA Institute Response: We hope that you will consider making the following changes to the rule, all of which are discussed in response to other questions:

- Allow Advisers to present fund-specific performance when advertising a fund.
- Allow the use of related performance in all advertisements, including those that are selling participation in a specific fund
- Allow money-weighted returns versus time-weighted returns when an Adviser controls the cash flows.
- Reconsider the requirement to present performance as of "the most recent practicable date," or provide guidance specific to GIPS Reports.
- Differentiate between related performance net returns and pooled investment vehicle net returns.
- When presenting performance of a specific fund, require that pooled fund net returns reflect the deduction of all fees and expenses, including administrative fees.
- Remove the exception to exclude portfolios from related performance even if the exclusion generates results that are no higher than if all portfolios had been included.
- Remove targeted returns from the definition of hypothetical performance.

- Allow Advisers to either apply model fees to non-fee-paying portfolios or to disclose the fact that non-fee-paying assets are included in the advertisement. In the latter case, the Adviser should be required to offer to provide information about the effect of such non-fee-paying assets on the returns.

Are there particular provisions of GIPS that we should consider in addressing the presentation of related performance?

CFA Institute Response: We have no additional comments.

10. *(p. 153) Should we retain the proposed rule's inclusion in the definition of "related portfolio" of a portfolio managed by the investment adviser for its own account or for its advisory affiliate? Why or why not?*

CFA Institute Response: We believe portfolios managed for an Adviser's own account or for it advisory affiliate should be considered related portfolios. This assumes the Adviser has discretion to manage the portfolio. The ownership of the assets should not affect whether the Adviser can present the portfolio's performance.

We have indicated that to satisfy the "net performance" requirement when presenting performance of a portfolio that belongs to the adviser or its affiliate, the adviser generally should apply the fees and expenses that an unaffiliated client would have paid in connection with the relevant portfolio whose performance is being advertised. Do commenters agree with this approach?

CFA Institute Response: We generally agree with this approach. However, this approach is different from the approach that the GIPS standards have taken and this could be a big change for Advisers that calculate composite net returns using actual fees. When an Adviser includes non-fee-paying portfolios in a composite and calculates net returns using actual investment management fees, the GIPS standards require disclosure of the percentage of assets represented by non-fee-paying portfolios as of each annual period end. This allows a reader to understand the potential effect of the non-fee-paying portfolios on composite returns. If this proposed new requirement were to come into effect, many Advisers will have to historically re-calculate and restate returns for any composite that included a non-fee-paying portfolio. We recommend providing flexibility here, to allow an Adviser to either apply model fees to non-fee-paying portfolios or to disclose the fact that non-fee-paying assets are included in the performance presented and offer to provide information about the effect of such non-fee-paying assets on the net returns. We think providing information about the effect of these non-fee-paying assets on the net returns presented would be sufficient to make related performance not misleading.

iii. Extracted Performance (p. 153)

1. *(p. 157) Are there circumstances under which extracted performance should be prohibited in Retail Advertisements? What types of circumstances?*

CFA Institute Response: We believe that when extracted performance is advertised as a standalone strategy, it should be required to have an allocation of cash.

Additionally, in any advertisement, when advertising extracted performance as a standalone strategy, we believe that the extracted performance must be representative of a distinct investment strategy (i.e., representative of a portfolio dedicated to that strategy).

If these two conditions are not met when presenting performance for a standalone strategy, we believe that extracted performance should be prohibited.

2. *(p. 157) Are there specific disclosures that we should require to decrease the likelihood that extracted performance would be misleading in Retail Advertisements (e.g., describing the fact that the performance does not represent the entire performance of any actual portfolio of an actual client of the investment adviser)? If so, should we identify those and specifically require their disclosure?*

CFA Institute Response: The disclosures mentioned in the discussion are as follows:

- Performance of the total portfolio (within the advertisement or offer to provide promptly)
- The extracted performance is only one particular strategy of the entire portfolio which had multiple strategies
- Whether the extracted performance reflects an allocation of the cash held by the entire portfolio from which the performance is extracted and the effect of such cash allocation, or of the absence of such an allocation, on the results portrayed
- The criteria used to extract the investments

Additionally, you mention that the following would be misleading:

- If the extracted performance excludes investments that fall within the criteria the Adviser represents it used to select the extract,
- Presenting performance time periods in a manner that is not fair and balanced.

We generally agree with this. However, when extracted performance is being advertised as a standalone strategy, we question the relevance of the performance of the total portfolio. Using your example, we don't know how meaningful performance of a multi-strategy portfolio would be for an investor who is interested in a fixed income mandate. This would get particularly complex if the Adviser includes in the extracted performance pieces of portfolios whose total accounts are managed in different strategies. However, we see the relevance when segment returns, or attribution, of a total portfolio are presented in an advertisement.

As mentioned previously, when presenting extracted performance as a standalone strategy, we believe there needs to be a fundamental belief by the Adviser that the extraction represents a strategy that could be managed as a standalone portfolio. Extracting the performance of two French equities from a global equity portfolio and presenting this as a French equity strategy

would be misleading. Under the GIPS standards, in order to include a "carve-out" in a composite, an Adviser must believe that the carve-out is representative of a stand-alone account managed or intended to be managed to that strategy. This would not be the case for the French equity extraction. We recommend including this concept in the rule.

Finally, we believe that detailed information about the criteria used to extract the investments could be overwhelming for a retail audience. We recommend instead allowing Advisers to either disclose the information in the advertisement or offer to provide the information on request. We believe the latter approach would be more meaningful than having long disclosures describing the logic, assumptions, and methodology.

3. *(p. 157) Is the proposed definition of "extracted performance" sufficiently clear based on our description above? Should we modify any of the elements of the proposed definition? If so, which element and why?*

CFA Institute Response: Below are the proposed definition of extracted performance and the definition of a carve-out under the GIPS standards:

> SEC Proposed Definition of Extracted Performance: the performance results of a subset of investments extracted from a portfolio
>
> GIPS Standards Definition of Carve-Out: A portion of a portfolio that is by itself representative of a distinct investment strategy. It may be used to create a track record for a narrower mandate from a multiple-strategy portfolio managed to a broader mandate.

The rule and discussion seem to imply that extracted performance is performance that is extracted from a single portfolio. While this may be the case, our experience is that extracted performance is typically not based on a single portfolio but is instead drawn from multiple portfolios. We believe that extracted performance should be subject to the same requirements as non-extracted performance, i.e., the related performance should be based on one or more related portfolio extracts.

Finally, we believe that guidance should be provided in the adopting release as to what types of performance "extracted performance" covers. For example, does it cover attribution?

4. *(p. 157) Under the current rule, have investment advisers taken the same approach that we take in the proposed rule with respect to extracted performance – i.e., providing or offering to provide the performance results of the entire portfolio from which the performance is extracted?*

CFA Institute Response: We have not observed Advisers taking the same approach as the proposed rule when advertising extracted performance as a standalone strategy. The GIPS standards require that if an Adviser allocates cash to a carve-out and includes the carve-out in a composite that it must do the same for all similar portfolio segments managed by the Adviser. Continuing with your example, if an Adviser carves out the fixed income segment from a multi-

asset class portfolio, it must do the same for all similar fixed income segments from all portfolios managed by the firm. The GIPS standards do not require an Adviser to provide the total portfolio performance when a carve-out with allocated cash is included in a composite. As previously explained, the carve-outs could come from total portfolios that are managed in a variety of strategies.

Advisers may present carve-out performance without cash but this is not considered GIPS-compliant performance, and may only be presented as supplemental information alongside the composite or fund performance from which it was extracted.

We see Advisers providing total portfolio performance when presenting segment returns or attribution in an advertisement.

> *To what extent and under what circumstances have any such investors been misled by the presentation of extracted performance?*

CFA Institute Response: We do not believe that properly constructed carve-out performance is misleading. At one point, the GIPS standards did not allow carve-out performance to be included in a composite, because it was thought that only portfolios managed with their own cash balance should be included in a composite. However, we have come to realize that carve-out performance can be useful to prospective clients, especially in the retail space where, as you also mention, Advisers manage multi-asset class portfolios and would like to show performance of a specific asset class. In the 2020 edition of the GIPS standards firms are once again allowed to synthetically allocate cash to carve-outs, for all periods.

We are not aware of any investor being misled by the use of extracted performance.

5. *(p. 157) With respect to extracted performance, should we require the disclosure or offer of additional information, other than the performance results of the entire portfolio from which the performance is extracted? What additional information would be appropriate to enable an audience to analyze extracted performance more fully?*

CFA Institute Response: We have no additional comments.

> *For example, should we require that an advertisement presenting extracted performance disclose the selection criteria and assumptions used by the adviser in selecting the relevant performance to be extracted?*

CFA Institute Response: As mentioned in question 2 on page 38 under "Extracted Performance," we believe that detailed information about the selection criteria and assumptions used by the Adviser could be overwhelming for a retail audience. We recommend instead allowing Advisers to either disclose the information in the advertisement or offer to provide the information on request. We believe the latter approach would be more meaningful than having long disclosures describing the logic, assumptions, and methodology.

> *Should we require disclosure of the percentage of the overall portfolio represented by the investments included in the extracted performance?*

CFA Institute Response: We do not believe this would be helpful, particularly when the extracted performance includes an extract from more than one portfolio. We believe that creating a proper composite of extracted accounts would best serve the retail investor.

Should we require disclosure of investments included in the extracted performance and a list of all investments in the portfolio from which the extracted performance was selected, to enable the audience to evaluate how the adviser made its determination?

CFA Institute Response: We do not believe this would be helpful, particular when the extracted performance includes an extract from more than one portfolio. We believe that creating a proper composite of extracted accounts would best serve the retail investor.

Should we require any extracted performance to include an allocation to cash?

CFA Institute Response: We believe that extracted performance that is presented as a strategy should be required to include an allocation of cash.

6. *(p. 158) Should we include any other requirements for Non-Retail Advertisements presenting extracted performance? What other requirements and why should we require them?*

CFA Institute Response: We believe the disclosures and other requirements described above should be the same for retail and non-retail advertisements.

7. *(p. 158) Instead of prescribing specific rules for the presentation of extracted performance, should we instead rely on the provisions of paragraph (a) of the proposed rule as we propose to do for cash allocations?*

CFA Institute Response: We believe that Advisers would benefit from guidance. We believe that the level of requirements provided in the proposed rule, plus adding the additional considerations and factors we mention above, would be appropriate.

iv. Hypothetical Performance (p. 158)

A. Types of Hypothetical Performance

1. *(p. 166) Is the proposed definition of "hypothetical performance" clear? If not, how should we modify this definition?*

SEC Proposed Definition of Hypothetical Performance

(5) Hypothetical performance means performance results that were not actually achieved by any portfolio of any client of the investment adviser. Hypothetical performance includes, but is not limited to:

(i) Performance derived from representative model portfolios that are managed contemporaneously alongside portfolios managed for actual clients;

> *(ii) Performance that is backtested by the application of a strategy to market data from prior periods when the strategy was not actually used during those periods; and*
>
> *(iii) Targeted or projected performance returns with respect to any portfolio or to the investment services offered or promoted in the advertisement.*
>
> *GIPS Standards Definition of Theoretical Performance: Performance that is not derived from a portfolio or composite with actual assets invested in the strategy presented. Theoretical performance includes model, backtested, hypothetical, simulated, indicative, ex ante, and forward-looking performance.*

CFA Institute Response: We believe the proposed definition should be modified to remove "of any client" from the first sentence. Under the proposed definition, proprietary seed capital portfolios would be considered hypothetical performance, because these portfolios are not a client portfolio. Pooled investment vehicles might also be captured by this definition because they too are not technically a client portfolio. We do not believe this was the intent.

We also believe that targeted returns should be removed from the definition of hypothetical performance. Targeted returns, such as those used as a benchmark or to describe the investment objective of a strategy, are not hypothetical performance but rather a figure used to define or measure the success of a strategy. On the other hand, projected performance, where an Adviser is taking historical data and applying assumptions to that data to predict what will happen in the future should be considered hypothetical performance. Therefore, we believe that targeted performance should be removed from the examples of hypothetical performance in the rule, but projected performance should be considered hypothetical performance.

Lastly, we recommend reconsidering the use of the term "representative model portfolio." As we mentioned earlier, Advisers often use the performance of a portfolio that is most representative of a strategy, and these are commonly referred to as representative portfolios or representative accounts.

> *For example, should we clarify the treatment of indexes (including indexes sponsored by or created by the adviser or its affiliate) and benchmarks under the definition of hypothetical performance?*

CFA Institute Response: We agree that indexes created by the Adviser should be considered hypothetical performance when the Adviser backtests the index to see how it would have performed. Other than this case, we do not believe that benchmarks should be considered hypothetical performance.

2. *(p. 166) Are there types of performance that investment advisers currently present in advertising that would meet the proposed rule's definition of "representative model performance" but should not be treated as hypothetical performance under the proposed rule? What types of performance and why should they not be treated as hypothetical performance?*

SEC Proposed Definition of Representative Model Performance

(5) Hypothetical performance means performance results that were not actually achieved by any portfolio of any client of the investment adviser. Hypothetical performance includes, but is not limited to:

(i) Performance derived from representative model portfolios that are managed contemporaneously alongside portfolios managed for actual clients;

CFA Institute Response: We are not aware of any portfolios that would meet this definition and should be treated as actual performance. We agree that portfolios that fall into this category should be treated as hypothetical performance.

3. *(p. 166) Do commenters agree with the proposed rule's treatment of targeted and projected returns as hypothetical performance?*

CFA Institute Response: As mentioned above, we believe that targeted performance should be removed from the examples of hypothetical performance in the rule, but projected performance should be considered hypothetical performance.

4. *(p. 166) Should we define "targeted returns" or "projected returns"? If so, how should we define them?*

CFA Institute Response: We believe targeted returns should be removed from the definition of hypothetical performance. We like the language used to explain projected returns and believe this could be used as the definition - the returns that the Adviser believes can be achieved using the advertised investment services.

Do commenters agree with our discussion above about what should be considered a target or projection?

CFA Institute Response: As previously explained, we suggest removing targeted returns from the definition of hypothetical performance. We agree that projected returns should include only the returns that an investment advisor projects for their own investment strategy, and not when the projection refers to how the market in general will perform nor when it refers to returns generated by an investor using an interactive tool.

Should we provide in the rule exclusions for specific kinds of presentations that would not be considered target or projected returns? Why or why not?

CFA Institute Response: We believe the rule text should not include exclusions for specific kinds of presentations that would not be considered projected returns. We think guidance on this point should be included in the adopting release.

5. *(p. 166) Should we prohibit hypothetical performance in advertisements?*

CFA Institute Response: We agree with the proposal to allow hypothetical performance subject to some conditions. Please see our later comments for our feedback on the proposed conditions. We agree that hypothetical performance should not be broadly distributed to the general public.

> *Should performance results of portfolios that are managed by an investment adviser, but without investing actual money, be treated differently than other types of performance results under the proposed rule?*

CFA Institute Response: We believe that performance of a "paper portfolio" should be considered hypothetical performance and should be treated the same as other types of hypothetical performance.

6. *(p. 167) Are our beliefs correct about the risks of backtested and representative performance and of targeted and projected returns?*

CFA Institute Response: We agree with your assessment of the risks.

> *Are there circumstances under which these types of hypothetical performance do not present the risks we identified?*

CFA Institute Response: All of these risks could be true, but there are cases where none of these are present. For example, when an Adviser uses model performance, it may be an accurate reflection of how the Adviser would actually trade a client account free of client restrictions and cash flows. The Adviser is using the model as a basis to trade actual client accounts and it reflects their actual investment ideas.

The main risk we see is that hypothetical performance would be used by someone who is not familiar with hypothetical performance and believes it to be actual performance.

> *Are there other risks that we should consider?*

CFA Institute Response: We do not believe that there are other risks that should be considered.

7. *(p. 167) Are there types of performance that would meet the proposed rule's definition of "backtested performance" but should not be treated as such? What types and how should we modify the definition?*

CFA Institute Response: We do not think there are other types of performance that would be inappropriately captured as backtested performance. However, we believe there are types of performance that would not be considered backtested performance based on the current definition but should be. By including the term "market data," the definition is limited to those strategies that start with market data. There could be strategies that take data from other portfolios managed by the Adviser or someone else and backtest an asset allocation strategy. We believe this should be considered backtested performance. We believe that the term "market data" should be removed from the definition.

8. *(p. 167) Are there types of performance that would meet the proposed rule's definition of "representative performance" but should not be treated as such? What types and how should we modify the definition?*

CFA Institute Response: As mentioned above, we are not aware of any portfolios that would meet this definition and should be treated as actual performance. We agree that portfolios that fall into this category should be treated as hypothetical.

9. *(p. 167) How do investment advisers currently present targeted or projected returns in advertisements?*

CFA Institute Response: For targeted returns, which we do not believe are hypothetical, we see Advisers include this information as a benchmark or as part of a strategy description.

We see projected returns most often used by private equity and real estate Advisers, where they project internal rates of return or multiples for individual holdings. Our experience is that this type of information is typically included in one-on-one presentations and is not broadly distributed.

Do investment advisers ever disclose to investors when targeted or projected returns are met or are not met, and the reasons why such returns are met or not met? Should we require such disclosure? Why or why not?

CFA Institute Response: We have seen Advisers make these disclosures. We do not believe this information should be required to be disclosed. What was projected in the past may be irrelevant. We believe the more important information is the current projection.

10. *(p. 167) Should we provide a specific exception for interactive financial analysis tools from the proposed rule's approach to performance of projected returns? If so, should we consider FINRA's approach or another approach? What approach and why?*

CFA Institute Response: We believe you should include language in the adopting release that is similar to the language in the discussion of the proposed rule.

11. *(p. 168) In complying with the current rule, have investment advisers addressed any of the risks of hypothetical performance we describe above, or other risks of hypothetical performance? If so, how?*

CFA Institute Response: In our experience, Advisers have addressed the risks by having Compliance and often Performance personnel review the assumptions and methodology and ensure the performance is calculated as described and is disclosed properly.

12. *(p. 168) Are there any specific disclosures that we should require to prevent any type of hypothetical performance from misleading the audience? If so, which disclosures should we*

require and why?

CFA Institute Response: We believe hypothetical performance should be adequately disclosed, including that it was created with the benefit of hindsight, if applicable, how the performance was derived, the methodology used, and any assumptions made.

13. *(p. 168) Are there additional uses for hypothetical performance generally, or any type of hypothetical* performance specifically, that benefit investors?

CFA Institute Response: We believe that the majority of investors rely on actual performance, and hypothetical performance should be used only when actual performance either does not exist or cannot be used for the specific purpose.

B. Conditions on Presentation of Hypothetical Performance

1. *(p. 177) Should we prohibit the presentation of hypothetical performance in any advertisement? Why or why not?*

CFA Institute Response: We do not believe hypothetical performance should be prohibited. However, we believe that if actual performance exists, the adopting release should encourage Advisers to present actual performance instead of or along with the hypothetical performance.

Instead of a complete prohibition, should we prohibit the presentation of hypothetical performance, or specific types of hypothetical performance, under specific circumstances? If so, what circumstances?

CFA Institute Response: Since it is not possible to identify every type of hypothetical performance or cover each unique situation, we suggest not prohibiting the presentation of hypothetical performance under specific circumstances.

Should we prohibit the presentation of hypothetical performance in Retail Advertisements but not in Non-Retail Advertisements (or vice versa)?

CFA Institute Response: We do not believe the presentation of hypothetical performance should be prohibited in retail or non-retail advertisements.

2. *(p. 177) Should we permit the presentation of hypothetical performance in any advertisement without condition? Why or why not?*

CFA Institute Response: We agree with your proposed rule. However, we believe the interpretation of condition A in the discussion of the proposed rule needs clarification.

Condition A states that any hypothetical performance is prohibited unless the Adviser "Adopts and implements policies and procedures reasonably designed to ensure that the hypothetical performance is relevant to the financial situation and investment objectives of the person to whom the advertisement is disseminated." We agree with this.

We interpret condition A to mean that an Adviser would need to have policies and procedures to determine what the investors needs are (i.e., which investment strategy is relevant to them based on their return requirements, risk tolerance, and other characteristics). However, the discussion of the proposed rule states the following, which sounds like an Adviser would need to determine if the investor would be able to perform due diligence on the hypothetical performance:

> *"This proposed condition is intended to ensure that the adviser provides hypothetical performance only where the recipient has the financial and analytical resources to assess the hypothetical performance."*
>
> *"hypothetical performance may be less relevant to the financial situation and investment objectives of investors that do not have access to analytical and other resources to enable them to analyze the hypothetical performance and underlying information. For example, analysis of hypothetical performance may require tools and/or other data to assess the impact of assumptions in driving hypothetical performance, such as factor or other performance attribution, fee compounding, or the probability of various outcomes. Without being able to subject hypothetical performance to additional analysis, this information would tell an investor little about an investment adviser's process or other information relevant to a decision to hire the adviser. Instead, viewing the hypothetical performance (without analyzing and performing the necessary due diligence on the underlying information) could mislead an investor to believe something about the adviser's experience or ability that is unwarranted."*
>
> *"To determine whether hypothetical performance is relevant with respect to a Retail Person, reasonably designed policies and procedures should include parameters that address whether the Retail Person has the resources to analyze the underlying assumptions and qualifications of the hypothetical performance to assess the adviser's investment strategy or processes, as well as the investment objectives for which such performance would be applicable."*

While we agree that hypothetical performance should not be distributed to a mass retail audience, we think that the interpretation above would also restrict Advisers from presenting hypothetical performance to most retail clients because most retail clients do not have "resources to analyze the underlying assumptions and qualifications of the hypothetical performance." We believe that the interpretation of condition A should indicate that an Adviser could consider hypothetical performance to be relevant to the financial situation and investment objectives of the person if the person has expressed interest in the strategy or the Adviser has determined it is an appropriate strategy for the investor based on their investment needs.

3. *(p. 177) Should we require, as proposed, that advisers adopt and implement policies and procedures designed to ensure that hypothetical performance is relevant to a recipient's financial situation and investment objectives?*

CFA Institute Response: See response above. We agree with the rule but believe the interpretation should be revised.

> *Would such policies and procedures ensure that hypothetical performance is only provided to those for whom it is relevant?*

CFA Institute Response: We believe these policies and procedures would suffice.

> *Would providing hypothetical performance only to those for whom it is relevant help prevent such performance from being misleading?*

CFA Institute Response: We believe that providing hypothetical performance only to those for whom it is relevant will help prevent such performance from being misleading.

> *Would advisers be able to make the determination that hypothetical performance is relevant?*

CFA Institute Response: We believe that Advisers will be able to make the determination that hypothetical performance is relevant.

4. *(p. 177) Should we consider another standard other than "relevant" to a recipient's "financial situation and investment objectives" to help protect against hypothetical performance being provided to persons who would be misled by it? For example, should we instead require that such performance be provided only to persons whom the adviser reasonably believes may use such performance in considering whether to hire or retain an adviser and that have sufficient access to analytical and other resources to evaluate or test the assumptions underlying the hypothetical performance so as to make the hypothetical performance not misleading?*

CFA Institute Response: Please see our response to question 2 on page 46 in this sectoin. We agree with condition A in the rule but believe the interpretation should be revised.

> *Alternatively, should we limit the distribution of this performance to persons whom the adviser reasonably believes would use it in evaluating whether to hire or retain the adviser?*

CFA Institute Response: We do not believe that limiting the distribution of hypothetical performance to persons whom the Adviser believes would use it in evaluating whether to hire or retain an Adviser would be a helpful approach. We believe that the "relevant" standard is appropriate.

> *Alternatively, should we avoid limiting at all the distribution of hypothetical performance, which some investors may find useful?*

CFA Institute Response: We believe the distribution of hypothetical performance should be limited, and generally agree with your proposed approach.

5. *(p. 178) Should we instead consider categorical approaches – e.g., should we instead allow hypothetical performance to be provided to Non-Retail Persons in all cases without requiring the adviser to adopt policies and procedures?*

CFA Institute Response: We believe that requiring Advisers to adopt reasonably designed policies and procedures for the use of hypothetical performance with both non-retail and retail persons is appropriate.

Should we allow its presentation to Non-Retail Persons but prohibit its presentation to Retail Persons entirely?

CFA Institute Response: As discussed above, we believe hypothetical performance should be allowed to be presented to both non-retail and retail persons.

6. *(p. 178) Are there specific disclosures that we should require to decrease the likelihood that hypothetical performance, or specific types of hypothetical performance, would be misleading – e.g., describing the fact that the performance was not generated by actual portfolios of actual clients of the investment adviser and describing the limitations of hypothetical performance? If so, should we identify those and specifically require their disclosure?*

CFA Institute Response: We do not believe specific disclosures should be required, but we think it would be helpful to provide an interpretation of what "risks and limitations" are in the adopting release. We found the examples included in the discussion of the proposed rule to be very helpful.

7. *(p. 178) Are there specific disclosures that we should require to decrease the likelihood that hypothetical performance would be misleading to Retail Persons? If so, should we identify those and specifically require those disclosures? Should we require different disclosures for Retail Persons and Non-Retail Persons, or is the tailoring implicitly permitted under the proposed rule's "sufficient information" standard enough?*

CFA Institute Response: We do not believe specific disclosures should be required, but it would be beneficial to have examples, as well as the interpretation that the disclosures should be tailored to the audience, similar to what you have included in the discussion of the proposed rule.

8. *(p. 179) Is there another approach that we should consider for hypothetical performance being provided to Retail Persons?*

CFA Institute Response: We have no additional comments.

Are there any types of hypothetical performance that are sufficiently similar to actual results of a portfolio of an actual client that we should permit their presentation in a Retail Advertisement or their dissemination to Retail Persons without conditions?

CFA Institute Response: We are not aware of any such types of hypothetical performance.

9. *(p. 179) Are the proposed "calculation information" and "risk information" provisions sufficiently clear based on our description above?*

CFA Institute Response: We believe the provisions are sufficiently clear with the description above. We believe it would be beneficial to have the description in the adopting release.

> *Should we require specifically that such information be designed to allow the audience to replicate the hypothetical performance presented? Why or why not?*

CFA Institute Response: We do not believe it would be feasible to require sufficient disclosure to enable an investor to replicate hypothetical performance in all cases.

For example, it might be feasible to provide such disclosure when a firm applies a backtest to market data. However, when a firm is applying fundamental investment decisions to a model account that is managed alongside other accounts in a real-time manner, it would not be possible to disclose enough information to allow someone to replicate the performance. It also would not be reasonable to expect that a prospect would have access to all of the data that would be necessary. Finally, the model itself may be proprietary.

We believe that the principle-based approach of requiring a disclosure that describes "the criteria used and assumptions made in calculating [or deriving] such hypothetical performance" or offering to provide such information suffices.

10. *(p. 179) Would investment advisers face any compliance challenges in complying with the proposed "calculation information" or "risk information" provisions?*

CFA Institute Response: We do not see any challenges in complying with the proposed calculation information or risk information provisions as they are written and described in the proposal.

> *Would there be circumstances in which investment advisers might have to provide proprietary or sensitive information? Should we take those challenges or circumstances into account? If so, how?*

CFA Institute Response: We believe that these challenges and circumstances should be take into account and can be addressed through disclosure. For example, if the Adviser believes information is proprietary, the Adviser should be required to disclose that the investor is taking on additional risk because the investor is unable to verify the methodology of the returns being shown to them.

11. *(p. 179) Should we require that the risk information be provided (not just offered to be provided) to Non-Retail Persons as well as to Retail Persons?*

CFA Institute Response: We believe that offering to provide risk information to non-retail persons as proposed suffices.

Conversely, should we allow the calculation information to be only offered to Non-Retail Persons (instead of requiring it to be provided)?

CFA Institute Response: We believe that the calculation information should be provided to both non-retail and retail persons, as proposed. However, as mentioned earlier, we do not believe it is feasible to provide enough information to enable the recipient to attempt to replicate the hypothetical performance using its own analytical tools or other resources, which might allow the recipient to evaluate further the utility of the hypothetical performance. We believe the rule and adopting release should not be written with this objective in mind.

12. *(p. 180) Under the current rule, have investment advisers taken the same approach that we are proposing with respect to hypothetical performance – i.e., providing or offering to provide specific information?*

CFA Institute Response: In our experience, we have seen a wide variety of practices. While most Advisers provide both the calculation and risk information directly on the presentation, we have also seen Advisers disclose that additional information is available upon request.

To what extent and under what circumstances have any such investors been misled by the presentation of hypothetical performance?

CFA Institute Response: We have not seen any specific instances where investors have been misled by the presentation of hypothetical performance. We believe it would be misleading if an Adviser presented hypothetical performance as if it were actual performance.

d. **General request for comment on performance advertising.**

1. *(p. 180) Are our beliefs correct that the proposed rule's requirements are consistent with widely-used, internationally-recognized standards of performance presentation, such as GIPS?*

CFA Institute Response: We believe that the proposed rule's requirements are generally consistent with the GIPS standards. Please see our response to question 9 under "Related Performance" on page 35 that discusses the differences.

Would investment advisers find it difficult or impossible to comply with both the provisions of the proposed rule and the requirements of any such standards in order to comply with the proposed rule's requirements? If so, which requirements would create such difficulty or impossibility and how? Should we address any such difficulty or impossibility? If so, how?

CFA Institute Response: Please see our response to question 9 on page 35 that discusses the challenges GIPS-compliant Advisers would face under the proposed rule. Please also see our response to part 2 to question 9 under "Related Performance" found on page 36 for our

suggestions for how to take those compliance challenges into account. We would like to see the rule conform more closely with the GIPS standards. However, we believe that the differences, while not ideal, could be managed.

> *Should we adopt a more principles-based approach to afford flexibility in the event that such private standards change?*

CFA Institute Response: We believe that the proposed rule generally strikes the right balance between being principles-based versus rules-based. While the GIPS standards will continue to evolve, we do not believe that potential future changes should be of concern. Advisers that comply with the GIPS standards are required to first and foremost comply with applicable laws and regulations regarding the calculation and presentation of performance. Our comments about wishing to align the rule more closely with the GIPS standards would allow for consistent performance to be used in all marketing materials, which we believe would benefit both Advisers and their investors.

2. *(p. 181) Are there specific concerns about performance advertising that the proposed rule does not take into account that we should consider? What specific concerns, and how should we take them into account? Conversely, are there provisions of the proposed rule's performance advertising provisions that address concerns you believe to be unfounded?*

CFA Institute Response: We have two additional comments about model delivery and benchmarks, which the proposed rule does not take into account but we hope you will consider.

A product growing in popularity for Advisers is the sale of an investment model to another Adviser who then implements the model for retail clients. We will refer to the Adviser who sells the model as the "model manager" and the Adviser who implements the model as the "implementation manager." The model manager may provide performance of actual client accounts it manages to the model strategy, including a GIPS-compliant composite, or it may provide model performance to the implementation manager. Under the current and proposed rules, it is unclear if the model manager (who provides a GIPS Report) has any responsibility for ensuring that the end client understands that they will not be invested with the manager who claims GIPS compliance, but rather invested with the implementation manager. For example, the implementation manager may ask for a GIPS Report, or other performance information, from the model manager to use in their marketing efforts. The GIPS compliant firm, who has an obligation to make every reasonable effort to provide GIPS compliant information to all prospective clients, will provide this. The GIPS compliant firm knows that the end client will be invested with the implementation manager, but the performance may still be helpful as long as the end client understands its limitations. Additional clarification would be helpful on what is allowed, who has the responsibility of ensuring this is not misleading to the end client, and if the model manager can assist their client (the implementation manager) without taking on additional liability.

Benchmarks are an important component of fairly representing performance. The proposed rule addresses the presentation of performance earned by an Adviser, but it does not require a comparison of this performance to a benchmark. Without providing an appropriate benchmark, an advertisement cannot illustrate whether an Adviser is successful in managing financial assets. For example, an Adviser can advertise that they earned 20%, 16% and 10% over the last 1, 5, and 10 years, but if the appropriate benchmark earned 22%, 17% and 11%, respectively, and that was not shown on the advertisement, an investor could be led to believe that the Adviser was successful when in fact he or she was not. Therefore, we believe an Adviser should be required to show returns of an appropriate benchmark for the same periods as presented for the Adviser's performance. We suggest limiting this requirement to the situation where the Adviser has benchmark performance available. For non-retail advertisements, the presentation of benchmark performance should be encouraged.

3. *(p. 181) Should we consider removing some of the proposed rule's requirements for performance advertising and instead rely on paragraph (a) of the proposed rule and the general anti-fraud provisions of the Federal securities laws to prevent the use of performance advertising that is false or misleading? Why or why not? Are there additional requirements that we should consider including in the proposed rule with respect to performance advertising in order to supplement paragraph (a)? What additional requirements and how would they supplement paragraph (a)?*

CFA Institute Response: As we state throughout our comments, we believe the rule should include requirements instead of having Advisers solely rely on paragraph (a). We do not believe anything further needs to be added to paragraph (a).

4. *(p. 181) Should we impose on Non-Retail Advertisements presenting performance results the same or similar requirements that the proposed rule imposes on Retail Advertisements? For example, should we require Non-Retail Advertisements to present net performance or to present performance results for certain specified periods of time? Why or why not?*

CFA Institute Response: We do not believe non-retail advertisements should be required to have net performance or standardized time periods. Non-retail clients have resources that retail clients do not have.

5. *(p. 182) Should we specify any types of information that advisers may refrain from disclosing when responding to prospective investors seeking the information that must be offered in advertisements?*

CFA Institute Response: We believe that Advisers should be required to provide all information that is offered in advertisements.

Are advisers concerned that their competitors may seek to acquire such information through requests responding to those offers?

CFA Institute Response: We do not believe this should be a concern. Advisers that advertise performance are making their performance public. The fact that a competitor may obtain information is a small downside risk.

Do advisers have any other concerns regarding competition that the proposed rule may cause or should address?

CFA Institute Response: We do not know of any other concerns.

6. Portability of Performance, Testimonials, Third Party Ratings, and Specific Investment Advice (p. 182)

1. *(p. 186) Do commenters believe that we should include specific provisions in the proposed rule to address the presentation of predecessor performance results? Or do commenters believe that the proposed rule, including the provisions of paragraph (a), will sufficiently prevent the presentation of predecessor performance results that are false or misleading?*

CFA Institute: We believe specific provisions should be included to address the presentation of predecessor performance results. This is an area ripe for abuse. Our experience is that many Advisers struggle with this topic, and any guidance would be welcomed. We recommend conforming your guidance with the requirements of the GIPS standards.

If we include specific provisions to address the presentation of predecessor performance results, what specific provisions should we include?

CFA Institute Response: The GIPS standards permit the use of predecessor performance when the following requirements are met for a composite or pooled fund:

a. Substantially all of the investment decision makers must be employed by the new or acquiring firm (e.g., research department staff, portfolio managers, and other relevant staff);

b. The decision-making process must remain substantially intact and independent within the new or acquiring firm;

c. The new or acquiring firm must have records to support the performance.

The performance from the predecessor firm may be linked to the performance of the new firm, the advertising Adviser" only if there is no break or gap in the management of the portfolios. If there is a break in performance between the predecessor firm and the new firm, the performance from the predecessor firm may be used but it must not be linked to the ongoing performance at the new firm.

For an Adviser to be able to use the track record from the predecessor firm as a GIPS-compliant track record, the track record from the predecessor firm must include all portfolios that were managed in the strategy at the predecessor firm – that is, it must be composite performance. If

the acquiring Adviser has records to support only a subset of portfolios that were managed at the predecessor firm, this performance may be used in limited circumstances, but it may not be linked to the ongoing track record of the acquiring Adviser and may not be presented as a GIPS-compliant track record. We believe that there may be value in presenting this subset performance, but only when presented on a one-on-one basis and only to prospective clients or prospective investors who the firm believes are sufficiently knowledgeable about investments and can understand the relevance and limitations of the track record being presented. This would be consistent with the current guidance in the Horizon no-action letter, which allows for the presentation of performance of all accounts managed in a substantially similar manner from a prior entity, unless the exclusion of any such account would not result in materially higher performance. In the proposed rule this concept has been expanded to cover all advertisements. We have previously suggested reconsidering expanding this concept to all track records. If the final rule removes the expansion of this concept to all advertisements, we recommend including it within portability provisions. We believe this concept is appropriate when considering performance from a prior entity, because it may not be possible to gather the information for all related portfolios from a prior entity.

> *How would those specific provisions prevent the presentation of predecessor performance results that is false or misleading?*

CFA Institute Response: We believe that incorporating guidance consistent with the GIPS standards would prevent the results from being false or misleading because:

- The performance is relevant, because substantially all of the investment decision makers have moved to the advertising Adviser and the investment process has remained substantially intact. The prospective investor will be investing in essentially the same product that was managed at the predecessor firm.
- The advertising Adviser will have records to substantiate that the performance being presented is actual performance, based on actual transactions and holdings.
- The performance is linked only when there is no gap in performance between the predecessor firm and the advertising Adviser.
- The track record of a composite will include all portfolios managed to the strategy at the predecessor firm.

Our experience is that firms are able to meet these portability tests and use performance from the prior firm only when the departure from the predecessor firm is "friendly." If the departure is not friendly, the advertising Adviser typically will not have records to support a complete composite history from the predecessor firm.

2. *(p. 186) Should we impose conditions on an advertising adviser seeking to present predecessor performance results achieved at a prior advisory firm?*

CFA Institute Response: We believe conditions should be imposed.

Should we require that the individual or individuals who currently manage accounts at the advertising adviser to have been "primarily responsible" for achieving the predecessor performance results at the prior firm? If so, should we specify how "primary responsibility" is determined?

CFA Institute Response: This concept is generally consistent with one of the portability requirements of the GIPS standards - the requirement that substantially all of the investment decision makers must be employed by the new or acquiring firm (e.g., research department staff, portfolio managers, and other relevant staff). We believe this is similar to saying that the individual or individuals who currently manage accounts at the advertising Adviser have been "primarily responsible" for achieving the predecessor performance results at the prior firm.

We currently do not specify how "substantially all" is determined. We have been asked for guidance on this point but have declined to provide detailed guidance. We believe that the facts and circumstances of each portability event will differ. We believe it would be challenging to determine what "primary responsibility" means given all of the unique scenarios Advisers face.

3. *(p. 186) Should we address circumstances in which predecessor performance results were achieved by portfolios managed by a committee (as opposed to an individual) at the prior firm? Should we require that if the portfolios at the predecessor firm were managed by a committee, the accounts at the advertising adviser must be managed by a committee comprising a substantial identity of the membership?*

CFA Institute Response: We believe the rule should not distinguish between individual portfolio managers versus a committee. We believe that requiring the individual or individuals who currently manage accounts at the advertising Adviser to have been "primarily responsible" for achieving the predecessor performance results at the prior firm would suffice, and cover both situations.

Should we define or provide additional guidance regarding the "substantial identity" required, or require that the committee comprises a specific percentage or subset of members? Should we establish any specific requirements for how much of a role an individual has to play on the committee at the predecessor firm and on the committee at the advertising adviser?

CFA Institute Response: We believe you should not provide specific guidance regarding the "substantial identity required." As mentioned previously, our experience is that the facts and circumstances of each portability event will differ. We believe it would be challenging to determine specific requirements for how much of a role an individual has to play on the committee at the predecessor firm and at the advertising Adviser, given all of the unique scenarios Advisers face.

4. *(p. 187) Is there any circumstance under which the membership of a committee at a predecessor firm is so different from the membership of a committee at the advertising adviser that any presentation of performance results from the predecessor firm should be prohibited? What are those circumstances?*

CFA Institute Response: We believe there are circumstances under which the membership of a committee at a predecessor firm is so different from the membership of a committee at the advertising Adviser that any presentation of performance results from the predecessor firm should be prohibited. We think this would be true whenever substantially all of the investment decision makers (e.g., research department staff, portfolio managers, and other relevant staff) are not employed by the advertising Adviser.

5. *(p. 187) Should the proposed rule distinguish between predecessor performance results on the basis of strategy – for example, between fundamental and quantitative strategies? Are presentations of predecessor performance results less likely to be misleading to the extent that those results were generated by use of a proprietary, algorithmic strategy that the advertising adviser "owns" and expects to use going forward? Why or why not?*

CFA Institute Response: We believe that there is no need to differentiate requirements based on strategy. Even if a quantitative strategy is run by a program, there are individuals who are monitoring and maintaining that program. This is why the GIPS standards include a test requiring that the decision-making process must remain substantially intact and independent within the new or acquiring firm. This requirement would address your concerns because it must be met regardless of the strategy.

Should the proposed rule distinguish between predecessor performance results on the basis of something other than strategy? What basis and why?

CFA Institute Response: We believe the proposed rule should focus on the continuity of the strategy, as the GIPS standards do.

6. *(p. 187) Should we require any similarity between the accounts managed at the predecessor firm and the accounts presented by the advertising adviser – for example, having similar investment policies, objectives, and strategies? A presentation of predecessor performance results could be false or misleading if the accounts managed at the predecessor firm are not sufficiently similar to the accounts that the adviser currently manages such that the prior results would not provide relevant information to the advertising adviser's prospective clients.4 Should the Commission take this approach and include such provision in the rule?*

CFA Institute Response: We believe the track record from the predecessor firm may only be used if the strategy of the accounts is consistent between the two firms. If the strategy changes once the portfolios move to the advertising Adviser, the track record from the predecessor is no

[4] See, e.g., Horizon Letter.

longer relevant. As previously stated, the GIPS standards require the decision-making process to remain substantially intact within the new firm. We believe this requirement can be met only if the accounts at the advertising Adviser are managed following the same strategy as was used at the predecessor firm. We believe this should be included as a provision in the rule.

> *If the Commission were to adopt this approach, should we specify how that similarity should be determined?*

CFA Institute Response: We do not believe you should specify how that similarity should be determined. We recommend taking the same approach as done in the discussion of related portfolios, where Advisers could use the same criteria used to for GIPS-compliance purposes to satisfy the rule requirements.

> *Should we allow advertising advisers to present any performance results from predecessor firms without requiring that the advertising adviser determine whether the accounts are similar or the results are relevant, and let investors evaluate the relevance themselves? Would this approach be appropriate in Non-Retail Advertisements and not Retail Advertisements? Why or why not?*

CFA Institute Response: We believe that the burden to determine relevance should not be on the investor. The Adviser should determine relevance, and only utilize the predecessor track record when the strategy is substantially similar as those of the services being offered or promoted in the advertisement.

7. *(p. 188) Should an investment adviser seeking to present predecessor performance results be required to make any specific representations or disclosures in the advertisement? Or elsewhere?*

CFA Institute Response: We believe an Adviser should be required to disclose that the track record is from a predecessor firm, and for which periods. We believe that the disclosure should be required to be included in the advertisement.

8. *(p. 188) Do commenters believe we should consider amendments to the books and records rule to address the substantiation of performance results from a predecessor firm? Do investment advisers encounter any difficulties in accessing and retaining the books and records substantiating the performance results of a predecessor firm? Are there alternative books and records or other information that we could allow advertising advisers to rely on or retain in order to satisfy their obligations under the books and records rule with respect to predecessor performance results? Are there other sources of records that advisers currently rely on to substantiate performance results of a predecessor firm?*

CFA Institute Response: Advisers often encounter difficulties in accessing and retaining the books and records substantiating the performance results from a predecessor firm. We generally do not believe that alternative books and records should be allowed. We do not believe that

reliance should be able to be placed on a verification report or a performance examination report. The documentation a verifier maintains to support a performance examination report would not, in most instances, suffice for recordkeeping purposes. The same is true for performance that has been subject to a financial statement audit. We also believe that service providers (verifiers and public accounting firms) would not wish to be viewed as a recordkeeping source, and this would also cause the verifier/public accounting firm to not be independent of the Adviser. We agree with one exception to maintaining books and records, and that is when the Adviser meets the requirements specified in the Salomon Brothers no-action letter (reliance is placed on the contemporaneously produced, publicly available NAVs). Although the proposed rule does not address mutual funds, mutual funds are often members of composites, so we believe it is appropriate to mention this.

9. *(p. 188) Do investment advisers encounter difficulties in determining who "owns" the relevant performance results? That is, are investment advisers able to agree who should be able to advertise the prior performance results from the predecessor firm? How do investment advisers make this determination? Should we adopt requirements to clarify under what circumstances an advertising adviser may present predecessor performance results?*

CFA Institute Response: In a friendly departure, typically there is no difficulty determining who "owns" the relevant performance results. The situation can be quite different, however, for an unfriendly departure. Because acquiring firms are required to have complete composite history from the prior firm, and must have records to support all portfolios that were in the composite, we find that there are limited circumstances in which these requirements can be met. One situation is when the composite at the prior firm included only a single mutual fund and reliance is placed on the publicly available NAVs consistent with the Salomon Brothers no-action letter. A second situation is when clients from the prior firm follow the departing team to the new firm, and the clients provide their supporting records. Because these situations are not that common, we believe that the risk that two firms will use the same history should not be a major concern and guidance for this is not necessary.

10. *(p. 189) Should we clarify that an advertising adviser may continue to advertise predecessor performance even if the personnel who achieved the predecessor performance, and who are employed by the advertising adviser, subsequently leave the advertising adviser? Why or why not?*

CFA Institute Response: We agree that an advertising Adviser may continue to advertise predecessor performance even if the personnel who achieved the predecessor performance, and who are employed by the advertising Adviser, subsequently leave the advertising Adviser. It would be helpful to clarify this in the rule.

Once performance is brought over to the advertising Adviser from the predecessor firm (because it has met all of the requirements we mentioned above), it is now considered a track record of the

firm (advertising Adviser), and not the performance of any specific individual or individuals. When an individual or team is at a firm managing a strategy, the firm is aware of the investment process and supports its operations. Firms are aware that people can leave and typically try to eliminate key man risk by understanding the processes a person is following. Therefore, when a person leaves, that process can, and typically does, stay the same. We do not think a portability situation should be held to a different standard than a non-portability situation.

8. Proposed Amendments to Form ADV (p. 195)

1. *(p. 197) Should we require more or less detailed information about advisers' advertising practices? If so, what additional information should we require, or what should we remove from the disclosure requirement, and why?*

CFA Institute Response: We agree that requiring Advisers to include disclosures about their advertising practices in Form ADV would be helpful to SEC staff, to help prepare for examinations. However, we are concerned about the use of this information by prospective clients of a firm, particularly with respect to the requirement to disclose verification status. We assume that this requirement contemplates disclosing if the firm has been verified relative to the GIPS standards. Simply stating that a firm has been "verified" may convey inappropriate assurance about a firm's performance results. A GIPS standards verification does not provide assurance on the firm's claim of compliance with the GIPS standards in its entirety, or on the performance of any specific composite or pooled fund. A verification is more akin to a controls report, which provides assurance on the design and implementation of certain policies and procedures for calculating and presenting performance. Because of the potential confusion surrounding the scope of a verification, the GIPS standards require firms that have been verified to disclose a description of what is included in a verification, and they must also disclose the fact that a verification does not provide assurance on the accuracy of any specific performance report. Firms must also disclose the period for which the firm has been verified.

In addition to a verification, a firm may choose to have a performance examination of a specific composite or pooled fund. A performance examination does provide assurance on the results of the specific composite or pooled fund that has been examined. A performance examination is more akin to an "audit" of a specific composite's or pooled fund's GIPS Report. (A GIPS Report is a report for a composite or pooled fund that includes all of the information for that composite or pooled fund that is required by the GIPS standards.) The GIPS standards require firms to disclose the period for which the composite or pooled fund has been examined.

Finally, we think it would be valuable if you inquired as to whether a firm claims compliance with the GIPS standards. A firm that claims compliance may not be verified, because a verification is optional. Knowing whether a firm claims compliance may help you prepare for examinations.

2. *(p. 197) Should we require more information about advisers' use of performance results in advertisements? For example, for advisers that use performance results in advertisements that are verified or reviewed by someone other than a related person, should we require the advisers to provide the name and contact information of such reviewer on a corresponding schedule? Why or why not?*

CFA Institute Response: We believe the name and contact information of an independent verifier should be required in a corresponding schedule, but should not be required in the ADV. However, as noted above, a verification does not provide assurance on the results of any composite or pooled fund. If you wish to understand the scope of work that has been conducted by an independent third party, we recommend asking the Adviser the following questions with respect to the GIPS standards:

- Does the firm claim compliance with the GIPS standards?
- For which period does the firm claim compliance with the GIPS standards?
- Has the firm been verified by an independent third party?
- If the firm has been verified, for which period has it been verified?
- Name of the verifier.
- Have any composites or pooled funds been examined?
- If any composites or pooled funds have been examined, provide a list of the examinations, including the period for which each examination has been conducted.

3. *(p. 197) For advisers that have their performance results verified or reviewed by a person who is not a related person, does such verification or review apply to all of the advisers' performance results, or only to some of the performance results? Please explain.*

CFA Institute Response: As described above, for Advisers who claim compliance with the GIPS standards, there are two types of testing that may be conducted – a firm-wide verification and a performance examination. Both of these reviews are done for a specified time period, so it is possible for the verification or performance examination to cover only a portion of the Adviser's track record.

A firm "verification" is a process by which an independent third party, i.e., "a verifier," assesses whether the Adviser policies and procedures related to composite and pooled fund maintenance as well as the calculation, presentation, and distribution of performance have been designed in compliance with the GIPS standards and have been implemented on a firm-wide basis. A verification does not provide assurance on the accuracy of any specific performance report. A verification is conducted for a specific period, e.g., from January 1, 12015 through December 31, 2019. The required tests that a verifier must conduct are specified in the GIPS standards for Verifiers. This testing includes reviewing the firm's policies and procedures to ensure they are complete and that they are consistent with the requirements of the GIPS standards. A verification utilizes a sampling process.

A "performance examination" is the detailed testing of a specific composite or pooled fund and its associated GIPS Report. A performance examination tests, for a specific composite or pooled fund:

- Whether the firm has constructed the composite in compliance with the GIPS standards (only applicable for composites),
- Whether the firm has calculated the composite or pooled fund performance in compliance with the GIPS standards, and
- Whether the firm has prepared and presented the composite or pooled fund's GIPS Report in compliance with the GIPS standards.

A performance examination may be performed for a specific period and is not required to cover the entire track record that is presented. Therefore, the GIPS standards require a firm to disclose for which period the performance examination has been conducted.

If an Adviser does not claim compliance with the GIPS standards, they may choose to have an independent third-party performance audit. These audits are not standardized and therefore can include a review of the firm or a specific presentation, calculation, system, performance-related policy or procedure. This again may only cover a certain time period.

4. *(p. 197) Should we require that advisers state if they have any of their results verified by such a third party?*

CFA Institute Response: Please see prior comments that explain that a verification does not provide assurance on the any performance results. Please also see our suggested questions to ask with respect to the GIPS standards.

5. *(p. 197) Should we require advisers to state the particular types of performance results they use in advertisements, such as related performance, hypothetical performance, or another type of performance (and if so, what type of performance)?*

CFA Institute Response: We believe that it would be helpful for your examination purposes to require Advisers to disclose if they have used certain types of performance within a specified period. We see no benefit in asking about related performance, because so many types of performance would qualify as related performance. Identifying those firms that advertise hypothetical performance could be helpful, as well as those that present performance from a prior firm.

Should we require them to state to whom they direct specific types of advertisements (for example, Retail Persons or Non-Retail Persons)? Why or why not?

CFA Institute Response: We do not believe this should be required. Given the fact that the definition of advertisement is so broad and encompasses so many communications (e.g., one-on-one e-mails), it would be virtually impossible to list all of the advertisements and to whom they are directed.

6. *(p. 198) Should we require advisers to disclose that they provide hypothetical performance to investors? If so, should we require advisers to provide descriptions of such hypothetical performance or any information about how they calculate hypothetical performance?*

CFA Institute Response: We do not believe a description of hypothetical performance should be required. Responding to such a question could be very challenging for a large firm. Additionally, each hypothetical performance calculation could be different, and thus it is not feasible to include a description of these calculations on the ADV.

7. *(p. 198) Should we require advisers to state whether their use of performance, testimonials, endorsements, third-party ratings, or specific investment advice includes information from predecessor or other firms? If so, should we require any additional information about the predecessor or other firm, such as a name and contact, and an affirmation that such firm permits the adviser's use of the performance results (if applicable) and affirms its accuracy?*

CFA Institute Response: Speaking only to the use of performance, we agree that Advisers should be required to state whether their performance track record includes information from a predecessor, but we do not think it is practical for a firm to get an affirmation that the predecessor firm permits the Adviser's use of the performance results and affirms its accuracy.

Conclusion

CFA Institute supports the SEC's efforts to ensure Advisers provide fair, accurate, complete, and timely representation of the kind and quality of advisory services they can provide to potential investment clients. We support efforts to prevent false advertising to protect investors from significant harm. We also support the Commission's decision to address performance by Advisers in their advertisements to attract new clients.

Should you have any questions about our positions, please do not hesitate to contact James Allen, CFA by phone at [redacted], or by email at [redacted], or Karyn Vincent by email at [redacted], or by phone at [redacted].

Sincerely,

/s/ Jim Allen

James Allen, CFA
Head, Capital Markets Policy
CFA Institute

/s/ Karyn D. Vincent

Karyn D. Vincent, CFA, CIPM
Senior Head, Global Industry Standards
CFA Institute