



February 10, 2020

VIA ELECTRONIC SUBMISSION

Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, D.C. 20549-1090

Re: Investment Adviser Advertisements; Compensation for Solicitations (SEC Release No. IA-5407; File No. S7-21-19 (Nov. 4, 2019))

Dear Ms. Countryman:

The American Investment Council (the “AIC”) appreciates the opportunity to submit this letter to the Securities and Exchange Commission (the “SEC”) on the proposal (the “Proposed Amendments”) to amend Rule 206(4)-1 (the “Advertising Rule”) and Rule 206(4)-3 (the “Cash Solicitation Rule”) under the Investment Advisers Act of 1940 (the “Advisers Act”) along with certain other related amendments.¹

The AIC is an advocacy, communications, and research organization established to advance access to capital, job creation, retirement security, innovation, and economic growth by promoting responsible long-term investment. In this effort, the AIC develops, analyzes, and distributes information about the private equity and private credit industry and its contributions to the U.S. and global economy. Established in 2007, and formerly known as the Private Equity Growth Capital Council, the AIC is based in Washington, D.C. The AIC’s members are the world’s leading private equity and private credit firms, united by their commitment to growing and strengthening the businesses in which they invest.²

The AIC commends the SEC’s efforts to modernize the Advertising Rule and appreciates the opportunity to provide comments on potential challenges that the implementation of the Proposed Amendments would have on investment advisers and especially on private equity fund managers.

As discussed below, the AIC does not believe that the Advertising Rule should apply to materials used in connection with the marketing of interests in private funds. The general anti-fraud

¹ Investment Adviser Advertisements; Compensation for Solicitations, SEC Release No. IA-5407; File No. S7-21-19 (Nov. 4, 2019) (the “Proposing Release”).

² For further information about the AIC and its members, please visit our website at <http://www.investmentcouncil.org>.

provisions of the federal securities laws, including the Advisers Act, provide a robust framework for the regulation of such materials. If, however, the SEC believes that the Advertising Rule should apply to private funds, the Proposed Amendments should be substantially modified in several respects, as discussed below. The AIC believes that the SEC should (i) reduce the number of prescriptive requirements that apply with respect to advertisements to Non-Retail Persons, (ii) reconsider the impact of a broader definition of an “advertisement” in combination with the new prescriptive requirements in the Proposed Amendments (including the requirement that all advertisements be reviewed and approved by a designated employee (the “Designated Person”) before disseminating the advertisement), (iii) not adopt the Designated Person provision, (iv) expand the “Non-Retail Person” definition to include “Accredited Investors” and “Qualified Clients” and reflect the existing regulatory framework for private funds (both for U.S. and non-U.S. persons) and apply the concept more broadly to advertisements provided to Non-Retail Persons, and (v) provide greater flexibility with respect to the presentation of performance information to Non-Retail Persons.

Finally, the AIC does not believe that the Cash Solicitation Rule should be expanded to cover the solicitation of investors in private funds.

I. Offerings of Private Funds Are Subject to Broad Anti-Fraud Provisions that Are Sufficiently Protective of Current and Prospective Investors, and Marketing Materials Relating to Such Offerings Should Not Be Treated as Advertisements.

An offering of interests in a private fund is subject to the general anti-fraud provisions under U.S. securities laws. Moreover, communications to private fund investors are subject to Section 206(4) of the Advisers Act and Rule 206(4)-8 thereunder. As such, as discussed throughout this letter, the AIC believes that it is unnecessary to subject private fund communications, particularly private placement memoranda (“PPMs”) and related materials, to the detailed conditions under the Proposed Amendments. These types of communications are designed to attract investors – not clients – and are addressed by Rule 206(4)-8 under the Advisers Act as well as other anti-fraud provisions under the U.S. federal securities laws. Moreover, private fund investors are, in general, highly sophisticated and, in most instances, would be viewed as Non-Retail Persons – that is, “qualified purchasers” as defined by Section 2(a)(51) of the Investment Company Act of 1940 (the “Investment Company Act”).³ The Proposing Release acknowledges that such investors have access to analytical and other resources that allow them to evaluate marketing materials. As such, marketing materials designed for private fund investors do not need to be subject to the same types of regulations applicable to managed accounts or investment vehicles targeted at retail investors. The SEC recently acknowledged this distinction in recent guidance on Form CRS. In particular, the SEC noted that Form CRS is not required to be delivered to a retail investor in a private equity fund as this is not the kind of investment advisory relationship the delivery requirement is intended to address.⁴

³ As discussed below, we believe that the definition should also include Accredited Investors, Qualified Clients, and certain other categories of persons.

⁴ “Delivery Requirements,” *Frequently Asked Questions on Form CRS*, available at <https://www.sec.gov/investment/form-crs-faq>.

Moreover, a number of conditions and prohibitions under the Proposed Amendments are drawn from FINRA rules and Rule 156 under the Securities Act of 1933 (the “Securities Act”),⁵ which were developed to address marketing of mutual funds to retail investors. These frameworks are in stark contrast to the intent and goals of private funds, which is to offer securities privately to sophisticated investors. As the AIC has noted in the past, subjecting private funds to this type of regulation is unnecessary and inappropriate given the resources and sophistication of private fund investors.⁶

II. The Definition of an “Advertisement.”

A. Instead of Expanding the Definition of an “Advertisement,” the AIC Suggests Narrowing the Definition and Relying on Select General Prohibitions to Apply to Other Informal Communications and Materials.

The AIC appreciates the SEC’s wish to update and modernize the definition of an “advertisement” to better align with the expansion of the types of communications used to market investment advisory services. However, the expanded definition in the Proposed Amendments will pose significant compliance challenges to private fund sponsors, particularly when paired with the other proposed changes to the Advertising Rule.

First, the SEC should clarify that investor account statements, transaction reports and other similar materials delivered to existing clients or private fund investors should not be considered “advertisements” even if such materials include market commentary or a discussion of an applicable investment thesis. The Proposing Release notes that the proposed definition is not intended to include investor account statements and transaction reports but also states that communications that include market commentary or a discussion of the adviser’s investment thesis may fall within the definition of an “advertisement,” depending on the facts and circumstances.⁷ This distinction is not consistent with current market practices. Reports to existing investors that include information about their investments often include some level of commentary on the performance of the investment. For example, an adviser may discuss how an investor’s investments are doing in comparison to the market and what the adviser’s expectation of future performance of the market may be. Similarly, an adviser may include information about prospective future investments and how these may line up with the adviser’s strategy. If a communication is limited to existing investors, and is primarily designed to explain the performance of the client/investor’s account or investment, it should not be treated as an advertisement.⁸

⁵ *E.g.*, Proposing Release at fns. 111 – 112 and the accompanying paragraph.

⁶ *See, e.g.*, Letter of the Private Equity Growth Capital Council to Secretary Elizabeth M. Murphy on the proposed amendments to Regulation D, Form D and Rule 156 under the Securities Act (Sept. 23, 2013).

⁷ Proposing Release at fn. 60 and the accompanying text.

⁸ *See* Investment Counsel Association of America, Inc., SEC No-Action Letter (March 1, 2004) (the “ICAA Letter”) (noting that “a written communication by an investment adviser to its existing clients generally would not be an advertisement within the meaning of rule 206(4)-1(b) merely because it discusses the adviser’s past specific recommendations concerning securities that are or were recently held by each of those clients. In general, written communications by advisers to their existing clients about the performance of the securities in their accounts are not offers of investment advisory services but are part of the adviser’s advisory services.”).

Second, the SEC should retain the current requirement that an advertisement be a communication directed “to more than one person.”⁹ As the Proposing Release noted, this restriction was originally included so as to exclude “face-to-face” conversations with clients.¹⁰ The AIC believes that modern equivalents to “face-to-face” conversations take a variety of forms using communication technology unavailable when the Advertising Rule was adopted in 1961, which include not just live oral communications, but also text messages, e-mails and social media interactions. The AIC believes that subjecting many of these modern “live” communications that are directed at only one person to the Advertising Rule would create an administrative nightmare for compliance personnel, particularly if the new approval requirements and other new requirements in the Proposed Amendments are implemented (even if such communications do not have to be reviewed by the Designated Person). We further believe that this exclusion should include communications to more than one person when such persons are agents or representatives of the same client or investor. We note that all such communications would still be subject to Rule 206(4)-8 as well as, in many circumstances, the recordkeeping requirements under the Advisers Act.

More generally, the AIC believes the SEC did not adequately consider the combined effect of the expanded definition of an “advertisement” along with the other proposed changes to the Advertising Rule. In particular, the expanded requirements with respect to performance presentations may cause practical issues with respect to nontraditional forms of advertising materials.

To limit this confusion and reduce these burdens, the SEC could instead retain a definition of an “advertisement” that covers only “traditional” forms of advertising materials and communications. As discussed above, the SEC should narrow the definition to exclude (i) investor reports and statements; (ii) one-on-one communications (regardless of the form of communication) including responses to requests for proposals and due diligence questionnaires;¹¹ and (iii) presentations to private fund investors concerning the performance of the funds in which they have invested (for example, at annual meetings of limited partners). These communications would remain subject to the general anti-fraud provisions of the Advisers Act (including Rule 206(4)-8) and, to the extent applicable, the other securities laws.

⁹ Proposing Release at pp. 41 – 42.

¹⁰ Proposing Release at fn. 85 and the accompanying text.

¹¹ The AIC believes that a response to a “request for proposal” or “due diligence questionnaire” requested by a current or prospective investor (or its consultant) is not an advertisement because, in responding to such request, the adviser is generally responding to a request by the investor or prospective investor for “specified information for that requester’s own purposes, rather than responding to a communication disseminated by an adviser for the adviser’s purpose of offering or promoting its services.” While the Proposed Amendments excludes from the definition of an “advertisement” responses to “unsolicited” requests for information, it would be helpful if the SEC confirmed that responses to such a request are not an advertisement even if the adviser previously sent marketing materials or had other contacts with the investor. This confirmation would be consistent with the approach taken in the ICAA Letter.

B. The SEC Should Expand the “Non-Broadcast Live Oral Communications” Exclusion to Include (i) All Unscripted Live Oral Communications, Whether or Not Broadcast, and (ii) Live Written (Not Just Oral) Communications Between an Adviser and Investors.

The Proposed Amendments would exclude “non-broadcast live oral communications” from the definition of an “advertisement.” This is intended to include “live oral communications that are not broadcast on radio, television, the internet, or any other similar medium.”¹² As a general matter, the AIC agrees with this exclusion, which is intended to “retain advisers’ ability to have face-to-face communications with investors” and preserve an adviser’s “ability to communicate directly with existing clients and investors... to the extent such communications do not ‘offer or promote’ the adviser’s services.”¹³

In furtherance of this intent, the AIC believes that the proposed exclusion should be expanded to include non-broadcast live written (in addition to oral) communication. Such an expansion would be consistent with the SEC’s intent “to reflect evolving methods of communication.”¹⁴ As discussed above, as methods of communication have evolved with the rise of technology, a number of communications now take place in live written form (*e.g.*, text messages, e-mails, instant messages). The AIC believes that it is important to acknowledge that such live written communications which are either one-on-one or restricted to a limited number of investors, to the extent that they do not “offer or promote” the adviser’s investment advisory services, are evolving forms of face-to-face communication with investors that should be excluded from the final rule.

Among other things, the SEC seeks comment on whether to extend the exclusion to live oral communications that are broadcast. The AIC believes that this extension would be an important clarification where the adviser may take part of an unscripted public appearance that is otherwise within the scope of the exclusion but which is broadcasted at a later time without the adviser’s consent. Such an extension would also serve to exclude unscripted public appearances where the members of the press are present, but the adviser is not aware of their presence.

The Proposing Release notes that “any script or storyboards, or other written materials prepared in advance for use during a live oral communication, as well as any slides or other written materials presented alongside or distributed as part of the live oral communication, would fall within the proposed definition of ‘advertisement’ if those materials otherwise meet the definition of ‘advertisement.’”¹⁵ The AIC seeks clarification that any such written materials prepared in conjunction with any live oral communications should not be considered “advertisements” and should be able to rely on the exclusion if (i) they are in draft form, (ii) they are internal documents not created for distribution, or (iii) all or portions of their content may not be provided to any prospective or current investor. The AIC believes that this clarification is important in ensuring that no unnecessary burdens are imposed on investment advisers and their compliance programs by imposing the Rule’s requirements on materials that the adviser does not intend to disseminate to prospective or current investors. In many cases, these materials may be

¹² Proposing Release at pp. 39 – 40.

¹³ Proposing Release at p. 42.

¹⁴ Proposing Release at p. 42.

¹⁵ Proposing Release at p. 42.

drafted to shape the investment adviser's remarks with the intent to ensure that no incorrect or misleading information is communicated.

C. The SEC Should Clarify that Communications that Are Not Intended to “Offer or Promote” an Adviser’s Investment Advisory Services or that Do Not “Seek to Obtain or Retain” Investors Be Excluded from the “Advertisement” Definition.

The Proposed Amendments would redefine an “advertisement” to include communications disseminated “to offer or promote” an adviser’s services or that “seek to obtain or retain” investors.¹⁶ Through such revised definition, the SEC intends to focus the proposed definition “on the goal of the communication.”¹⁷

The SEC should confirm that certain communications (including interviews and press discussion) that are not intended to be promotional in nature are excluded from the definition of an “advertisement.” Currently, advisers have a limited ability to speak publicly about the non-investment advisory services that they provide or the fundraisings that they are currently engaged in or may seek to be engaged in. To the extent that such communications are not promotional in nature – that is to say, they do not offer or promote the adviser’s investment advisory services, and they do not seek to obtain or retain investors – the SEC should clarify that such communications fall outside of the scope of the Advertising Rule.¹⁸

D. The SEC Should Clarify the Circumstances under which Third-Party Content Should Be Attributed to an Investment Adviser.

The Proposed Amendments would redefine an “advertisement” to include “any communication, disseminated by any means, *by or on behalf of* an investment adviser.” Among other things, the new definition appears to be designed to make the investment adviser responsible for materials distributed by third parties to the extent that information in such materials can be attributed to the adviser. The Proposing Release notes that this expansion of the definition is “intended to reflect the application of the current rule to communications provided by investment advisers through intermediaries.”¹⁹

The Proposing Release notes that whether to attribute third-party communications to an adviser would depend on a facts-and-circumstances analysis, specifically whether the adviser took affirmative steps in the preparation of the content or whether the adviser explicitly or implicitly endorsed or approved the information.²⁰ As discussed below, the AIC believes that this may result in advisers being responsible for advertising materials disseminated by persons who the adviser does not control.

¹⁶ Proposing Release at fn. 54 and the accompanying text.

¹⁷ Proposing Release at p. 30. In this respect, the AIC asks that the SEC confirm that communications that were sent erroneously to prospective or current investors are not subject to Rule 206(4)-(1).

¹⁸ Examples of such communications include materials concerning the management services and support that the adviser provides to portfolio companies or fundraisings by portfolio companies. These communications are generally designed to attract “deal flow” and are directed to managers or owners of potential portfolio companies and other entrepreneurs and are not directed to potential or existing fund investors.

¹⁹ Proposing Release at pp. 24 – 25.

²⁰ Proposing Release at pp. 25 – 26.

1. Attribution Should Be Limited to Content for which the Adviser Has Final Editorial Control.

The Proposing Release seeks comment on, among other things, whether further clarifications are necessary (including identifying any specific indicia) to determine when a communication is disseminated “on behalf of” an adviser and when an adviser might have exercised “sufficient influence.”²¹ The AIC believes that further clarification is necessary in this respect. In particular, in determining whether the adviser took affirmative steps in the preparation of content, the Proposing Release seems to assume that an adviser’s exercise of control will be effective and does not contemplate instances where the adviser’s comments to third-party content are ignored or not accepted (either in part or in full). For example, if an adviser comments on a draft newspaper article that falls within the definition of an “advertisement,” then the Proposed Amendments appear to attribute the article’s content to the adviser regardless of whether the article was edited to reflect the adviser’s comments. The AIC believes that it is inappropriate to attribute such content to advisers and may have the unintended consequence of discouraging an adviser from correcting information that is going to be widely disseminated but is prepared by third parties over which the adviser has no control.

Further, to this end, the SEC should clarify that, to the extent that the adviser’s control, editing or similar rights are limited to only a section of the information being presented, and the adviser does not have any rights as to the distribution of the content, then only the information over which the adviser has final editorial control should be subject to the Advertising Rule.

Similarly, in determining whether an adviser has endorsed content distributed by intermediaries, the SEC should clarify that, in the fund-of-funds context, information provided by an underlying fund manager would not be considered an “advertisement” by such underlying fund manager if an unaffiliated fund of funds sponsor shares that information with its underlying investors. A similar concern arises where an unaffiliated investment adviser distributes materials to high net worth investors (whether through a consulting relationship or through a high net worth “feeder”). In such instances, the underlying fund manager has little to no information on the ultimate recipients of such information and does not have control as to what content is shared (or omitted) and the manner in which the content is disseminated. Furthermore, to the extent that the information includes performance information, the underlying fund manager may face practical difficulties in determining whether the material will be disseminated to Retail Investors (as defined by the Proposed Amendments).

2. Exceptions Should Be Made for Third-Party Content Online that Is Edited by an Adviser According to a Set of Neutral, Pre-Established Policies and Procedures.

The Proposing Release acknowledges that determining the scope of attribution can be challenging in light of social media and third-party platforms that allow users to express their views. In this respect, the Proposing Release requested comment on, among other things,

²¹ Proposing Release at p. 29.

whether to allow editing of third-party content pursuant to a set of neutral, pre-established policies and procedures without attributing the content to the adviser.²²

The AIC believes that advisers would benefit from the ability to apply community guidelines or a set of neutral, pre-established policies and procedures on content found on social media and online sources. In particular, the AIC believes that it is important for advisers to be able to edit or remove certain online content if the adviser is acting in accordance with a policy that is disclosed and is not intended to suppress bona fide and material negative comments. In particular, such policies could be limited to the removal of spam, links to external webpages, irrelevant comments, repeat comments from common offenders using the same IP address, and profane or inappropriate language.

III. The General Prohibitions.

A. The Expansion of the General Prohibitions Is Inappropriate, Particularly as They Might Apply to Private Fund Sponsors.

As a general matter, the AIC believes that, to the extent that the Advertising Rule is applicable to communications with investors in private funds, the existing general anti-fraud provision in Rule 206(4)-1(a)(5), as well as Rule 206(4)-8, which are based on well-understood concepts under the U.S. securities laws, are sufficiently protective of investors. Expanding the general anti-fraud provision of the Rule (which currently prohibits “any untrue statement of a material fact, or which is otherwise false or misleading”) to seven “general” anti-fraud provisions as proposed is unnecessary and appears to be designed to incorporate concepts from other regulatory schemes, including FINRA and those applicable to mutual funds. In particular, the Proposing Release cites FINRA Rule 2210 and Rule 156 under the Securities Act as influencing a number of the proposed prohibitions.²³ We believe that these changes will also impose additional recordkeeping burdens on investment advisers.

As a general matter, Rule 156 was adopted to create a framework for retail products following the SEC’s withdrawal of its Statement of Policy on registered investment company sales literature.²⁴ It was designed to “provide some guidance to persons who wish to determine whether [mutual fund] sales literature is misleading.”²⁵

It is unclear why the SEC believes that applying Rule 156 to private funds is necessary. As the AIC has previously commented, such an expansion may lead regulators and investors to equate private equity funds offered to sophisticated investors with retail mutual funds – which are two distinctively different investment vehicles.²⁶ Further to this point, any experience gained from the application of Rule 156 would appear to be limited to the distribution of marketing materials

²² Proposing Release at p. 30.

²³ *E.g.*, Proposing Release at fns. 111 – 112 and the accompanying paragraph.

²⁴ Mutual Fund Sales Literature Interpretive Rule, SEC Release Nos. IC-10915; 34-16299; 33-6140 (Oct. 26, 1979) (“Rule 156 Adopting Release”); Investment Company Sales Literature Interpretive Rule, SEC Release Nos. IC-10621; 34-15621; 33-6034 (Mar. 8, 1979) (“Rule 156 Proposing Release”).

²⁵ Rule 156, Proposing Release at fn. 4 and the accompanying text.

²⁶ Letter of the Private Equity Growth Capital Council to Secretary Elizabeth M. Murphy on the proposed amendments to Regulation D, Form D and Rule 156 under the Securities Act (Sept. 23, 2013).

to retail investors of mutual funds and not more broadly applicable to sophisticated investors in private funds.

At a minimum, these types of prohibitions should be limited to retail accounts that invest in publicly traded securities.

B. The General Prohibition against Unsubstantiated Material Claims Is Unnecessary and Will Impose Considerable Burdens.

The Proposed Amendments would prohibit any material claim or statement that is unsubstantiated. The Proposing Release states that this requirement is similar to provisions contained in FINRA Rule 2210 and Rule 156 under the Securities Act.²⁷

As noted above, the AIC does not believe that applying FINRA Rule 2210 and Rule 156 to private fund sponsors is necessary or appropriate. The current anti-fraud prohibitions are sufficiently protective of recipients of advertisements, as these already ensure that investment advisers disseminate information that is truthful and not misleading.

If the proposed prohibition is included in the final rule, the SEC should provide further guidance on its application and the intended burdens on advisers. Specifically, the AIC and its members seek further guidance on the intended effects of this prohibition on an adviser's books and records, including, for example, whether an investment adviser would be expected to retain records that substantiate any statement contained in an advertisement. Such guidance should be taken into account in the SEC's assessment of the cost and paperwork burdens that would be imposed by the Proposed Amendments.

IV. The Proposed Amendments Would Impose Unnecessary and Burdensome Compliance Requirements on Advisers that Are Duplicative of Current Obligations.

A. The "Designated Person" Provision of the Proposed Amendments Is Unnecessary and Will Impose Additional Compliance Burdens on Investment Advisers.

As noted above, the Proposed Amendments would prohibit an investment adviser from disseminating an advertisement unless the advertisement "has been previously reviewed and approved as being consistent with the requirements of this section by a [Designated Person]." The Proposing Release states that the SEC believes that this new requirement "may reduce the likelihood of advisers violating the proposed rule" and that "requiring a written record of the review and approval of the advertisement will allow our examination staff to better review adviser compliance with the rule."

Investment advisers, including private fund sponsors, currently have adequate incentives to comply with the Advertising Rule – compliance is required by law and subject to review by the SEC's examination program. Moreover, registered investment advisers must, under Rule 206(4)-7, adopt policies and procedures reasonably designed to prevent violations of the Advisers Act and the rules adopted thereunder by the firm and its supervised persons. We

²⁷ Proposing Release at fn. 117 and the accompanying text.

believe that the Chief Compliance Officers of private fund sponsors invest considerable time and resources in developing such policies, including policies and procedures designed to comply with the Advertising Rule and Rule 206(4)-8. These policies will generally include a process for reviewing the disclosures that will be used in private fund marketing materials.²⁸ Given the existence of, and the SEC's rigorous enforcement of, Rule 206(4)-7, the proposed Designated Person requirement will require modifications of compliance systems previously established by many firms. The suggestion that the review of each advertisement be documented will also impose additional recordkeeping and compliance burdens on firms. The AIC strongly believes that this provision should not be adopted.

B. The AIC Does Not Believe that Any New or Additional Policies and Procedures Should Be Required to Be Implemented by Advisers to Ensure Compliance.

The Proposed Amendments include a number of instances requiring (or suggesting that it may be required for) an adviser to implement new or additional policies and procedures in order to ensure compliance with the Proposed Amendments. For example, the Proposing Release notes that an adviser who wishes to use third-party ratings “should develop policies and procedures to implement [a] ‘reasonable belief’” that all requisite disclosures have been made.²⁹ Similarly, the definition of “Non-Retail Advertisement” would require that an adviser adopt and implement “policies and procedures reasonably designed to ensure that the advertisement is disseminated solely to non-retail persons.”³⁰ With respect to the presentation of hypothetical performance, the Proposed Amendments would also require that an adviser adopt “policies and procedures reasonably designed to ensure that [such performance] is disseminated only to persons for which it is relevant to their financial situation and investment objectives.”³¹

The AIC does not believe that these explicit requirements to adopt new or additional policies and procedures are necessary and believes that they are, in fact, duplicative of advisers' existing obligations. As noted above, advisers are already subject to (and robustly examined on) broad and well-understood compliance requirements under Rule 206(4)-7 of the Advisers Act. The AIC believes that the existing compliance requirements are sufficiently protective of current and prospective investors to ensure compliance with the Proposed Amendments. Moreover, any explicit requirements of new or additional policies and procedures may create confusion given the overlapping nature of Rule 206(4)-7's obligations.

²⁸ The Proposing Release, in fact, recognizes that “most advisers currently require such reviews for broadly disseminated communications.” Proposing Release at p. 194.

²⁹ Proposing Release at p. 93.

³⁰ Proposing Release at p. 110. We would note that the Proposing Release contrasts this new requirement against current obligations under Rule 2a51-1(h) under the Investment Company Act. In particular, the Proposing Release notes that the SEC believes “that many investment advisers have developed policies and procedures to implement this ‘reasonable belief’ provision. Accordingly, [the SEC believes] that advisers would utilize or modify those same policies and procedures as necessary to comply with the proposed rule.” Proposing Release at pp. 112 – 113.

³¹ Proposing Release at 161.

V. The Conditions Imposed on the Use of Testimonials, Endorsements, and Third-Party Ratings Are Unnecessary and Unduly Burdensome.

A. The Use of Testimonials Remain Subject to Too Many Conditions.

The Proposed Amendments would allow the use of testimonials, endorsements, and third-party rankings subject to certain conditions. While the elimination of the testimonial prohibition is welcome, the commentary in the Proposing Release suggests that the use of testimonials will continue to be significantly restricted.

The Proposing Release notes that the general anti-fraud prohibitions retained in the Proposed Amendments would prohibit the “cherry-picking” of testimonials.³² As such, an adviser could not use a single testimonial or subset of testimonials if the testimonial(s) were not representative of that adviser’s investors. The Proposing Release further notes that a general disclaimer that the testimonial “may not be typical of all investors” would not be sufficient to allow the adviser to use such testimonial.³³ The Proposing Release does not suggest how an adviser may ascertain whether a testimonial is representative of that adviser’s investors. Such a determination may require that an adviser poll or survey a material sample of its investors. (The AIC understands that it is rare for advisers to conduct such polls or surveys of investors.) Even if an adviser were to engage in such a poll or survey, it may not be practical to determine whether certain testimonial statements are representative of that adviser’s investors.

The AIC believes that applying these principles to the testimonials in the fashion that the SEC suggests in the Proposing Release is overly restrictive and does not accommodate different facts and circumstances. For example, an investment adviser should be able to present testimonials that (i) are accurate quotations from an investor or client, (ii) do not include performance information or information that the adviser knows to be inaccurate, (iii) are presented only to sophisticated investors, and (iv) are accompanied by appropriate disclosure, including the name of the investor, the fact that the investor’s experience may not be representative, and any other material facts about the relationship that the investor has with the adviser (*e.g.*, familial or material economic arrangement).³⁴

Similarly, the Proposing Release suggests that this same condition would apply to endorsements. As such, the Proposing Release suggests that an adviser may be required to poll non-investors in order to determine whether an endorsement is representative of other non-investors. The application of this condition to endorsements would raise the same issues as with respect to testimonials, discussed above. Therefore, the AIC believes that the SEC should instead adopt an approach that is more flexible based on the facts and circumstances of how (and to whom) the endorsement is presented. Furthermore, we note that adopting the Proposed Amendments (along with the guidance in the Proposing Release) would represent a restriction on how endorsements

³² Proposing Release at pp. 82 – 84.

³³ Proposing Release at fn. 167.

³⁴ As a separate matter, while the Proposed Amendments would define a “testimonial” as “any statement of a client’s or investor’s experience with the investment adviser or its advisory affiliates, as defined in the Form ADV Glossary of Terms,” the AIC asks the SEC to confirm that statements in marketing materials (such as pitchbooks or other private equity promotional materials) from the management of underlying portfolio companies would not be considered “testimonials” subject to the Proposed Amendments.

are currently treated – namely, endorsements are presently subject to the general anti-fraud provisions of the Advertising Rule (and the other applicable anti-fraud provisions of the U.S. federal securities laws) without any prescriptive conditions on their use.

B. The Additional Requirements Imposed on Third-Party Ratings Are Unnecessary.

Similarly, the use of third-party ratings, while subject to the general anti-fraud provisions, is not specifically addressed by the Advertising Rule. The Proposed Amendments would require that an adviser form a reasonable belief that any questionnaire or survey used in the preparation of the third-party rating was (i) not designed to produce a pre-determined result, or (ii) structured to allow participants to provide both positive and negative responses.³⁵ This condition would likely require that an adviser have access to the questionnaire or survey used in the preparation of the rating.

In light of the fact that third-party ratings are generally conducted by a third party unaffiliated with the adviser and that the adviser does not have control over the process used in order to determine the rating, it is unclear what concern this condition is intended to address. Specifically, if the adviser was not involved in the determination of the rating (other than to provide any requested information to the third party conducting the rating), additional conditions seem unnecessary.

Finally, the Proposed Amendments would already require that advertisements that include third-party ratings disclose certain information, such as whether compensation was paid to the third party in connection with the rating. This disclosure should provide sufficient information for a recipient to evaluate the rating in connection with deciding to retain an investment adviser or invest in a private fund.

VI. Definition of “Retail Person.”

A. The Proposed Definition of “Non-Retail Person” Poses Significant Compliance Challenges and Does Not Reflect Market Practices in Private Equity.

The AIC commends the SEC for proposing to include a distinction between retail and non-retail recipients of advertisements. The change is intended to acknowledge that Non-Retail Persons have “sufficient resources to consider and analyze certain types of performance information without additional disclosures and conditions.”³⁶ The Proposed Amendments would define a “Non-Retail Advertisement” as an advertisement for which an adviser has adopted and implemented policies and procedures reasonably designed to ensure that the advertisement is disseminated solely to “qualified purchasers” and certain “knowledgeable employees” (each, as defined in the Investment Company Act).³⁷ Any other advertisement would be a “Retail Advertisement.” As such, the Proposed Amendments would require a fund sponsor to determine whether any current and prospective investor in a pooled investment vehicle is a “qualified

³⁵ Proposing Release at p. 93.

³⁶ Proposing Release at p. 110.

³⁷ Proposing Release at p. 109.

purchaser” or “knowledgeable employee” at the time the advertisement is disseminated for the purpose of identifying the conditions applicable to such advertisement.

1. The “Non-Retail Person” Definition Should Be Expanded to Include “Accredited Investors” and “Qualified Clients.”

The AIC believes that the Non-Retail Person definition should be expanded to include both Accredited Investors and Qualified Clients. The AIC believes that the Accredited Investor and Qualified Client standards would be sufficiently protective of advertisement recipients. In the first instance, the Accredited Investor standard is already intended to identify “the particular class of persons [that] needs the protections of the Securities Act” and is a well-known and understood proxy for an investor’s ability to “assess an investment opportunity” and “bear the risk of a loss.”³⁸ Similarly, the Qualified Client standard is intended to identify “persons with whom a registered investment adviser may enter into an advisory contract” and recognizes that such persons have the “financial experience and ability to bear the risks of performance arrangements, including the risk of loss that are inherent in those arrangements.”³⁹ If the Proposed Amendments are adopted as proposed, the AIC expects that private fund sponsors will reduce the number of private funds that rely on Section 3(c)(1), as private fund sponsors are likely to conclude that the additional burden of preparing marketing materials for Retail Persons may not be worth the time and effort. The AIC believes that the recommended expansion of the Non-Retail Person definition to include Accredited Investors and Qualified Clients would facilitate a private fund sponsor being able to provide a uniform set of marketing materials to investors in a Section 3(c)(1) fund, would prevent any unintended consequences or adverse effects on capital raising, and would also ease some of the compliance issues discussed below.

2. The Proposed Definition of “Non-Retail Person” Undercuts the Broad Scope of Securities Law Exceptions that Advisers Rely on for Private Placements.

Investors in a private fund that relies on Section 3(c)(7) must be Qualified Purchasers. In practice, however, a private fund sponsor may, on occasion, rely on other exceptions under the Investment Company Act that do not require investors to be Qualified Purchasers. For example, an adviser may rely on Section 3(c)(1) of the Investment Company Act for purposes of raising investment vehicles targeted at its employees or “friends and family” of the private fund sponsor. Because such investors may not qualify as “Non-Retail Persons” as defined in the Proposed Amendments, a fund sponsor could be required to prepare multiple marketing materials for dissemination to each set of investors. Such a result will be cumbersome and will impose compliance burdens that are unnecessary given the nature of the investors in these parallel funds. This difficulty would likely be avoided if the definition of Non-Retail Persons was expanded to include Accredited Investors.

The Proposed Amendments also do not take into account fund offerings that occur outside of the United States and are therefore not subject to registration requirements under the Investment Company Act or the Securities Act. Specifically, if a fund organized outside of the United States

³⁸ *Amending the “Accredited Investor” Definition*, Release Nos. 33-10734; 34-87784; File No. S7-25-19 (Dec. 18, 2019).

³⁹ Proposing Release at pp. 117 – 118.

is relying on Regulation S under the Securities Act, an adviser may not require that investors who are not “U.S. Persons” (as defined in Regulation S) be Qualified Purchasers. We do not believe that it is necessary for the SEC to extend the additional disclosures required for Retail Investors to non-U.S. persons who are investing in such funds outside of the United States. Such offerings will likely be subject to investor protection regulations in those jurisdictions.

3. The Definition of “Non-Retail Person” Will Pose Compliance Challenges.

The definition of a “Non-Retail Advertisement” will pose significant and unnecessary compliance challenges in the private fund context. The most significant (and unnecessary) burden is the requirement that the adviser develop a reasonable belief as to the status of an investor as a Non-Retail Person prior to disseminating an advertisement. The Proposing Release states that the SEC “believe[s] that many investment advisers have developed policies and procedures to implement this ‘reasonable belief’ provision” in connection with investments in private funds and “that advisers would utilize or modify those same policies and procedures as necessary to comply with the proposed rule.”⁴⁰

However, as required by Section 3(c)(7) of the Investment Company Act and Rule 3c-5 thereunder, private fund sponsors determine an investor’s status as a “qualified purchaser” (or “knowledgeable employee”) at the time the investor agrees to acquire an interest in the private fund. Often, these policies and procedures include questionnaires that are completed as part of the private fund’s subscription process, long after advertising materials typically have been distributed. As a market matter, prospective investors generally are unwilling to complete detailed questionnaires regarding their assets or financial sophistication until they understand and wish to pursue an investment opportunity.

Therefore, the AIC disagrees that private fund sponsors will be able to apply the same policies and procedures with respect to advertisement distributions as it is difficult and sometimes impractical to have all investors accurately complete questionnaires prior to distributing fund marketing materials. In particular, applying the “look-through” requirements under the Securities Act or Investment Company Act to investors may be a time-consuming exercise in which investors may be reluctant to participate prior to investment.

The proposed distinction between Retail and Non-Retail Advertisements could have the unintended consequence of subjecting all communications to the higher retail standard. As discussed above, in light of current requirements and practices, advisers to private funds may not know whether new potential investors are Retail or Non-Retail Persons until after the investor has submitted its investor qualification statement, which typically occurs after advertising materials are provided.

Similarly, private fund advisers often begin marketing a fund with the expectation that the fund will be available only to Qualified Purchasers, but, due to a variety of factors, the adviser may later decide to open the fund to non-Qualified Purchasers. If such advisers did not begin with marketing materials prepared for Retail Persons – despite the adviser’s intention to market the

⁴⁰ Proposing Release at p. 112.

fund to Non-Retail Persons only – the adviser could be forced to expend additional time and resources in order to revise its marketing materials for newly targeted Retail Persons. The AIC believes that preparing separate marketing materials for Retail and Non-Retail Persons in anticipation of various unknowns would impose a significant burden for private fund sponsors with a significant potential for compliance errors.

These issues can be heightened as they relate to fund-of-funds or similar investors if the private fund sponsor is required to determine the status of the investors before providing marketing materials. Such pooled investment vehicles may have other pooled investment vehicles as investors, requiring further levels of review up a fund-of-funds structure. The underlying fund manager may be faced with information barriers in looking through complex fund-of-fund structures, a challenge further aggravated by confidentiality obligations that fund-of-fund investors typically negotiate with their own beneficial owners, thereby further limiting the underlying fund manager’s ability to receive necessary information to assess their status. Without a practical limitation on the look-through requirement, it may become impractical for an underlying fund manager to provide marketing materials appropriate for a Non-Retail Person for use in the marketing of a fund-of-funds (which is likely to rely on Section 3(c)(7) and thus be limited to Non-Retail Investors). Requiring that the adviser assume that any such marketing materials be treated as Retail Advertisements would have the result of providing Non-Retail Persons with information that they do not need or require.

In any event, if the final rule retains the current definition of “Non-Retail Persons,” it should include a presumption that advertisements for Section 3(c)(7) funds should always be deemed to be “Non-Retail Advertisements” since investors in such funds, by definition, are limited to Non-Retail Persons. Any investor who is not a Non-Retail Person would be prohibited from making an investment in the fund, so there would be no actual harm if such person received an advertisement regarding the Section 3(c)(7) fund. Furthermore, this exclusion would address the issue discussed above, since the private fund sponsor could continue to rely on applying its existing policies and procedures regarding developing a reasonable belief that an investor was a “qualified purchaser” or “knowledgeable employee” at the time of investment.

B. The Proposed Definition of “Non-Retail Person” Should Be Expanded to Include Other Kinds of Sponsor Employees.

To better reflect the current regulatory framework, market practices, and the sophistication of private equity investors, the Proposed Amendments should be further modified to expand the definition of Non-Retail Person to include employees of the investment advisers and their family members.

The AIC appreciates the SEC’s acknowledgement that certain investors who are not Qualified Purchasers may still have the requisite sophistication and resources to consider and analyze certain types of investment performance. The only category of persons recognized, however, is limited to “knowledgeable employees” (as defined in the Investment Company Act). The AIC requests that the SEC consider expanding this category to include (i) any “supervised person” of the adviser, and (ii) any person or entity that provides bona fide services to either the adviser, the private fund that the adviser manages, or the portfolio companies owned by such private fund. The AIC believes that such persons, like Knowledgeable Employees, are individuals that “have a

significant amount of investment experience” and who participate in the investment activities of the private equity fund “in connection with their regular functions or duties.”

VII. Differing Conditions between “Retail” and “Non-Retail” Advertisements.

A. The Requirement to Provide a Schedule of Fees and Expenses When Disseminating Gross Performance to Non-Retail Persons Is Unnecessary.

The AIC applauds the proposed amendment that would no longer require that net performance be provided to Non-Retail Persons. However, we believe that the approach proposed by the SEC should be refined.

The Proposed Amendments would prohibit the use of “gross performance” in Non-Retail Advertisements unless the adviser “provides or offers to provide promptly a schedule of fees or expenses to the investor.”⁴¹ The Proposing Release claims that Non-Retail Persons, even with their increased bargaining power, may struggle at times to negotiate to receive transparent information.⁴²

The Proposed Amendments overlook the flexibility afforded under the current regulatory framework to tailor disclosures based on the particular private fund and specific investors. Private fund sponsors engage in a wide range of strategies and asset classes (including private equity, credit, infrastructure and real estate), and private funds are structured in different ways (including for tax and regulatory reasons). To reflect these differences, the fees and expenses that are charged (and the way they are charged) vary significantly among private funds. As a result of this, investors in private equity funds can, and do, negotiate for targeted disclosure of fees and expenses, tailoring disclosure based on the specific investments. In fact, investors in private equity have been reluctant to press for “standardized” disclosures imposed by third parties. This is reflected, for example, by the limited market acceptance among the sponsor and investor communities of ILPA’s proposed standardized disclosure framework. This limited acceptance may reflect the fact that variations in private fund expense structures may make “standardized” disclosures more difficult to provide or less useful to private fund investors. Therefore, any cookie-cutter approach to fee and expense disclosure may actually obfuscate important differences in the fee structures of different types of private funds.

The required schedule is also in contrast with the Proposing Release’s rationale in differentiating between a Retail and Non-Retail Person for purposes of performance advertisement. In choosing the “qualified purchaser” standard as the basis for defining a “Non-Retail Person,” the Proposing Release acknowledges that “qualified purchasers are regularly in a position to negotiate the terms of their arrangements with investment advisers, whether as separate account clients or as fund investors.” In fact, the Proposing Release goes further and notes that a Qualified Purchaser’s “access to analytical and other resources generally provides them with the opportunity to ask

⁴¹ Proposing Release at fn. 256 and the accompanying text.

⁴² Proposing Release at fn. 260 and the accompanying text citing a letter from the Institutional Limited Partners Association (“ILPA”).

questions of, and receive information from, the appropriate advisory personnel, and enables them to assess that information before making investment decisions.”⁴³

The AIC has previously commented on the various opportunities that sophisticated investors have (and use) during the course of negotiations to both ask for and receive information and negotiate issues (including requests to receive additional information over the life of a private fund).⁴⁴ The AIC continues to believe that the negotiation process is robust and provides for a constructive engagement between the parties and that the SEC does not need to, and should not, amend its rules in a way that would unnecessarily interfere with this process, particularly in light of the sophistication of private equity fund investors.

Furthermore, the SEC does not consider the variety of situations where creating such a schedule of fees and expenses may be difficult or speculative. For example, a firm may spin out from a larger financial institution where all of the investments were proprietary investments made using the balance sheet of the financial institution. In such circumstances, there may have been no fees and expenses, or the fees and expenses that were charged with respect to the investments may have been materially different both in amounts and in structure. Similarly, for a newly created private equity fund, the creation of a schedule of fees and expenses may prove to be particularly difficult if it is expected that the fee schedule will reflect the carried interest received by the fund’s general partner. While carried interest is not a fee or expense borne by investors, but rather a general partner’s profit interest retained at the time a private equity fund makes an investment, the inclusion of carried interest on such a schedule can provide important information when reviewing a private equity fund’s performance. In the absence of realization, however, it will be difficult for an investor to appreciate the impact of the carried interest on fund performance if the fund has not generated returns yet. Finally, in the private fund context, in light of the diversity of products and strategies, it is unclear what fund expenses would need to be included or how certain fees and expenses (like management fee offsets) would need to be reflected. As such, we believe that the process of creating a track record that reflects fees and expenses is, in the private fund context, best left to be negotiated between fund sponsors and any prospective investors that desire them. These specific issues often are present for new firms or where a firm is starting a new strategy, and, therefore, restricting the flexibility to present gross performance to sophisticated investors would restrict competition and choice in investment products.

If the SEC determines that a schedule of fees and expenses should be required to be offered to Non-Retail Persons, then it should not be required to be provided when providing Non-Retail Persons with certain kinds of customized performance. In particular, when advisers choose to portray related, extracted, and hypothetical performance, the presentation may not be based on actual portfolios and investments. In the context of extracted performance, for example, assigning a portion of a fund’s overall organizational or other expenses to a single transaction or to a subset of transactions would require a number of assumptions that could greatly increase the possibility to mispresent information and reduce the utility of the information to prospective investors. As such, a fee and expense schedule would be speculative and potentially misleading.

⁴³ Proposing Release at p. 111.

⁴⁴ Letter of the American Investment Counsel to Brent J. Fields, Secretary, Securities and Exchange Commission (Feb. 15, 2019).

Additionally, the AIC seeks clarification that, if the requirement to provide a schedule of fees and expenses is implemented in the final rule, the schedule of fees and expenses associated with related (and extracted) performance would only be required to include fees and expenses that are common across all underlying investments. In particular, for large investment managers with many and differing products and accounts, it may become burdensome to create an itemized schedule of fees and expenses for each underlying portfolio and investment. It is also unclear what benefit the recipients of marketing materials and other materials deemed to be advertisements would receive from such information. As such, the AIC seeks clarification that any schedule of fees and expenses required for related (and extracted) performance would only need to include fees and expenses that are portfolio-wide – that is to say, fees and expenses that are charged across all underlying investments in the related or extracted performance.

B. Private Equity Funds Should Not Be Required to Provide Performance for Prescribed Time Periods in Retail Advertisements.

The Proposed Amendments would require that performance information in Retail Advertisements include the “performance results of the same portfolio for 1-, 5-, and 10-year periods.” The Proposing Release notes that the inclusion of such prescribed time periods would “provide the audience with insight into the experience of the investment adviser over set periods that are likely to reflect how the advertised portfolio(s) performed during different market or economic conditions.”⁴⁵

While such presentations may be appropriate for certain types of funds (such as mutual funds), this approach is unwarranted (and may be confusing) in the context of a private equity fund. Such periods (especially 5- and 10-year periods) may not exist for the portfolio advertised. The fund that is offered will typically not have any performance to report, and, for private fund sponsors that offer a new fund approximately every three years, even the previous fund may not have 5- or 10-year performance period available. Unlike the performance of mutual funds with actively managed portfolios, the performance of closed-ended private equity funds can be expected to vary substantially over the term of the fund, which generally lasts between seven and twelve years, with early years often negatively impacted by organizational expenses’ “J-curve” effect on net performance. While the use of prescribed time periods may be appropriate for funds that offer investors the opportunity to redeem their interests, this is not the case with private equity funds.

C. The Requirement to Include a Side-By-Side Comparison of Positive Performance and a Comparable Index or Benchmark Should Be Limited to Retail Advertisements.

The Proposed Amendments would prohibit that an advertisement “include any untrue statements of a material fact, or that omit a material fact necessary in order to make the statement made, in light of the circumstances under which it was made, not misleading.” The Proposing Release cites as an example “advertising that an adviser’s performance was positive during the last fiscal year may be misleading if the adviser omitted that an index or benchmark consisting of a substantively comparable portfolio of securities experienced significantly higher returns during

⁴⁵ Proposing Release at pp. 130 – 131.

the same time period.”⁴⁶ As such, in order to avoid misleading investors, advisers in this case would be required to “include the relevant index or benchmark or otherwise disclose that the adviser’s performance, although positive, significantly underperformed the market.”⁴⁷

The AIC believes that any such side-by-side comparison should only be required, if at all, for Retail Advertisements. The AIC believes that it is consistent with the Proposing Release to assume that Non-Retail Persons, having “resources to consider and analyze... performance information without additional disclosures and conditions,” would not require such side-by-side comparisons. This approach is also consistent with the Proposed Amendments’ elimination of a side-by-side comparison of gross and net performance for Non-Retail Advertisements.

D. Advertisements Provided to Non-Retail Persons Should Be Exempt from the Prescriptive Restrictions of the Proposed Amendments.

The AIC believes that other specific requirements of the Proposed Amendments should not apply to Non-Retail Persons. For example, as discussed above, the presentation of testimonials and endorsements are much less likely to be subject to misunderstanding when provided to Non-Retail Persons who are more capable of assessing the value of statements from third parties. For similar reasons, the AIC believes that investment advisers should be provided greater flexibility when presenting case studies to Non-Retail Persons. As noted above, the AIC believes that it is unnecessary to apply the Advertising Rule to private fund marketing materials – but if it is, the SEC should provide greater flexibility for private fund sponsors, consistent with its views on Non-Retail Persons, to evaluate all advertisements provided to Non-Retail Persons with a flexible facts-and-circumstances approach under the general anti-fraud provisions of the Advertising Rule.

VIII. The AIC Would Appreciate Further Clarification on a Number of Points Related to Performance Presentations.

A. The SEC Should Clarify that a Private Fund’s Related Performance Is Not Required to Include the Performance of Separately Managed Accounts or of Previous Funds.

The Proposed Amendments would define a “related portfolio” as a “portfolio, managed by the investment advisers, with substantially similar investment policies, objectives, and strategies as those of the services being offered or promoted in the advertisement.”⁴⁸

The AIC seeks clarification that this definition would not include separately managed accounts (“SMAs”). In certain circumstances, investment advisers may choose to negotiate SMA s on a one-on-one basis with certain investors or clients. These SMA s are generally customized to reflect specific investment objectives and desired restrictions and investments of a client. In addition, while these SMA s may have similar investment policies, objectives, and strategies than the private funds that the investment adviser manages, SMA s tend to have varying structures and have customized fees and expenses that may not be comparable to private funds. Thus, the AIC

⁴⁶ Proposing Release at pp. 54 – 55.

⁴⁷ Proposing Release at p. 55.

⁴⁸ Proposing Release at fn. 278 and the accompanying text.

believes that it would be inappropriate and inconsistent with the intent of the Proposed Release to include SMAs in the definition of a “related portfolio.”

Similarly, the AIC seeks clarification that this definition is not intended to include previous funds (either on a fund-by-fund or composite basis depending on the related performance triggering the requirement). In particular, including the performance of an adviser’s earlier funds (even if these funds have substantially similar investment policies, objectives, and strategies) may not be representative of more recent performance. The markets in which many private equity funds invest and operate are dynamic and likely to change considerably over time. Successor funds may be substantially larger than previous funds, resulting in larger investments or more diverse investment portfolios. Successor funds may also benefit from changes in the investment team over time. The inclusion of such portfolios may make private placement offering materials and pitch books unduly long and complex, particularly for private fund advisers with long firm histories.

B. The SEC Should Clarify that Performance Targets Are Not Hypothetical Performance.

The Proposing Release notes that projections reflect the returns that an adviser believes it can achieve. By comparison, a target reflects the return that an adviser may seek to achieve based on the risk/returns of its proposed investment strategy. Such targets are useful to private fund investors as they seek to include different targeted return profiles in a diversified portfolio of private funds. Yet, the Proposing Release appears to treat both such presentations as “hypothetical” performance. While projected returns are hypothetical in nature, target returns are not. Target returns are intended to reflect an adviser’s goal over a prescribed period of time, typically based on the adviser’s methodology for underwriting the investments that will appear in the relevant fund’s portfolio. While target returns may be based on past performance, they are aspirational in nature and not intended to convey hypothetical or projected future performance. Thus, it is unnecessary to subject performance targets to the same framework as other types of hypothetical or projected investment performance.

C. The SEC Should Clarify that, When Showing Hypothetical Performance, the Adviser Should Not be Required to Speculate on the Likelihood of a Given Event Occurring.

Among the prescribed conditions in order to show hypothetical performance, the Proposed Amendments would require that an adviser “provide sufficient information to enable the recipient to understand the criteria used and assumptions made in calculating the hypothetical performance.”⁴⁹ While the AIC believes that this language is consistent with market practice, the Proposing Release suggests that this would include disclosing “the likelihood of a given event occurring” for purposes of providing information on the underlying assumptions.⁵⁰ The AIC believes that this information might result in a summary of the basis for the assumptions becoming unduly speculative. Requiring the adviser to engage in such speculation is

⁴⁹ Proposing Release at p. 168.

⁵⁰ Proposing Release at pp. 172 – 173.

unreasonable, particularly in the context of presentations to Non-Retail Investors (who are capable of analyzing the reasonableness of the adviser's assumptions).

D. The SEC Should Clarify that Providing an Adviser's Full One-Year Track Record Would Allow the Adviser to Present Past Specific Performance, Case Studies and Other Select Performance.

The Proposed Amendments would eliminate the requirement under the current rule that prohibits references to past specific recommendations in an advertisement that do not set out or offer to furnish a list of all recommendations made by such investment adviser in the last year. The Proposing Release also notes that, if an adviser chooses to provide a list of all specific investment advice made in a period of no shorter than the preceding year, such a list would meet the Proposed Amendment's "fair and balanced" standard.⁵¹ The AIC appreciates the flexibility that would be provided by the Proposed Amendments to present performance information without furnishing a one-year track record as well as the acknowledgement that presenting a full one-year track record will meet the proposed "fair and balanced" standard.

The AIC believes that the SEC should also acknowledge that by presenting a complete list of investments for the applicable track record, the investment adviser has the flexibility to provide case studies and other information with respect to some of these investments without running the risk that its selection of such case studies would not be deemed to be fair and balanced or otherwise misleading.

E. The SEC Should Clarify the Framework for the Portability of Performance.

The Proposing Release seems to suggest that disclosing the performance that an investment team achieved at a prior firm would be subject to a number of new conditions that are not currently required under SEC No-Action Letters. The AIC seeks clarification that the standards for integrating performance into a firm's track record were not intended to be raised.

AIC believes that there are circumstances where it is beneficial for investors to be provided with information concerning the experience that members of the investment team may have acquired at prior firms (including information concerning the performance of investments where the employee participated in the sourcing, execution, oversight or disposition of such investments), provided such information is presented in a manner that is not misleading (and the firm has the former employer's permission to use such information). Generally, this would include disclosure that the performance is not part of the track record of employee's current firm and other material facts concerning the performance (*e.g.*, the person's role at the prior firm, the role of other persons at the prior firm, and differences in the investment strategies). The AIC believes that any overly restrictive approach to the presentation of performance from prior firms may result in clients or investors being denied information that they may consider useful in evaluating whether to retain an adviser or invest in a fund.

⁵¹ Proposing Release at p. 67.

IX. The AIC Does Not Believe that Any Additional Changes Are Required to Form ADV in order to Implement the Final Rule and Ensure Compliance.

The Proposed Amendments would amend Item 5 of Part 1A of Form ADV to add a subsection “to require information about an adviser’s use in its advertisements of performance results, testimonials, endorsements, third party ratings, and its previously investment advice.”⁵² The proposed amendments to Form ADV seem inconsistent with the other disclosures currently required. The AIC does not believe that such amendments are necessary in order to monitor compliance with the final rule or for the SEC to prepare for examinations, especially as the SEC’s Office of Compliance Inspections and Examinations has other tools currently at its disposal, which it has historically used for the same efforts (such as requesting a firm to provide information concerning its advertising practice in its document requests).

X. The AIC Does Not Believe that the Cash Solicitation Rule Should be Extended to Persons Referring Investors to Private Funds.

The AIC does not believe that the Cash Solicitation Rule should be expanded to cover the solicitation of investors in private funds. The Proposing Release states that it is expanding the coverage of the Rule because it “would increase protections to such investors primarily by making them aware of a solicitor’s financial interest in the investor’s investment in a private fund and prohibiting the use of disqualified solicitors under the proposed rule.”⁵³ The Proposing Release also states that investors in private funds “may not be aware that the person engaging in the solicitation activity may be compensated by the adviser” and the related conflicts.⁵⁴

The AIC respectfully disagrees with these premises. First, if the person engaging in the solicitation is a registered broker dealer, it will be subject to a regulatory framework that assures that its financial interest in the offering will be known to investors. Similarly, if the person engaging in the solicitation is an employee of the fund sponsor, investors will understand that the employee has an interest in the success of the offering. We also note that the vast majority of private fund offerings are conducted under Rule 506 of Regulation D and, therefore, the solicitors and placement agents (among others) are subject to the disqualification provisions of Rule 506(d) of Regulation D. Therefore, we do not believe that the expansion of the Cash Solicitation Rule in this fashion is necessary to accomplish the SEC’s objectives; they are already accomplished. Finally, the additional unnecessary layer of regulation would (i) require an unnecessary separate disclosure when disclosure within the PPM or other offering document would be more efficient, and (ii) create unnecessary complications with respect to private fund offerings reliant on Regulation S to non-U.S. persons utilizing non-U.S. placement agents who may not be familiar with U.S. federal securities laws and may be unwilling to provide the necessary representations.

⁵² Proposing Release at pp. 195 – 196.

⁵³ Proposing Release at p. 210.

⁵⁴ Proposing Release at p. 210.

AMERICAN INVESTMENT COUNCIL

The AIC appreciates the opportunity to comment on the Proposal and would be pleased to answer any questions that you might have concerning our comments.

Respectfully submitted,

A handwritten signature in blue ink that reads "Jason Mulvihill". The signature is written in a cursive, flowing style.

Jason Mulvihill
Chief Operating Officer & General Counsel
American Investment Council