

CLIENT ALERT

SEC Division of Examinations Issues Risk Alert on Initial Observations Regarding Advisers Act Marketing Rule Compliance

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AUTHORS

**Adam S. Aderton | Benjamin B. Allensworth | James E. Anderson | Brian Baltz
Justin L. Browder | Anne C. Choe | Michelle Tekin**

On April 17, 2024, the Division of Examinations (the “Division”) of the U.S. Securities and Exchange Commission (the “SEC”) issued a risk alert highlighting observations of the Division staff (the “Staff”) regarding registered investment advisers’ compliance with Rule 206(4)-1 (the “Marketing Rule”) under the Investment Advisers Act of 1940, as amended (the “Advisers Act”).¹ The Staff has announced that assessments of whether advisers are in compliance with the Marketing Rule would be one of the Division’s examinations priorities.² Notably, the risk alert was released after a second set of SEC enforcement actions against investment advisers related to Marketing Rule compliance.³

¹ *Initial Observations Regarding Advisers Act Marketing Rule Compliance*, Division of Examinations (Apr. 17, 2024), available [here](#).

² See *2023 Examination Priorities*, Division of Examinations 2024 (Feb. 27, 2023), available [here](#); see also *2024 Examination Priorities*, Division of Examinations (Oct. 16, 2023), available [here](#). For a discussion on the *2024 Examination Priorities*, please see the Willkie Farr & Gallagher LLP Client Alert, available [here](#).

³ On September 11, 2023, the SEC announced charges against nine registered investment advisers for advertising hypothetical performance to the general public on their websites without adopting and/or implementing policies and procedures required by the Marketing Rule. *SEC Sweep Into Marketing Rule Violations Results in Charges Against Nine Investment Advisers*, SEC Press Release (Sept. 11, 2023), available [here](#). On April 12, 2024, the SEC announced charges against five registered investment advisers for advertising hypothetical performance to the general public, making false and misleading statements in advertisements, advertising misleading model performance, being unable to substantiate performance shown in its advertisements, failing to enter into written agreements with individuals that were compensated for endorsements, and committing recordkeeping and compliance violations required by the Marketing Rule. *SEC Charges Five Investment Advisers for Marketing Rule Violations*, SEC Press Release (Apr. 12, 2024), available [here](#).

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The risk alert provides guidance highlighting the issues that the Staff has focused on in its examinations, as well as various deficiencies the Staff has observed in examinations, including failures to adopt and implement appropriate written policies designed to prevent violations of the Marketing Rule, advertisements that failed to comply with the general prohibitions in the Marketing Rule, and books and records and Form ADV deficiencies related to the Marketing Rule.

A. Observations Regarding Compliance Rule, Books and Records Rule and Form ADV

Compliance Rule

The Staff observed that, typically, (1) advisers' compliance policies and procedures included processes to comply with the Marketing Rule, and (2) advisers provided training for relevant staff on the Marketing Rule requirements and the advisers' marketing policies and procedures. The Staff observed that, generally, advisers that updated their written marketing-related policies and procedures established a process for reviewing advertisements, which in many instances required preapproval of advertisements before dissemination.

The Staff also observed instances where advisers' policies and procedures were not reasonably designed or implemented to address compliance with the Marketing Rule, which resulted in gaps for preventing violations of the Marketing Rule, Rule 204-2 (the "Books and Records Rule"), or both. For example, the Staff observed policies and procedures that it deemed deficient because they:

- Consisted only of general descriptions and expectations related to the Marketing Rule.
- Did not address applicable marketing channels utilized by the advisers, such as websites and social media.
- Were informal rather than in writing.
- Were incomplete, not updated, or partially updated for certain applicable marketing topics.
- Were not tailored to address advisers' specific advertisements (e.g., policies and procedures to address the general prohibitions in the Marketing Rule, and advertising requirements for testimonials, endorsements, and third-party ratings utilized by advisers in advertisements).
- Did not adequately address the preservation and maintenance of advertisements and related documents, such as copies of any questionnaires or surveys used in the preparation of a third-party rating (in the event the adviser has received such documents) included or appearing in any advertisement.
- Were updated to reflect the Marketing Rule but were not implemented. For example, the Staff observed advisers' policies that required net of fees performance to be included with any performance advertisement; however, the Staff observed those same advisers including only gross performance in advertisements.

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Books and Records Rule

The Staff observed that advisers typically had updated their policies and procedures to reflect Marketing Rule-related books and records maintenance and preservation requirements. Nonetheless, the Staff observed Marketing Rule-related books and records deficiencies, including:

- Advisers completed questionnaires or surveys used in the preparation of a third-party rating but did not maintain a copy of such questionnaires.
- Advisers did not maintain copies of information posted to social media.
- Advisers did not maintain documentation to support performance claims included in advertisements.

Observations Related to Form ADV

The Staff observed that many advisers had updated their Form ADVs including: (1) Part 1A, Item 5.L related to advertising; and (2) Part 2A, Item 14 brochure disclosures related to advertising (Client Referrals and Other Compensation).

The Staff observed deficiencies related to the Marketing Rule on Form ADV, including instances where advisers inaccurately reported on Form ADV, Part 1A, that their advertisements did not include:

- Third-party ratings, when their websites included third-party ratings or social media posts that touted the firms as being ranked in certain third-party ratings.
- Performance results, when performance results were included in their marketing materials.
- Hypothetical performance, when hypothetical performance was included in advertisements.

The Staff also observed that adviser Form ADVs included outdated references to the prior Cash Solicitation Rule (Advisers Act Rule 206(4)-3), inaccurately indicated that no referral arrangements existed, and omitted material terms and compensation of referral arrangements on Form ADV, Part 2A, Item 14.

B. Observations Regarding Compliance with the Marketing Rule's General Prohibitions

In their review of Marketing Rule compliance, the Staff assessed whether advisers violated any of the Marketing Rule's general prohibitions, highlighting a focus on advisers:

- Including an untrue statement of a material fact or omitting a material fact necessary to make the statement made, in light of the circumstances under which it was made, not misleading.

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- Including a material statement of fact that the adviser does not have a reasonable basis for believing it will be able to substantiate upon demand by the Commission.
- Including information that would reasonably be likely to cause an untrue or misleading implication or inference to be drawn concerning a material fact relating to the adviser.
- Discussing any potential benefits to clients or investors connected with or resulting from the adviser's services or methods of operation without providing fair and balanced treatment of any associated material risks or limitations.
- Referencing specific investment advice provided by the adviser in a manner that is not fair and balanced.
- Including or excluding performance results, or presenting performance time periods, in a manner that is not fair and balanced.
- Providing information that is otherwise materially misleading.

Observations Related to the Marketing Rule's General Prohibitions

The Staff observed the following deficiencies related to the Marketing Rule's general prohibitions:

- The Staff observed advertisements that included untrue statements of material facts, including:
 - stating that the advisers were "free of all conflicts," when actual conflicts existed.
 - stating material facts about the advisers' businesses that were inaccurate, including:
 - statements that a network of personnel perform advisory services for clients when a sole individual performs such services; and
 - statements representing erroneous adviser personnel qualifications, such as their education, experience, and professional designations.
 - describing material facts about advisory services or products offered that were inaccurate, including:
 - referencing certain investment mandates of the advisers in advertisements when there were no such mandates used by the firms (e.g., ESG mandates);
 - claiming that investment processes were validated by professional institutions when they were not;

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- stating that the adviser considered certain risk tolerances when recommending investment strategies when all clients were placed into the same strategy without consideration of risk tolerances;
 - referencing a list of approved securities that did not exist;
 - referencing formalized securities screening processes that did not exist; and
 - misrepresenting the advisers' client base, such as describing the adviser as a "private fund adviser" when the firm did not advise any private funds.
- publicizing the receipt of certain awards or accolades that were not received.
- The Staff observed advertisements that omitted material facts necessary to make statements not misleading or that included information that could have reasonably caused untrue or misleading implications or inferences to be drawn concerning material facts relating to the advisers, for example:
 - statements that advisers were different from other advisers because they acted in the "best interest of clients," without disclosing that all investment advisers have a fiduciary duty to act in their clients' best interests.
 - recommending certain investments (e.g., on podcasts or websites) without disclosing the conflicts of interest attributed to the compensation paid to or received by the advisers for such recommendations.
 - untrue or misleading claims, such as:
 - stating that the advisers were "seen on" national media, implying appearances in national news media, without disclosing that the "appearances" were in fact paid advertisements; and
 - advertising images of celebrities in marketing materials in a manner that implied the celebrities endorsed the firms when such celebrities did not endorse the firms.
 - untrue or misleading performance claims, including:
 - advertising cumulative profits that the advisers believed were not achievable or were impossible to achieve without unlimited money to invest;
 - presenting performance information that did not provide adequate disclosure regarding the share classes included in the performance returns;

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- using lower fees in calculations for net of fees performance returns than were offered to the intended audience; and
- omitting material information regarding fees and expenses used in calculating returns.
- citing SEC registration beyond factual statements as to advisers' registration status in a way to imply that SEC registration was representative of a particular level of skill or ability, or that the SEC had either approved or passed upon the advisers' business practices. The Staff also observed advisers including the SEC logo on their websites with the purpose of implying that the websites or the advisers had been approved or endorsed by the SEC.
- including third-party ratings:
 - implying the advisers were the sole top recipients of certain awards when the awards went to multiple recipients or the advisers were not the top recipients; and
 - indicating that the advisers were highly rated by various organizations without disclosing that the methodologies for such ratings were based primarily or solely on factors that were not related to the quality of investment advice, such as assets under management, the number of clients, or that adviser personnel nominated fellow employees for such awards.
- including testimonials that were misleading. For example, advisers included testimonials from clients of a third-party product on the advisers' websites without any disclosures explaining the context of the testimonials, implying that the testimonials were about the advisers' services rather than the third-party product.
- Performance advertisements contained information that was misleading, such as:
 - Benchmark index comparisons that did not define the index or provide sufficient context to enable an understanding of the basis for such comparison or disclose that the benchmark performance did not include reinvestment of dividends.
 - Performance presentations that contained: (1) outdated market data information only (e.g., market data from more than five years prior); or (2) investment products that were no longer available to clients and included lower investment costs than were available.

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- Statements or presentations regarding:
 - advisers' performance track record with securities that were not purchased by the advisers in a similar manner in their clients' accounts;
 - claims that the advisers achieved above average performance results without clarifying that the advisers did not yet have clients or performance track records; and
 - investment recommendations containing performance information that did not include disclosures to provide context to the presentations, such as advertising performance during time periods when most investors would have experienced the advertised performance returns because of general market performance.
- The Staff observed advertisements that included statements about the potential benefits connected with the advisers' services or methods of operation that did not provide fair and balanced treatment of material risks of limitations associated with the potential benefits.
- The Staff observed advertisements that included only the most profitable investments or specifically excluded certain investments without providing sufficient information and context to evaluate the rationale, such as investments that were written off as a loss or were lower performing investments. The Staff also observed advisers that had not established criteria in their policies and procedures to ensure references to specific investment advice shown in advertisements were provided in a fair and balanced manner.
- The Staff observed advertisements that included or excluded certain performance results or presented performance time periods in manners that were not fair and balanced, for example:
 - Advertisements that did not disclose the time period or did not disclose whether the returns were calculated for the same time period as additional performance information included in the same advertisement.
 - Advertisements that included or excluded certain performance results in manners that were not fair and balanced, such as advertisements that included the performance of only realized investment information in the total net return figure and excluded unrealized investments.
- The Staff observed advertisements that appeared to otherwise be materially misleading, including, presenting disclosures in an unreadable font on websites or in videos.

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C. Conclusion

The risk alert offers valuable insight into the specific issues that the Staff is reviewing with respect to investment advisers' practices, policies, and procedures under the Marketing Rule as well as common deficiencies identified by the Staff. In particular, registered investment advisers should take note of the breadth of deficiencies identified by the Staff, which include issues under the Marketing Rule's general prohibitions, issues related to quantitative metrics, including performance, and issues related to qualitative statements in advertising materials. Notably, the risk alert did not focus on deficiencies related to certain other requirements under the Marketing Rule, such as testimonials and endorsements, which suggests that the Division may focus on these other aspects of the marketing Rule in future examinations. Registered investment advisers should ensure they have adopted and implemented compliance policies and procedures reasonably designed to comply with all of the requirements under the Marketing Rule, the Books and Records Rule, and Form ADV disclosure obligations.

If you have any questions regarding this client alert, please contact the following attorneys or the Willkie attorney with whom you regularly work.

Adam S. Aderton

202 303 1224

aaderton@willkie.com

Benjamin B. Allensworth

202 303 1273

ballensworth@willkie.com

James E. Anderson

202 303 1114

janderson@willkie.com

Brian Baltz

202 303 1094

bbaltz@willkie.com

Justin L. Browder

202 303 1264

jbrowder@willkie.com

Anne C. Choe

202 303 1285

achoe@willkie.com

Michelle Tekin

202 303 1368

mtekin@willkie.com

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