

MEMO# 35366

July 3, 2023

SEC Examinations Division Staff Issues Marketing Rule Risk Alert Regarding Additional Areas of Focus

[35366]

July 03, 2023

TO: Advertising Compliance Advisory Committee

Chief Compliance Officer Committee

Investment Advisers Committee

SEC Rules Committee SUBJECTS: Advertising

Compliance

Disclosure

Investment Advisers

Litigation & Enforcement RE: SEC Examinations Division Staff Issues Marketing Rule Risk Alert Regarding Additional Areas of Focus

As you may recall, in February, when the SEC's Division of Examinations published its 2023 Examination Priorities, listed under "Notable New and Significant Focus Areas" was compliance with rules recently adopted under the Investment Company Act of 1940 and the Investment Advisers Act of 1940. The rules listed in this section included the new marketing rule, Rule 206(4)-1 under the Advisers Act.[\[1\]](#) On June 8, 2023, the Division published a risk alert ("Risk Alert")[\[2\]](#) to notify registrants of the areas the Division will prioritize when conducting examinations for compliance with this new rule.[\[3\]](#) According to the Risk Alert, the areas of emphasis in these examinations will include (1) testimonials and endorsements; (2) third-party ratings; and (3) Form ADV. Further, the Risk Alert reiterated the previously announced areas of review pertaining to Marketing Rule compliance,[\[4\]](#) including a continued focus on the Marketing Rule's general prohibitions. This Risk Alert is described in more detail below.

Summarizing Previously Stated Areas of Review

The Risk Alert first highlighted areas of Marketing Rule compliance that the SEC staff has been reviewing as announced in September of 2022. These areas and the scope of their review include:

- Policies and procedures: whether have advisers adopted and implemented written policies and procedures that are reasonably designed to prevent violations of the

Advisers Act, including the Marketing Rule.

- Substantiation: whether advisers have a reasonable basis for believing they will be able to substantiate material statements of fact in their firm's advertisements.
- Performance advertising: whether advisers comply with performance advertising requirements stipulated by the Marketing Rule.
- Books and records: whether advisers are in compliance with Advisers Act Rule 204-2, as amended, requiring advisers to maintain certain records (e.g., records of all disseminated advertisements, including certain internal working papers, performance related information, and documentation for oral advertisements, testimonials and endorsements).

General Prohibitions

The Risk Alert notes that the staff has, and will continue to, focus on whether advisers have disseminated advertisements that violate any of the Marketing Rule's general prohibitions. These include:

- Untrue facts or material omissions: making 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;
- Substantiation: making 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 SEC;
- Misleading implications: 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;
- Treatment of material risks and limitations: discussing any potential benefits without providing fair and balanced treatment of any associated material risks or limitations;
- Fair and balanced investment advice: referencing specific investment advice provided by the adviser that is not presented in a fair and balanced manner;
- Fair and balanced performance results: including or excluding performance results, or presenting performance time periods, in a manner that is not fair and balanced; and
- Other misleading material: including information in an advertisement that is otherwise materially misleading.

Additional Marketing Rule Areas of Focus

In addition to the above, these examinations will include:

1) Testimonials and Endorsements

The SEC staff stated they will review whether advertisements that use testimonials and endorsements comply with the Marketing Rule requirements, including whether:

- Disclosures provided, include clear and prominent disclosure of whether the "promoter" is a client or investor, is compensated, and if there are material conflicts of interest;
- Oversight conditions are met;
- Written agreements are entered into, where required; and
- If ineligible persons have been compensated for testimonials or endorsements, whether the adviser knew or reasonably should have known the person was ineligible, including certain "bad actors" that are prohibited from acting as promoters, unless such promoters meet the conditions for exemptions.

2) Third-Party Ratings

Additionally, the SEC staff will review whether advertisements that use third-party ratings are compliant with respect to the following requirements:

- Whether the adviser provides, or reasonably believes that the third-party rating provides, clear and prominent disclosure of: (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 the adviser either directly or indirectly provided compensation in connection with obtaining or using the third-party rating; and
- If questionnaires or surveys used in preparation of a third-party rating, that they meet certain conditions, such as that the adviser has a reasonable basis for believing that such questionnaire or survey is designed to make it equally easy for a participant to provide favorable and unfavorable responses and is not intended to produce any predetermined result.

Form ADV

Lastly, the Risk Alert notes that amended Form ADV requires advisers to provide additional information regarding their marketing practices and that the SEC staff will review whether advisers accurately completed these questions in their annual Form ADV amendments.

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Notes

[1] See <https://www.sec.gov/files/2023-exam-priorities.pdf> at p. 9.

[2] See <https://www.sec.gov/files/risk-alert-marketing-rule-announcement-phase-3-060823.pdf>.

[3] During an April meeting with ICI staff, Richard Best, Director of the EXAMS Division, informed ICI staff that he hopes to publish Risk Alerts prior to beginning targeted reviews of compliance with new rules in order to better inform registrants of the areas of focus in these reviews. The current Risk Alert is the first of such Risk Alerts.

[4] See <https://www.sec.gov/files/exams-risk-alert-marketing-rule.pdf>.