



ACA COMPLIANCE GROUP

Changes to Marketing and Advertising Rules

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SEC Proposes Expansive Changes to Marketing and Advertising Rules

In an effort to ensure that the regulations applying to investment advisers remain relevant in the digital age, the staff of the U.S. Securities and Exchange Commission (“SEC” or “Commission”) announced significant changes to the rules and guidance surrounding the marketing and advertising activities of registered investment advisers and the engagement of solicitors. Discussing the proposed rule changes, Chairman Jay Clayton stated,

“The advertising and solicitation rules provide important protections when advisers seek to attract clients and investors, yet neither rule has changed significantly since its adoption several decades ago.... The reforms we have proposed today are designed to address market developments and to improve the quality of information available to investors, enabling them to make more informed choices.”

Broadly, the proposed amendments to the advertising and solicitation rules appear to be the Commission’s attempt to bring the volumes of disjointed rules, guidance, and no-action letters refining the rules in the decades since their adoption into a coherent set of regulations. In summary, the proposed rules would:

- » replace the current advertising rule with more expansive, principles-based provisions;
- » permit the use of testimonials, endorsements, and third-party ratings subject to certain conditions;
- » provide tailored requirements for the presentation of performance results based on an advertisement’s intended audience;
- » expand the solicitation rule to cover solicitation arrangements involving all forms of compensation subject to a new de minimis threshold;
- » update aspects of the solicitation rule such as who is disqualified from acting as a solicitor; and
- » requiring additional disclosure regarding solicitor conflicts of interest.

MARKETING AND ADVERTISING

The first specific change proposed for the advertising rule is a new definition for “advertisement.” If the definition is adopted, an advertisement will “include any communication, disseminated by any means, by or on behalf of an investment adviser, that offers or promotes investment advisory services or that seeks to obtain or retain advisory clients or investors in any pooled investment vehicle advised by the adviser.”

Also under the proposed change, the following would not be considered advertisements:

- » Live oral communications that are not broadcast;
 - » Responses to certain unsolicited requests for specified information;
 - » An advertisement, other sales material, or sales literature that is about a registered investment company or a business development company and is within the scope of other Commission rules; and
 - » Information required to be contained in a statutory or regulatory notice, filing, or other communication.
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Next, the Commission proposes to redefine the list of prohibited marketing and advertising activities under the advertising rule, which includes codifying guidance previously contained in no-action letters. The revised list reads as follows:

- » Making an untrue statement of a material fact, or omission of a material fact necessary to make the statement made, in light of the circumstances under which it was made, not misleading;
- » Making a material claim or statement that is unsubstantiated;
- » Making an untrue or misleading implication about, or being reasonably likely to cause an untrue or misleading inference to be drawn concerning a material fact relating to the investment adviser;
- » Discussing or implying potential benefits without a clear, prominent discussion of the associated material risks or other limitations;
- » Referring to specific investment advice provided by the adviser that is not presented in a fair and balanced manner;
- » Including or excluding performance results, or presenting performance time periods, in a manner that is not fair and balanced; and
- » Being otherwise materially misleading.

Third, the SEC has proposed a new set of prohibitions regarding the presentation of performance. “Clover”, the “IAA”, “Franklin”, and other oldies but goodies in the no-action letter realm have been reduced to a more easily navigable list of proscribed behaviors as follows:

- » Including gross performance results unless the advertisement provides (or offers to provide promptly) a schedule of fees and expenses deducted to calculate net performance;
- » Any statement that the calculation or presentation of performance results has been approved or reviewed by the Commission;
- » Presenting performance results from some but not all portfolios with investment policies, objectives, and strategies substantially similar to [the portfolios being offered or promoted in the advertisement, with limited exceptions;
- » Presenting performance results for a subset of investments extracted from a portfolio unless the advertisement provides or offers to provide promptly the performance results of all investments in the portfolio; and
- » Presenting hypothetical performance unless the adviser adopts and implements policies and procedures reasonably designed to ensure the performance is relevant to the recipient’s financial situation and investment objectives and provides certain specified information underlying the hypothetical performance.

Notably, much of the proposed changes to performance presentation requirements appear to mirror those of the Global Investment Performance Standards (“GIPS®”) adopted by the CFA Institute and, in fact, GIPS and the 2020 GIPS Standards are referenced extensively throughout the staff’s proposal. In crafting the proposed requirements, the staff specifically notes that they “believe that the proposed rule’s requirements with respect to performance advertising are generally consistent with widely used, internationally recognized standards of performance reporting, such as GIPS” Ostensibly, the staff appears to suggest that performance presentations that are GIPS compliant will also be compliant with the requirements of the new rule, which would represent welcome guidance and clarity by the asset management community.

The SEC also appears to be addressing the long absent division between the treatment of institutional and retail clients under the advertising rules and has proposed to implement a new regulation targeting retail investors that would require the presentation of net performance alongside any presentation of gross performance. The new rule would also require the presentation of the performance results of any portfolio or certain composite aggregations across one, five, and ten-year periods.

Finally, while it is a well-accepted and widely deployed industry best practice, the SEC has decided to require all advertisements to be reviewed for consistency with the requirements and approved in writing by a designated employee before dissemination with two exceptions: communications directed to a single person/household or live oral communications broadcast on radio, television, the internet, or any other similar medium. The staff notes that they “believe it is important that investment advisers have a process in place designed to promote compliance with the proposed rule’s requirements” and that requiring “a written record of the review and approval of the advertisement will allow our examination staff to better review adviser compliance with the rule”.

Advisers should also note that the Division of Investment Management is reviewing all relevant existing no-action guidance that may be affected by the proposed rule changes to determine whether or to what extent the guidance should be withdrawn.

SOLICITATION

In a bow to the changing landscape of client and investor sourcing, the Commission has proposed changes to the rules surrounding the engagement of solicitors, including the removal of the requirement for “cash payments” to trigger the rule. The proposed rule covers solicitation arrangements that involve any form of “compensation,” including non-cash compensation such as directed brokerage, awards or other prizes, and free or discounted services. Of particular note to advisers of private funds, the SEC has proposed expanding the solicitation rule to cover solicitation activities geared toward investors in private funds, which are currently exempt from the rule.

The current exemptions for solicitors that refer investors for impersonal investment advice and for solicitors who are employees of or otherwise affiliated with the adviser would remain, but the Commission has proposed doing away with requiring written agreements for these types of solicitors. In addition, if the proposed changes are adopted, the rule would have new exemptions for de minimis compensation and for advisers that participate in certain nonprofit programs.

In an apparent exchange for loosening the more burdensome areas of the solicitation rule, the SEC also proposed some new restrictions on solicitors. These include an expanded list of disciplinary events that would disqualify persons from acting as solicitors, modifications to the requirement to enter into written agreements with solicitors, and modifications to the current solicitor disclosure to include additional information about conflicts of interest. The requirement for advisers to have a reasonable basis for believing a solicitor has complied with the rule’s written agreement, including complying with the solicitor disclosure requirement, remains unchanged.

In summation, the proposed rules do not appear to alter previous rules or guidance issued by the SEC significantly but rather attempt to address the gray areas, novel issues, gaps, and conundrums that have arisen since the original rules’ enactment.

[View the text of the proposed rules here.](#)

ACA GUIDANCE

ACA suggests that this is a perfect time for advisers to review their advertising and solicitation activities to ensure they follow the current rules, as well as to assess any realignment of practices that might be necessary to comply with the proposed rules.

FOR MORE INFORMATION

For more information about the proposed changes or to learn how ACA can help in reviewing your current advertising and marketing compliance programs, please contact **Michael Pitts** at mpitts@acacompliancegroup.com or **781-375-5770**.