

# Marketing Rule: A glimpse of what to look forward to

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SEC has recently published Marketing Rule 206(4) that applies to [investment advisors](#). Through this article, we bring to light the reforms and modernization of existing guidelines taking into consideration the impacts and changes that technology has on traditional rules.

Here we list out potential effects of this rule and some resulting thoughts around it.

## **Background of the rule:**

The Investment Advisers Act 1940 is a body that regulates companies involved in investing, reinvesting and trading in securities. After a decade of long standing rules the organization has decided to reform and amend the existing rules on December 2020. The Act came into effect on May 4, 2021 by merging the rules that govern investment adviser advertisements and payments to solicitors into one single rule known as the “Marketing rule” to regulate investment advisers marketing communications.

## **Time period to comply:**

The Act was published in the U.S Federal Register on 4th March, 2021 and will be given an 18 month transition period for [compliance](#) which lapses on 4th November, 2022.

## **Changes that led to reformation:**

1. Advancements in [technology](#) and mode of communications
  2. Changes in the expectations of investors seeking advisory services
  3. Diversification of profiles in the investment advisory industry
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**There are broadly three categories that these can be broken down into:**

## **Category 1: Advertisements**

Additions to existing rules:

- Due to rapidly growing technological advancements and increasing dependence on electronic communications there is an inclusion to regulate both direct and indirect forms of communications with existing and new investors along with clients for new products and services  
*For example:* Third-party social media comments that an adviser endorses or promotes, and non-written communications, such as pre-recorded videos
- The rule replaces prohibitions with principle based framework. It relaxes certain prohibitions based on specifications made on past investment recommendations. The act specifies that a company can present specific past investment recommendations in an advertisement excluding a full year of recommendations provided it is portrayed in a fair and balanced manner
- The Rule exempts communications with investors in private funds that rely on Section 3(c) (1) or 3(c) (7) from registering as an investment company under [the Investment Company Act of 1940](#)
- The rule considers direct communications with prospective or current advisory clients to be advertisements only if there is an inclusion of [hypothetical performance](#) and the adviser is not providing the hypothetical performance in response to specific and unsolicited questions or requests from the advisory client

Must haves:

- The statements made in an advertisement should be true and not misleading and should not omit any details that are material and required to be provided
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When questioned or demanded to provide justification for the said statements the advisor should have material evidence and facts to support mentioned statements

- The advisor should communicate the exact details mentioned in the statements and not make verbal additions to it
- Performances mentioned in the statements should be fair and not misleading. There should not be any over or under statements of it

Excludes:

- Spontaneous communications between investors and clients on topics not related to investment products
- Communications with existing clients and investors that do not offer new or additional advisory services to be advertisements

## **Category 2: Testimonies and Endorsements**

Must have:

- An advisor that uses testimonials and endorsements in advertisements should abide and comply with the [marketing rule](#)
- The advisor should mention the identity of the person making a testimonial or an endorsement and whether compensation is provided for it
- Additional disclosures for compensation and conflicts of interest can either be a part of the advertisements or provided separately
- Advisers generally must enter into written agreements with third parties who will be compensated for testimonials and endorsements

Excludes

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- Registered broker-dealers who solicit individuals that are investing for personal, family or household purposes, and certain investment adviser personnel, are generally excluded from the disclosure requirements for testimonials and endorsements
- The Rule prohibits advisers from paying any person for a testimonial or endorsement if that person has been subject to certain disqualifying events (fraud, convicted, etc.) under the Advisers Act and violates securities laws or laws laid down by SEC
- A person can be excluded from entering into a written agreement where the promoter is an affiliate of the adviser or the promoter is paid minimum value compensation (i.e., \$1,000 or less or the equivalent value in non-cash compensation, during the preceding twelve months)

### **Category 3: Third Party Disclosures**

Must have:

- The marketing rule instructs advisors that use third party ratings in advertisements provide appropriate disclosure that the methods of obtaining the foresaid ratings like questionnaires and surveys are fair and not bias
- The amended books and records rule requires an advisor to keep copies of all the advertisements. It also requires advisors to document and keep copies of written communications, calculations of performance results, and material evidence that testimonies, endorsements and third party ratings comply with the marketing rule. The record of such copies should also be disclosed to clients and investors
- Term 5 of Part 1A of Form ADV will require information about an adviser's and its relying advisers' use in any advertisements of (a) performance results, (b) previous investment advice, (c) testimonials, (d) endorsements, and (e) third-party ratings

Excludes

- The rule prohibits the use of third-party ratings in an advertisement, unless the adviser provides disclosures and satisfies certain criteria pertaining to the preparation of the rating.
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**Sources:**

[SEC.gov | SEC Adopts Modernized Marketing Rule for Investment Advisers](#)

[SEC's New Marketing Rule for Investment Advisers Goes into Effect | Publications and Presentations | Arnold & Porter \(arnoldporter.com\)](#)

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