Investment Adviser Marketing

A Small Entity Compliance Guide[1]

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Introduction

On December 22, 2020, the Securities and Exchange Commission (the “Commission”) adopted amendments under the Investment Advisers Act of 1940 (the “Advisers Act” or the “Act”) to update rules that govern investment adviser marketing. The amendments create a single rule (the “marketing rule”) that replaces the current advertising and cash solicitation rules, Rule 206(4)-1 and Rule 206(4)-3, respectively. These amendments reflect market developments and regulatory changes since the advertising rule’s adoption in 1961 and the cash solicitation rule’s adoption in 1979. The marketing rule is designed to comprehensively and efficiently regulate advisers’ marketing communications. The Commission also adopted related amendments to Rule 204-2, the books and records rule, and Form ADV, the investment adviser registration form.

Who must follow the marketing rule (Rule 206(4)-1)?

The marketing rule applies to any investment adviser registered or required to be registered with the Commission under section 203 of the Act that directly or indirectly disseminates an advertisement.

What is the definition of advertisement under the marketing rule?

The amended definition of “advertisement” includes two separate parts. The first part generally includes the kinds of communications traditionally covered by the advertising rule and the second generally includes the kinds of activities previously covered by the cash solicitation rule.

- The first part includes any direct or indirect communication an investment adviser makes that: (i) offers the investment adviser’s investment advisory services with regard to securities to prospective clients or private fund investors, or (ii) offers new investment advisory services with regard to securities to current clients or private fund investors.

    - The first part does not include one-on-one communications. However, hypothetical performance information does not qualify for this one-on-one exclusion unless provided in response to an unsolicited investor request or to a private fund investor.
    - The first part also does not include extemporaneous, live, oral communications, and information contained in a statutory or regulatory notice, filing, or other required communication.
- The second part generally includes any endorsement or testimonial for which an adviser provides cash or non-cash compensation directly or indirectly (*e.g.*, directed brokerage, awards or other prizes, and reduced advisory fees).

What types of practices does the marketing rule prohibit in all advertisements?

The marketing rule contains seven general prohibitions on types of activity that could be false or misleading that apply to all advertisements. It also prohibits advertisements that contain testimonials, endorsements, third-party ratings, and performance information, unless certain conditions are met, as described below.

Under the general prohibitions, an advertisement may not:

- include an untrue statement of a material fact, or omit to state a material fact necessary to make the statement made, in light of the circumstances under which it was made, not misleading;
- include 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;
- include 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;
- discuss any potential benefits without providing fair and balanced treatment of any associated material risks or limitations;
- reference specific investment advice provided by the adviser that is not presented in a fair and balanced manner;
- include or exclude performance results, or presenting performance time periods, in a manner that is not fair and balanced; and
- otherwise be materially misleading.

May an adviser use testimonials and endorsements in an advertisement under the marketing rule?

The marketing rule permits the use of testimonials and endorsements in an advertisement, if the adviser satisfies certain disclosure, oversight, and disqualification provisions:

- *Disclosure*. Advertisements must clearly and prominently disclose whether the person giving the testimonial or endorsement (the “promoter”) is a client and whether the promoter is compensated. Additional disclosures are required regarding compensation and conflicts of interest. There are exceptions from the disclosure requirements under certain circumstances for testimonials or endorsements by SEC-registered broker-dealers and certain personnel and affiliates.
- *Oversight and Written Agreement.* An adviser that uses testimonials or endorsements in an advertisement must oversee compliance with the marketing rule. An adviser also must enter into a written agreement with promoters, except where the promoter is an affiliate of the adviser or the promoter receives *de minimis* compensation (*i.e.*, $1,000 or less, or the equivalent value in non-cash compensation, during the preceding twelve months).
- *Disqualification*. The rule prohibits certain “bad actors” from acting as promoters for compensation, subject to exceptions where other disqualification provisions apply.

May an adviser use third-party ratings in an advertisement under the marketing rule?

The marketing rule allows the use of third-party ratings in an advertisement, if the adviser provides disclosures and satisfies certain criteria pertaining to the preparation of the rating.

May an adviser include performance information in an advertisement under the marketing rule?

The marketing rule allows the inclusion of performance information in an advertisement, if certain conditions are met. The marketing rule prohibits including in any advertisement:

- gross performance, unless the advertisement also presents net performance subject to certain conditions;
- any performance results, unless they are provided for specific time periods in most circumstances;
- any statement that the Commission has approved or reviewed any calculation or presentation of performance results;
- performance results from fewer than all portfolios with substantially similar investment policies, objectives, and strategies as those being offered in the advertisement, with limited exceptions;
- performance results of a subset of investments extracted from a portfolio, unless the advertisement provides, or offers to provide promptly, the performance results of the total portfolio;
- hypothetical performance (which does not include performance generated by interactive analysis tools), unless the adviser adopts and implements 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 information underlying the hypothetical performance; and
- predecessor performance, unless there is appropriate similarity with regard to the personnel and accounts at the predecessor adviser and the personnel and accounts at the advertising adviser. In addition, the advertising adviser must include all relevant disclosures clearly and prominently in the advertisement.

What are the recordkeeping requirements associated with the marketing rule?

Amended rule 204-2 includes recordkeeping requirements associated with the marketing rule. Investment advisers must make and keep copies of all advertisements they directly or indirectly disseminate. Certain alternative methods for complying with this requirement are available for oral advertisements, including oral testimonials and oral endorsements. The amended rule also includes specific requirements for making and keeping records related to performance information, testimonials, endorsements, and third-party ratings.

What are the Form ADV reporting requirements associated with the marketing rule?

The Commission amended Form ADV to require advisers to provide additional information regarding their marketing practices.

Is prior staff guidance on adviser advertising practices being withdrawn?

The staff of the Division of Investment Management will withdraw no-action letters and other guidance addressing the application of the advertising and cash solicitation rules as those positions are either incorporated into the marketing rule or will no longer apply. A list of the letters will be available on the Commission's website.

When may an adviser comply with the amended rules and when must it begin to comply?

The marketing rule and amendments to the books and records rule and Form ADV are effective May 4, 2021. The Commission has set a compliance date of November 4, 2022 (eighteen months following the effective date) to give advisers sufficient time to comply with the provisions of the amended rules and Form. Advisers may begin to comply with the marketing rule any time starting on the effective date.

Other resources

The adopting release can be found on the Commission's website at https://www.sec.gov/rules/final/2020/ia-5653.pdf.

The proposing release can be found on the Commission's website at https://www.sec.gov/rules/proposed/2019/ia-5407.pdf.

Staff FAQs on the marketing rule can be found on the Commission's website at https://www.sec.gov/investment/marketing-faq.

Contacting the Commission

The Commission's Division of Investment Management is happy to assist small entities with questions regarding rule 206(4)-1. You may submit a question by email to IMOCC@sec.gov. Additionally, you may contact the Division of Investment Management's Office of Chief Counsel at (202) 551-6825.

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[1] This guide was prepared by the staff of the U.S. Securities and Exchange Commission as a "small entity compliance guide" under Section 212 of the Small Business Regulatory Enforcement Fairness Act of 1996, as amended. The guide summarizes and explains rules and form amendments adopted by the Commission, but is not a substitute for any rule or form itself. Only the rule or form itself can provide complete and definitive information regarding its requirements.

Modified: May 4, 2021