SEC Marketing Rule vs. GIPS Standards

This matrix details considerations for advertising performance under the SEC Marketing Rule and compares the requirements to those of the Global Investment Performance Standards (GIPS®). Firms that claim compliance with the GIPS standards are likely ahead of the curve when it comes to complying with the Marketing Rule, but they may still need to review and consider amendments to their GIPS compliance policies and procedures as well as their GIPS Reports in light of the new regulatory requirements. Firms that do not currently adhere to the GIPS standards will likely have an additional workload in order to meet the requirements of the Marketing Rule beyond that which is outlined here.

SEC Marketing Rule	GIPS Standards	Solution
Composite Construction and Related Performance		
When presenting performance of a strategy, show related performance either on a portfolio-by-portfolio basis or as a composite of all related portfolios. May exclude a related portfolio if (a) performance is not materially higher than if all related portfolios had been included, and (b) the exclusion of any related portfolio does not alter the presentation of performance for the prescribed time periods.	When presenting performance of a strategy, composite performance must be used. All portfolios that meet the defined composite criteria must be included in the composite.	Advisers may rely on the GIPS standards when constructing composites of related portfolios. Therefore, no impact on GIPS-compliant firms. Advisers that do not follow the GIPS standards and/or have not constructed composites should likely look to do so in order to meet the requirements of the Marketing Rule.
Proprietary and Seed Capital Portfolios		
An adviser must invest an amount of seed capital that is sufficient to demonstrate the strategy to investors; otherwise, the advertisement would be considered hypothetical performance and subject to such additional requirements.	No requirements specifically addressing the inclusion of proprietary or seed capital portfolios in composite. Proprietary and seed capital portfolios may be included in a composite, if they are managed consistent with the composite's investment mandate, objective, or strategy.	GIPS-compliant firms will need to ensure that seed capital accounts are of sufficient size for the strategy. If not, they will need to be excluded from the composite and the composite will need to be restated.

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Non-Fee-Paying Portfolios		
Firms are not allowed to exclude related portfolios from an advertisement based on the fees a portfolio pays or does not pay. Net returns for non-fee-paying portfolios should reflect the deduction of a model fee.	Firms have the option to exclude non-fee-paying portfolios from composites. Alternatively, composites may include non-fee-paying portfolios, with appropriate disclosure. Net returns for non-fee-paying portfolios may reflect the deduction of actual investment management fees, which may be $0.	If non-fee-paying portfolios have been excluded from composites, the firm will need to amend their composite membership policies to require their inclusion. Revising historical composite membership and restating performance might be necessary. GIPS-compliant firms should apply model fees to any non-fee-paying portfolios when calculating composite net returns. A model fee should also be applied to any non-fee-paying assets in calculating a pooled fund's net returns.
Gross-of-Fees Performance		
Gross performance is performance 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. Gross performance is not explicitly required to reflect the deduction of transaction costs. If transaction costs have not been deducted, this should be disclosed.	Gross-of-fees returns must reflect the deduction of transaction costs. Pure gross returns that have not been reduced by transaction costs may be included as supplemental information.	GIPS-compliant firms are not impacted, as GIPS-compliant net performance should be at least as conservative as required by the Marketing Rule. Note that GIPS-compliant performance will reflect the deduction of transaction costs while SEC-compliant presentations may not, so long as the results are accompanied by appropriate disclosure.
Net-of-Fees Performance		
Net performance must reflect 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	Net-of-fees returns must reflect the deduction of management fees and transaction costs, but not custody fees. Must also reflect the	GIPS-compliant firms may have to adjust net returns to deduct any custody fees the client pays to the adviser. Revising historical

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investment advisory services to the relevant portfolio, including advisory fees, any advisory fees paid to underlying investment vehicles, and custody fees if paid to the adviser.	deduction of fees and expenses paid to underlying funds.	calculations and restating performance might be necessary.
Pooled Fund Net Performance		
See above. No separate definition of net performance for pooled funds.	Net performance included in a GIPS Pooled Fund Report must reflect the deduction of all fees and expenses incurred by the fund, including investment management fees, administrative fees, transaction costs, and all other fees and expenses. Must also reflect the deduction of fees and expenses paid to underlying funds.	GIPS-compliant firms are not impacted, as GIPS-compliant net performance should be at least as conservative as required by the Marketing Rule.
Presentation of Gross-of and Net-of-Fees Returns		
Net returns must be presented; if gross returns are presented, net returns must be presented with equal prominence, in a format designed to facilitate comparison, calculated using the same methodology, and calculated for the same time periods.	May present only gross returns, only net returns, or both. Wrap fee composites must present net returns that reflect the deduction of the entire fee that a prospect would pay.	GIPS-complaint firms must ensure that GIPS Reports used as advertisements include net returns. If gross returns are also presented, the gross and net returns must be presented for the same periods, shown with equal prominence, and in a format designed to facilitate comparison.
Model Fees		
Net returns using a model fee must: (1) be no higher than if actual fees had been deducted, or (2) reflect the deduction of the highest fee relevant to the intended audience.	When using a model fee to calculate net-of-fees returns, the model fee must be appropriate to prospective clients. Additionally, net returns calculated using a model fee must be equal to or lower than if actual fees were	GIPS-compliant firms must consider the intended audience of the presentation to make sure the model fee applied is appropriate. For example, if the highest fee charged historically was applied to calculate

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	used. Net returns not meeting these requirements may be presented as supplemental information in a GIPS Report.	net returns and the firm starts to offer the strategy to a different market segment and the fees for the service are now higher than those that were charged historically, the firm will need to revise historical calculations and restate net returns to apply a model fee that reflects the fees offered to prospective clients currently.
Actual Fees		
Net returns calculated using actual management fees are generally acceptable. However, if the fee to be charged to the intended audience is anticipated to be higher than the actual fees charged (for example, if non-fee-paying portfolios were included in the composite historically), the firm must use a model fee that reflects the anticipated fee to be charged in order not to violate the Marketing Rule's general prohibitions.	Net returns using actual fees are acceptable under the GIPS standards.	GIPS-compliant firms who calculate net returns using actual fees must confirm that the results are representative of the fees offered to the intended audience of the performance presentation. If the firm has provided clients with significant fee breaks and the actual fees used to calculate performance are found to be considerably lower than the management fees offered to current prospects, then recalculating historical net returns to apply a model fee that represents the fees offered to the intended audience might be necessary.
Calculation Methodology		
Advisers may use any return calculation methodology, provided that it does not violate the general prohibitions of the Marketing Rule.	Generally, the GIPS standards require time-weighted return, but allow for money-weighted returns in certain circumstances.	No impact on GIPS-compliant firms.

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Required Time Periods & Return Types		
Must present 1-, 5-, and 10-year net-of-fees returns (or for life of portfolio) through the most recent calendar year-end. There are no prescribed time periods for private fund performance. The presentation of benchmark results is not explicitly required.	Annual time periods required for time-weighted returns. A single since-inception annualized return is required for money-weighted returns. The GIPS standards recommend presenting both gross-of-fees and net-of-fees returns. Benchmark returns must be presented for the same time periods as composite or pooled fund returns.	Assuming a GIPS Report is a standalone advertisement, the GIPS Report will need to be updated to include 1-, 5-, and 10-year net-of-fees returns (or since inception) and must include benchmark returns for the same periods. Private funds (and, as an extension, composites that are comprised solely of private funds) are exempt from this requirement. However, under the GIPS standards, firms may elect to present money-weighted returns for composites that consist of portfolios other than private funds. If doing so, presenting a single since-inception money-weighted return would not be sufficient and would need to be accompanied by 1-, 5-, and 10-years, if applicable.
Track Record Length		
Requires a 10-year track record (or since inception) in order to present the prescribed time periods. Private funds are exempt.	When initially attaining GIPS compliance, firms must present at least 5 years of performance (or since inception if <5 years) and build up to a 10-year performance track record.	GIPS-compliant firms that claim compliance for less than 10 years may need to present performance that links non-GIPS compliant performance to GIPS-compliant performance by: (1) including linked performance in the GIPS Report and disclosing the conflict between the GIPS standards and the Marketing Rule or (2) including linked performance in materials that are part of the advertisement but outside of the GIPS Report.

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Timeliness of Returns		
Returns must be no less recent than the most recent calendar year-end, but may need to be more recent to comply with the general prohibitions. The prescribed time periods are also expected to be updated within 30 days of year-end.	GIPS Reports for composites and pooled funds that present time-weighted returns must include annual periods but may also include year-to-date returns. Reports must include the most recent annual period within 12 months of the period end.	If GIPS Reports are used as a standalone advertisement, they should be updated within 30 days of calendar year-end with the required prescribed time periods (1-, 5-, and 10-year returns) and performance may also need to be updated mid-year to comply with the general prohibitions of the Marketing Rule.
Hypothetical/Theoretical Performance		
Defined as performance results that were not actually achieved by any portfolio of the adviser, including model performance, backtested performance, and targeted or projected returns. The presentation of hypothetical performance must be limited to investors who have access to the resources to independently analyze this information and who have expertise to understand the risks and limitations. Advisers must adopt policies and procedures reasonably designed to ensure that hypothetical performance information is relevant to the likely financial situation and investment objectives of the advertisement's intended audience.	Total firm assets, composite assets, and pooled fund assets must include only actual assets managed by the firm (i.e., must exclude hypothetical assets and performance). Hypothetical/theoretical performance cannot be linked to actual performance. Hypothetical performance can be presented separate from GIPS-compliant performance. The GIPS standards do not outline conditions on who can receive hypothetical performance.	All advisers, including GIPS-complaint firms, must adopt policies and procedures to determine who can receive hypothetical/ theoretical performance. Information that may not have been considered hypothetical performance in the past, such as target returns, must be treated as such going forward.

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Carve-Outs/Extracted Performance		
Extracted performance is the performance results of a subset of investments extracted from a single portfolio. Advisers may present extracted performance, as long as the advertisement provides, or offers to provide promptly, the performance results of the total portfolio from which the performance was extracted. A composite of extracts is not subject to the same requirements as extracts from a single portfolio. Instead, composites of extracts must be treated as hypothetical performance. Does not require the allocation of cash to extracts.	A carve-out is a portion of a portfolio that is, by itself, representative of a distinct investment strategy. It may be used as a track record for a narrower mandate from a multiple-strategy portfolio managed to a broader mandate. The GIPS standards do not address the presentation of extracts from single portfolios. They are only addressed in the context of composites. GIPS-compliant firms are not required to present performance of the total portfolio that the carve-out is taken from. However, GIPS-compliant firms are required to create and present performance for separate composites of standalone portfolios managed to the strategy. Carve-out returns must include cash, either accounted for separately or allocated synthetically.	GIPS-compliant firms do not need to make any changes to their carve-out calculation policies and procedures. However, GIPS-compliant firms will need to treat carve-out composite performance in the same manner as hypothetical performance and limit its distribution to investors who have the resources and financial expertise to assess the information. Due to this, carve-out composite performance will typically not be appropriate to include in broad-use advertisements; rather, composites of standalone portfolios will need to be presented.
Predecessor Performance/Portability		
Portability requires an ongoing assessment. If portability tests are no longer met (e.g., person(s) primarily responsible for predecessor performance leaves), the ported performance may no longer be used. Composites may exclude portfolios from prior firm if results are not materially higher	Portability is viewed as a point-in-time event. If portability tests are met, prior firm performance becomes performance of the new or acquiring firm. Composite performance must include all accounts managed to the strategy at the prior firm. Ongoing assessment of the portability tests is not needed.	Firms will have to discontinue showing predecessor performance if portability tests are no longer met after the acquisition, merger or transaction date. Firms will need to adopt ongoing policies to monitor for personnel departures and revise track record inception dates accordingly.

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and doing so does not change performance for the prescribed time periods.		

This matrix is prepared solely for educational purposes. It is not legal or professional advice. Readers must not rely on it to provide such advice, either generally or with respect to a particular question or issue. You should reference this overview in conjunction with applicable regulatory rules and regulations.

About GUARDIAN PERFORMANCE SOLUTIONS

Guardian Performance Solutions LLC is a specialty compliance consulting firm dedicated to assisting advisers to achieve and maintain compliance with the Global Investment Performance Standards (GIPS®) and create compliant performance advertisements. We help investment advisers achieve their goals of marketing their services and growing their business, while also meeting their regulatory obligations and adhering to industry accepted standards and best practices. Because we don't provide verification services, we are free from independence concerns and can take a hands-on approach to developing and managing an adviser's performance advertising compliance program, which can include constructing composites, calculating and validating performance results, creating materials, and writing policies and procedures. Additional information can be found at www.GuardianPerformanceSolutions.com.

About Focus 1 Associates

Focus 1 Associates LLC specializes in assisting registered investment advisers—institutional, wealth advisers, family offices, and advisers to private funds—with their compliance needs under Rule 206(4)-7 of the Investment Advisers Act of 1940. Our RIA compliance services are built on a quality control process that affords complete confidence in your compliance program. Most of our services include unlimited consulting and tangible tools, such as templates and sample documents to help your firm get a jump start on meeting SEC compliance rules and regulations. Our team of experienced SEC Compliance Consultants is committed to delivering practical, solutions-oriented assistance, such as providing a framework and associated workflow that we help the chief compliance officer put in place to support the firm's SEC compliance program. Additional information can be found at www. Focus1Associates.com.