

November 4th is approaching; Are You Ready for the SEC's New Marketing Rule?



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In December 2020, the U.S. Securities and Exchange Commission (the “SEC”) adopted amendments under the Investment Advisers Act of 1940 (the “Advisers Act”) to update rules that govern investment adviser marketing¹. These amendments create a single merged rule, Rule 206 (4)-1 under the Advisers Act, (the “Marketing Rule”) that combines and replaces both the current “Advertising Rule” (Rule 206 (4)-1) and “Cash Solicitation Rule” (Rule 206(4)-3), related to compensation for the use of solicitors and placement agents. The new Marketing Rule represents a substantial overhaul of the existing landscape, as neither the Advertising Rule nor the Cash Solicitation Rule has been amended significantly since their adoption over forty years ago². The new Marketing Rule is poised to have a substantial, but not yet fully understood impact on the manner in which investment advisers promote themselves.

The new Marketing Rule is designed to comprehensively and efficiently regulate advisers’ marketing communications. In addition to adopting the unified Marketing Rule, the SEC has also made related amendments to Rule 204-2 under the Advisers Act, the “Books and Records Rule” and to Form ADV.

- Form ADV will now require advisers to provide additional information about the advisers’ marketing practices, including specific information about the use of performance, prior recommendations, testimonials, endorsements, and third-party rankings advertising, and whether the adviser provides compensation in connection with the use of testimonials, endorsements or third-party ratings.
- Under the amendments to the Books and Records Rule, advisers will be required, among other things, to archive and maintain records of all advertisements that the adviser has circulated, which under the new Marketing Rule, will encompass email, websites, social media profiles and an ever-expanding list of platforms.

We note however that neither of these related amendments are discussed at length in this bulletin.

¹ [SEC Adopts Modernized Marketing Rule for Investment Advisers](#) (December 22, 2020).

² [Marketing Rule Adopting Release, No. IA-5653](#), page 6 (December 22, 2020).

The November 4th Compliance Deadline

The Marketing Rule became effective on May 4, 2021, with an 18-month implementation period. Phased-in compliance is not an option for advisers, as compliance is an “all or nothing” proposition. The Marketing Rule requires full compliance by **November 4, 2022**.

The Advisers and Firms Affected

The Marketing Rule on its face applies only to registered investment advisers (RIAs). The Marketing Rule was issued pursuant to the anti-fraud provisions of the Advisers Act in Section 206, which are applicable to “any investment adviser”, including, for example, exempt reporting advisers (ERAs). For ERAs, then, the Marketing Rule provides a set of best practices to align advertising materials and fundraising practices with the anti-fraud rules. **Why The SEC Adopted the Marketing Rule Now**

Since the adoption of the Advertising Rule and Cash Solicitation Rule in the early 1960s and late 1970s, an era that predated the internet and personal computers, advertising and referral practices have evolved. Simultaneously, the technology used for these communications has advanced, the nature and profiles of the advisers in the investment advisory industry have diversified and the expectations and types of investors shopping for advisory services have changed. For example, the use of the internet, mobile applications, and social media has become an integral part of business communications. As such, investors have come to rely on these forms of communication to obtain information, including reviews and referrals, when considering which advising services to elect.

Similarly, advisers and third parties also rely on these same types of digital outlets to attract and refer potential customers. Private funds and their advisers often hire promoters to obtain investors in the funds. Many promoters and referral practices have expanded to include, for example, various types of compensation, including non-cash compensation, in referral arrangements.

Accordingly, the SEC has found that the old rules are now out of touch with the landscape that they govern. The Marketing Rule seeks to recognize these developments and to reflect modern habits by utilizing principles-based provisions instead of *per se* prohibitions³. This bulletin highlights several key changes to the advertising and solicitation practices and requirements of investment advisers imposed by the new Marketing Rule.

The Marketing Rule’s Impact on Advertisements and Solicitations

Overview

Advisers routinely use advertisements to provide investors with useful information as they contemplate whether to utilize that adviser’s investment advisory services. The amendments to the Advertising Rule: (i) modify the definition of “advertisement” to be more evergreen in light of ever-changing technology; (ii) replace four *per se* prohibitions with a set of seven more general principle-based prohibitions on certain advertising practices applicable to all advertisements; (iii) provide certain restrictions and conditions on testimonials, endorsements, and third-party ratings; and (iv) include tailored requirements for the presentation of performance results, based on an advertisement’s intended audience⁴. The amendments to the Cash Solicitation Rule: (i) expand the rule to cover solicitation arrangements involving all forms of compensation, rather than only cash compensation; (ii) expand the rule to apply to the solicitation of current and prospective investors in any private fund, rather than only to “clients” (including prospective clients) of the investment adviser; (iii) eliminate requirements duplicative of other rules; (iv)

³ [Marketing Rule Adopting Release, No. IA-5653](#), page 7 (December 22, 2020).

⁴ [Marketing Rule Adopting Release, No. IA-5653](#), page 9 (December 22, 2020).

include exceptions for de minimis payments and certain non-profit programs; and (v) expand the types of disciplinary events that would trigger the rule's disqualification provisions⁵.

Definition of Advertisement. Among other revisions, the new Marketing Rule deletes references in the current Advertising Rule to specific types of communications to ensure that modern communication methods are captured within the rule, rather than the methods that were most common when the SEC adopted the current rule (e.g., newspapers, television, and radio). An "advertisement" now includes any direct or indirect communication an investment advisor makes that (i) offers its services regarding securities to existing or prospective clients, or (ii) includes any endorsement or testimonial for which an advisor provides cash or noncash compensation. Accordingly, the Marketing Rule now also applies to electronic communications, such that digital platforms like websites, email, instant messaging platforms, etc. will find themselves under regulatory scrutiny. The second prong of the expanded definition means that a variety of communications including endorsements and testimonials, which may be presented on various digital or social media platforms will also be subject to certain disclosure requirements. These revisions will expand the scope of the current rule to encompass all offers of an investment adviser's investment advisory services with regard to securities regardless of how they are disseminated, with limited exceptions⁶.

General Prohibitions. The Marketing Rule sets forth certain general prohibitions governing how information is presented. As the prohibitions are principle-based and are not per se prohibitions, advisers will have to analyze the particular facts and circumstances of each advertisement, including the nature of the audience to which the advertisement is directed. Information presented in an advertisement cannot:

- Include untrue statements and omissions
- Include unsubstantiated material statements of fact
- Include untrue or misleading implications or inferences
- Fail to provide fair and balanced treatment of material risks or material limitations
- Fail to present specific investment advice in a fair and balanced manner
- Cherry-pick performance results or otherwise present performance in a manner that is not fair and balanced
- Be materially misleading

Testimonials and Endorsements. The Marketing Rule eliminates the long-standing prohibition on the use of testimonials and endorsements and permits their use if the adviser satisfies certain disclosure, written agreement, oversight and in certain cases, disqualification provisions. For example, advisers will be required to disclose the identity of the person providing the testimonial, the reason for promoting the adviser, whether there are any conflicts of interest, and if the referring person is being compensated, appropriate disclosures of the compensation arrangement. There are also certain exemptions for arrangements involving *de minimis* compensation, affiliated personnel, registered broker-dealers, and certain persons to the extent they are covered by Rule 506(d) of Regulation D under the Securities Act with respect to a securities offering.

Third-Party Ratings. The Marketing Rule prohibits the use of third-party ratings unless the adviser provides certain disclosures and satisfies specified criteria pertaining to the preparation of the rating. The adviser is required to have a reasonable basis for believing that any questionnaire or survey used in the preparation of the third-party rating is fair and the underlying questionnaire or survey must also be structured to make it equally easy for a participant to provide favorable and unfavorable responses. The advertisement referencing a third-party rating must clearly and prominently disclose (or the investment adviser must reasonably believe that such rating itself clearly and prominently discloses): (i) the date on which the rating was given and the period of time upon which the rating was based, (ii) the identity of the third party that created and tabulated the rating, and (iii) if applicable, that

⁵ [Id](#) at page 10.

⁶ [Marketing Rule Adopting Release, No. IA-5653](#), page 17 (December 22, 2020).

compensation has been provided directly or indirectly by the adviser in connection with obtaining or using the third-party rating.

Performance Information Generally. Certain types of performance information will require new, updated or enhanced disclosures. In this context, the Marketing Rule sets forth specific conditions for presenting performance information relating to (i) gross and net performance, (ii) standard and prescribed time periods, (iii) statements about SEC approval, (iv) selective related and past performance, (v) hypothetical performance, and (vi) predecessor performance.

- **Gross Performance.** Gross performance may not be used unless the advertisement also presents net performance with equal prominence.
- **Standard Prescribed Periods.** Performance information must include one-, five-, and ten-year (or shorter applicable life of the portfolio) period. Private funds are exempted because performance results from their early years, when their capital is still being deployed, may not be meaningful for investors.
- **Statements about SEC Approval.** The adviser must not state or suggest that the SEC has reviewed or approved the performance information.
- **Selective Related or Past Performance.** The Marketing Rule prohibits the use of selective past performance. Subject to limited exceptions, advisers must list performance results from all portfolios with investment policies, objectives, and strategies that are substantially similar to the portfolio being offered in the advertisement.
- **Hypothetical Performance.** Hypothetical performance (which includes target performance and projected performance), should not be listed unless the adviser adopts and implements compliance policies and procedures reasonably designed to ensure that the performance is relevant to the likely financial situation and investment objectives of the intended audience and the adviser provides certain additional information.
- **Predecessor Performance.** Predecessor performance may only be used if (i) the personnel primarily responsible for achieving the prior performance manages accounts at the advertising adviser, (ii) the accounts that were managed by personnel at the predecessor adviser are sufficiently similar to the accounts that they manage at the advertising adviser, and (iii) all accounts that were managed in a substantially similar manner are advertised, unless the exclusion of any such account would not result in materially higher performance and the exclusion of any account does not change the presentation of any applicable time periods. In addition, the advertisement must include all relevant disclosures clearly and prominently, including that the performance results were from accounts managed at another entity.

SEC Examination Priorities for the New Marketing Rule

Any advertisements disseminated on or after November 4, 2022 by advisers registered or required to be registered with the SEC, are subject to the Marketing Rule. The SEC, in a risk alert published last month, titled, "[Examinations Focused on the New Investment Adviser Marketing Rule](#)" announced that it intends to begin investigations and enforcement of the new Marketing Rule. In that alert, it highlighted certain areas through which its staff will conduct a number of specific national initiatives, as well as a broad review through the examination process, for compliance with the Marketing Rule. These areas include, but are not limited to:

- **Marketing Rule Policies and Procedures.** The staff expects to review whether investment advisers have adopted and implemented written policies and procedures that are reasonably designed to prevent violations by the advisers and their supervised persons of the Advisers Act, including the Marketing Rule⁷.

⁷ [Examinations Focused on the New Investment Adviser Marketing Rule, Risk Alert, the U.S. Securities and Exchange Commission, Division of Examinations](#) (September 19, 2022).

These reviews could be achieved through conducting internal pre-review and approval of advertisements, reviewing a sample of advertisements based on risk, or pre-approving templates.

- **Substantiation Requirement.** The staff will review whether investment advisers have a reasonable basis for believing they will be able to substantiate material statements of fact in advertisements. An adviser could demonstrate such a belief by making a record contemporaneous with the advertisement demonstrating the basis for their belief. An adviser might also choose to implement policies and procedures to address how this requirement is met. However, if an adviser is unable to substantiate the material claims of fact made in an advertisement when the SEC demands it, the SEC will presume that the adviser did not have a reasonable basis for its belief⁸.
- **Performance Advertising Requirements.** The staff will review whether investment advisers are compliant with the performance advertising requirements in the Marketing Rule.
- **Books and Records; Form ADV.** The staff will also be reviewing for compliance with the new books and records requirements set forth in Rule 204-2. In addition, the SEC will be checking on advisers' annual Form ADV amendment to ensure that advisers are providing the additional information regarding their marketing practices, as required by the amended rules.

Ensuring Compliance.

We anticipate regulatory scrutiny and follow-up enforcement actions related to advisers' compliance with the new Marketing Rule. Following an 18-month implementation period, we do not anticipate much leniency from the SEC following November 4th. The SEC has withdrawn or modified a significant number of No-Action Letters issued under the previous Advertising Rule and Cash Solicitation Rule⁹ and is maintaining a list of Marketing Compliance Frequently Asked Questions¹⁰ to inform advisers' implementation of the new Marketing Rule. Firms and investment advisers will no longer be able to rely on the provisions of any withdrawn letters and will need to ensure compliance by November 4th¹¹.

Firms and advisers should consider whether they need to update or revise their marketing materials, written policies, procedures and systems to ensure they are reasonably designed to prevent violations of the Marketing Rule by the advisers and their supervised persons. In addition, as the Books and Records Rule, as amended, will require investment advisers to make and keep certain records, such as records of all advertisements they disseminate¹², advisers may need to update their firm's policies and retention systems to incorporate these added requirements.

⁸ [Marketing Rule Adopting Release, No. IA-5653](#), page 71 (December 22, 2020).

⁹ [Division of Investment Management Staff Statement Regarding Withdrawal and Modification of Staff Letters Related to Rule Making on Investment Advisers Marketing, Information Update, U.S. Securities and Exchange Commission](#) (October 2021).

¹⁰ [SEC Marketing Compliance Frequently Asked Questions](#) (April 14, 2021).

¹¹ [Id.](#)

¹² [Examinations Focused on the New Investment Adviser Marketing Rule, Risk Alert, the U.S. Securities and Exchange Commission, Division of Examinations](#) (September 19, 2022).