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The SEC's New Marketing Rule – Practically Speaking: What Is an Advertisement?

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In December 2020, the Securities and Exchange Commission (SEC) finalized amendments to its advertising and solicitation rules under the Investment Advisers Act of 1940, as amended. Those finalized amendments merged the Advisers Act's current advertising rule (Rule 206(4)-1) with the cash solicitation rule (Rule 206(4)-3) under a new rule: Rule 206(4)-1, the Investment Adviser Marketing rule.

SEC-registered investment advisers (RIAs) must comply with the new marketing rule by November 4, 2022.

Commentary going back to December 2020 has explained what the new marketing rule says. But considerably less commentary has explained what, practically speaking, RIAs should be doing to ensure their marketing efforts, documents, systems, and procedures comply with the new marketing rule.

This is one of five "Practically Speaking" alerts providing succinct and practical high-level guidance from our attorneys regarding five aspects of the new marketing rule that we see as most impactful on RIAs' marketing efforts.

What Is an Advertisement?

Overview

As a threshold matter, the new marketing rule applies to communications that are "advertisements" under the rule. An advertisement under the rule is a communication that meets either of two tests (referred to as two "prongs" of the rule).

Prong 1

Under the first prong, a direct or indirect communication that an investment adviser makes to more than one person is an advertisement if it:

1. Offers the adviser's investment advisory services to prospective clients or investors in a private fund advised by the investment adviser, or
2. Offers new investment advisory services to current clients or private fund investors.

However, if a communication discusses hypothetical performance, the "to more than one person" limitation does

not apply, unless it is a one-on-one communication with the recipient private fund investor, or the communication is a response to an unsolicited request for information about hypothetical performance.

Also, a communication is not an advertisement under the first prong if it includes information contained in a required communication under a statute or regulation, if that information is "reasonably designed to satisfy the requirements of" what is required of that communication under the law.

In addition, "extemporaneous, live, oral communications" are not advertisements under the first prong.

Prong 2

Under the second prong, an endorsement or testimonial for which an investment adviser provides compensation, directly or indirectly, is an advertisement. Note, there is no one-on-one exception for Prong 2.

Endorsements and testimonials are covered in a separate alert.

As with the first prong, a communication is not an advertisement under the second prong if it includes information contained in a required communication under a statute or regulation, if that information is "reasonably designed to satisfy the requirements of" what is required of that communication under the law.

Practically Speaking, What Now?

Given the new marketing rule's two prongs for determining whether a communication is an advertisement, legal, compliance, and marketing personnel at RIAs that have not yet adopted the new rule should keep the following pointers in mind when reviewing (and revising) their pre-November 4, 2022 marketing materials for continued use in a compliant manner under the rule, and/or when creating new compliant materials:

1. When it comes to advertisements, the new marketing rule will not discriminate based on the medium of a particular communication. All forms of non-"extemporaneous, live, oral communications" – other than one-on-one communications that do not have performance data or testimonials or endorsements in them – should be reviewed to determine whether they are an advertisement under the rule.
2. Not all things that seem like "one-on-one communications" will be treated as such. Train your team on what a one-to-one communication is under the rule. Until this has been implemented, it may be best to cast a broad net and apply the one-on-one exception conservatively.
3. In some cases, the inclusion of hypothetical performance can transform a one-to-one communication into an advertisement. In addition, a one-to-one communication that includes a paid testimonial or endorsement is an advertisement under the marketing rule. Any marketing communications, particularly emails, should be reviewed to determine if, given the nature of those communications, the inclusion of hypothetical performance or a paid testimonial or endorsement would result in "advertisement" status, and if so, what additional actions must be taken to bring those advertisements into compliance with the new marketing rule.
4. The first prong of the new marketing rule covers "indirect" communications. The SEC will likely attribute to an RIA any communications created, adopted, or disseminated with the RIA's participation, or that are disseminated with the RIA's authorization. If the RIA is working with one or more third parties (such as solicitors and third-party marketers) on a communication, the RIA needs to ensure that the third-party communications comply with the new marketing rule.

RIAs should make sure their social media policies applicable to managers and other personnel provide for prior

approval as warranted, and provide disclaimers for those individuals to use when making communications the SEC would likely deem to be advertisements under the new marketing rule and attributable to the RIA.

1. "Extemporaneous, live, oral communications" are exempted from the first prong, but prepared comments made during a live webcast or presentation would not fall under this exclusion. However, if the live webcast or presentation is recorded, dissemination (e.g., posting or sharing) of the previously recorded version would be an advertisement. Thus, webcast scripts and presentations should be reviewed, and webcast panelists and presenters should be educated about the marketing rule and securities laws generally, especially as to how prepared or off-the-cuff comments could be treated under such laws.
2. RIAs should have in place a policy that requires a review of any and all testimonials or endorsements that are going to be included in any communication.

All RIAs should also keep in mind that, while only "advertisements" from RIAs come under the scope of the new marketing rule, all U.S. investment advisers' communications, including those by unregistered advisers, are (still) subject to the Advisers Act's antifraud provisions.

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