

SEC's New RIA Rules

Moderator:

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Topics

- Marketing Rule
- Technology
- FinTech
- Supervision
- Proposed Rules
- CE Requirements
- Questions

Marketing Rule – Definition

- Any direct or indirect communication to >1 person that offers the RIA's investment advisory services with regard to securities.
- Any direct or indirect communication to one or more persons if the communication includes hypothetical performance that offers the investment adviser's investment advisory services with regard to securities.
- Any endorsement or testimonial for which an investment adviser provides compensation, directly or indirectly.

Marketing Rule – Prescriptive Elements

- General Prohibitions
- Substantiation
- Record Keeping
- Noncash Compensation to Promoters
- Third-party Ratings
- Form ADV Amendments
- Testing Policies and Procedures

Marketing Rule – Recent Guidance re: Examinations

- Policies and Procedures
 - Are they updated, objective and testable?
- Substantiation
 - Has the adviser documented a reasonable basis for belief or has the ability to substantiate?
- Performance Advertising
- Books & Records
 - Does the adviser retain internal working papers, performance related information, and documentation for oral advertisements, testimonials, and endorsements?
 - Does the adviser have the ability to maintain records to accurately complete Form ADV?

Marketing Rule – Rule 206(4)-1(b) Testimonials and Endorsements

- The Cash Solicitation rule was merged into the Marketing Rule with solicitation activities now included in the definition of endorsement.
- Compliance with the new Rule was required by November 4, 2022.

Testimonials and Endorsements (cont.)

- Significant items include:
 - Enhanced client disclosure requirement – must disclose at the time of the dissemination:
 - Whether the testimonial/endorsement was given by a client/investor or not
 - Cash and non-cash compensation
 - Material conflicts
 - Material terms of direct or indirect compensation

Testimonials and Endorsements (cont.)

- Adviser oversight – The adviser must have:
 - a reasonable basis that the testimonial/endorsement complies with the requirements of the Rule
 - a written agreement with the person giving the testimonial/endorsement describing the scope of the activities and the terms of compensation

Testimonials and Endorsements (cont.)

- Exemptions
 - testimonial/endorsement disseminated for no compensation or de minimis compensation (\$1,000 or less during the prior 12 months), no written agreement is required
 - testimonial/endorsement by an adviser's control or affiliated person
 - testimonial/endorsement by a broker or dealer registered with the SEC if:
 - it is a recommendation subject to Reg BI
 - it is provided to a person who is not a retail customer (as defined by Reg BI)

Testimonials and Endorsements (cont.)

- Action Items:
 - Review all referral relationships and document all relationships that require documentation
 - Review and revise, as necessary, all existing solicitor agreements to ensure they comply with Marketing Rule
 - Update compliance procedures and forms used to comply with the Marketing Rule

Guidelines for Performance Advertising

Advertising Traps:

- Third-Party communications
- Gross vs. Net Performance
- Reference to Related Portfolio Performance
- Extracted Performance
- Hypothetical Performance
- Predecessor Track Records

SEC Marketing Rule Sweep Exams

- SEC Sweep Exams: Initial Targeted Areas
 - <https://www.sec.gov/files/exams-risk-alert-marketing-rule.pdf>
- Update policies and procedures designed to prevent violations
 - Contemporaneous Book & Record to demonstrate reasonable belief in accuracy
 - Objective and testable procedures
 - Pre-review and approval, sampling of advertising used, and pre-approving templates
- Substantiation of material statements of fact on demand
- Compliance with performance requirements in the Marketing Rule
- ADV Marketing Rule Updates
- Books and Records – Similar to Broker-Dealer Rules

Technology - Program Necessities

- CRM
 - Electronic Recordkeeping
 - Trade Order Management
 - Portfolio Reporting Software
 - Secure Document Delivery
- Cybersecurity Program
 - Account Takeover
 - Fraudulent Funds Transfer
 - Multifactor Authentication
 - Secure Delivery of Documents Containing PII
 - Password Policy (Reset/Sharing)
 - Training
 - Incidence Response Plan
 - Remote Work
 - Vendor Due Diligence Program

Technology – Dangers/Off-Channel Communications

- **SEC LEVIES \$1.1 BILLION IN FINES FOR FAILURES TO MAINTAIN AND PRESERVE ELECTRONIC COMMUNICATIONS**
- Communicating business matters using text messaging applications on personal devices
- Employees at all levels including senior executives
- Violation of recordkeeping

- Action Items
 - Review and enhance policies and procedures to address the use of personal email, texting and social media relative to business-related matters.
 - Address the use of personal devices at during the annual compliance meeting, include it on a written agenda and required sign in so attendance can be tracked
 - Include an initial, quarterly and annual acknowledgement by each employee
 - Require the installation of the firm approved app on personal devices
 - Prohibit texting of any business related/client related communication other than through firm approved applications.

SEC Enforcement Examination Priorities

- RIAs
 - Marketing Rule, custody, valuation, portfolio management conflicts,
- Broker-Dealers
 - Supervisory programs, electronic communication, AML Customer Protection Rule
- Both
 - Standards of conduct - Reg BI, Fiduciary Duty and form CRS
 - Environmental Social Governance (ESG) investing
 - Information Security and Operational Resiliency
 - Vendor due diligence- books and records
 - Emerging Technology and Crypto Assets.

Proposed Rules

- Safeguarding Advisory Client Assets
- Cybersecurity Risk Management for Investment Advisers, Registered Investment Companies, and Business Development Companies
- Regulation S-P: Privacy of Consumer Financial Information and Safeguarding Customer Information
- Outsourcing by Investment Advisers
- Environmental, Social, and Governance Disclosures for Investment Advisers and Investment Companies
- Private Fund Advisers; Documentation of Registered Investment Adviser Compliance Reviews

CE for IARs



NASAA (as of 4/25/2023)

Key Takeaways

- RIA rules and regulations are becoming increasingly similar to brokerage rules
 - More prescriptive with supervision, testing, and recordkeeping requirements
 - Expect more examinations
- Pace of change is very fast
 - Need to keep up with the right tools and updated procedures

Resources

- Marketing
 - Marketing Rule Adopting Release, No. IA-5653 (December 22, 2020).
 - Withdrawal and Modification of 203 No-Action Letters, (October 2021).
 - IM Information Update, 2021-10 (October 2021).
 - Examinations Focused on the New Investment Adviser Marketing Rule (Sep. 19, 2022)
 - Observations from Examinations of Newly-Registered Advisers, (Mar. 27, 2023).
- MNPI Controls
 - April 2022 Risk Alert: Investment Adviser MNPI Compliance Issues – focus is on alternative data sources and expert networks
 - In re Mio Partners (Nov. 19, 2021). (RIA that was affiliated with a consulting firm had inadequate policies and procedures to prevent the consultants from misusing material nonpublic information they obtained as consultants to public companies while they were simultaneously overseeing the RIA's investment decisions).
- Conflicts of Interests
 - August 2022 Staff Bulletin: Standards of Conduct for Broker-Dealers and Investment Advisers Conflicts of Interest
 - October 2019 Frequently Asked Questions Regarding Disclosure of Certain Financial Conflicts Related to Investment Adviser Compensation

Resources (cont.)

- Ongoing Challenges for RIAs
 - SEC v. Commonwealth Equity Services, LLC (Apr. 7, 2023). (Federal court order dismissing summary judgment on failure of SEC to provide notice of disclosure requirements.)
 - Article on Rep as PM account challenges
- CE for IARs
 - Other NASAA's Investment Adviser Representative Continuing Education Website
- Other
 - Observations from Examinations of Newly-Registered Advisers (Mar. 27, 2023)
 - Observations From Broker-Dealer and Investment Adviser Compliance Examinations Related to Prevention of Identity Theft Under Regulation S-ID (Dec. 5, 2022)
 - 2023 SEC Examination Priorities (Jan. 2023)
 - Article on SEC Staff expectations of RIA compliance programs
 - Article on considerations for account type recommendations

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CLE CODE WORD: SOLICITATION