



May 29, 2014

## **CLIENT ALERT**

### **SEC GUIDANCE ON INVESTMENT ADVISER USE OF SOCIAL MEDIA AND ADVERTISING**

The SEC Division of Investment Management issued IM Guidance Update No. 2014-14 (the “Guidance Update”) on March 28, 2014<sup>1</sup> to clarify how an investment adviser may use public commentary about the adviser that appears on independent third-party social media websites, without violating the general prohibition against using testimonials in advertising. To avail itself of the ability to use public commentary appearing on independent social media websites in its own advertising, an adviser must meet the conditions set forth in the Guidance Update.

#### **Background**

Section 206(4) of the Investment Advisers Act of 1940, as amended (the “Advisers Act”) generally prohibits an adviser from engaging in any act, practice or course of business that the SEC defines as fraudulent, deceptive or manipulative. Rule 206(4)-1(a)(1) of the Advisers Act (the “Testimonial Rule”) prohibits investment advisers from using testimonials in their advertisements. The SEC considers testimonials used in advertising to be inherently misleading because of the tendency of investment advisers to include only positive testimonials (and ignore the negative ones). The SEC has stated that the Testimonial Rule forbids the use of a testimonial

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<sup>1</sup> A copy of the Guidance Update is available at [www.sec.gov/investment/im-guidance-2014-04.pdf](http://www.sec.gov/investment/im-guidance-2014-04.pdf).

by an investment adviser in advertisements because the testimonial may give rise to the fraudulent or deceptive implication that the experience of the person giving the testimony is typical of the adviser's clients. The term "testimonial" is not defined in the Rule but, historically, the SEC has interpreted the term "testimonial" to include a "statement of a client's experience with or endorsement of an investment adviser." Whether a statement is a testimonial is dependent on the facts and circumstances relating to the statement. By way of example, if an investment adviser were to publish on its own social media website, public commentary that is an explicit or implicit statement of a client's experience with or endorsement of the adviser, it would violate the Testimonial Rule. On the other hand, advertisements that contains non-investment related commentary regarding the adviser, such as the religious affiliation or community service of one of its principals does not violate the Testimonial Rule.<sup>2</sup>

## The Guidance Update

The Guidance Update provides that (a) when an investment adviser has no ability to affect which public commentary is included or how the public commentary is presented on an independent social media website (such as *Angie's List* or *Yelp*); (b) where the commentators' ability to include the public commentary is not restricted; and (c) where the independent social media website allows for the viewing of all public commentary and updating of new commentary on a real-time basis, the concerns underlying the Testimonial Rule may not be implicated. The Guidance Update clarifies that under certain circumstances, an adviser's publication of all of the testimonials about the adviser from an independent social media website on the adviser's own social media website, would not implicate the concerns underlying the Testimonial Rule.<sup>3</sup>

The Guidance Update sets forth the following conditions that must be met for an adviser to be able to publish public commentary from an independent social media website on its own social media website and not violate the Testimonial Rule:

- the independent social media website provides content that is independent of the adviser;
- there is no material connection between the independent social media website and the adviser that would call into question the independence of the site or the commentary; and
- the adviser publishes all of the unedited comments that appear on the independent social media website regarding the adviser.

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<sup>2</sup> The SEC continues to recognize the need to adopt and clarify its rules in light of the changing face of technology as it applies to the use of social media. See our previous Client Alert, *Using Social Media to Disclose Information*, dated April 12, 2013, available [here](#).

<sup>3</sup> The Guidance Update relates only to the publication of commentary on independent social media websites and the reference to such information; it does not relate to advertisements on non-social media (newspaper, radio, television). Social media allows for instantaneous updating of posted commentary and concurrent viewing of all the comment history; in contrast, newspaper, radio and television are static media that reflect public commentary at a particular point in time and are limited media that typically would not reproduce all of the available public commentary simultaneously.

## Independence

Commentary would not be independent of the adviser if the adviser directly or indirectly authored the commentary on the independent social media website, regardless of whether it did so in its own name or another's. Also, if the adviser is allowed to suppress the publication of all or part of the commentary, edit the commentary, organize or prioritize the order of the commentary that is included on the independent social media website, the Testimonial Rule generally would be implicated.

## No Material Connection

No material connection between the independent social media website and the adviser can exist that would call into question the independence of the site or commentary. For example, the adviser may not (a) compensate a social media user for authorizing a commentary; or (b) prioritize, remove or edit the commentary. Also, an adviser could not have a supervisory person, client or prospective client submit a testimonial about the adviser and then use such testimonial in its own advertising without implicating the Testimonial Rule.

## All Unedited Comments Included

The adviser could not prioritize or edit a commentary appearing on an independent social media website before publishing it on its own website. An adviser may not publish a testimonial from an independent social media website that, directly or indirectly, emphasizes commentary favorable to the adviser or de-emphasizes commentary unfavorable to the adviser. The adviser may publish only the totality of the testimonials from an independent social media website and may not highlight or give prominence to a subset of the testimonials. The adviser may publish the testimonials in a content-neutral manner (for example, chronologically or alphabetically), which presents positive and negative commentary with equal prominence. It should be noted that social media users are free to display the commentary and sort by any criteria, including by the lowest or highest rating. Advisers may facilitate on their own websites a user's viewing of the commentary by providing a sorting mechanism as long as the adviser does not itself sort the commentary. For an adviser to publish commentary from an independent social media website on its own website, it must also publish real-time updates on its own website as new comments are posted on the independent social media website.

Despite the foregoing, an adviser may not publish on its own social media website, public commentary that is an explicit or implicit statement of a client's experience with, or endorsement of the adviser. The SEC believes such public commentary would be a testimonial within the prohibition of the Testimonial Rule, and its use in an advertisement by an adviser would be prohibited.

## Additional Dos and Don'ts

- **Mathematical Averages** – An adviser may publish testimonials from an independent social media website that includes a mathematical average of the commentary, provided the commenters themselves rate the advisers based on a rating system that is not designed

to elicit any pre-determined results that could benefit the adviser. Neither the independent social media website nor the adviser may provide a subjective analysis of the commentary.

- **Adviser’s Advertisements** – An adviser that advertises on an independent social media website that also features independent public commentary, and then publishes the independent public commentary on its own website does not violate the Testimonial Rule, provided: (a) it was “readily apparent” to a reader that the adviser’s advertisement is separate from the public commentary on the independent social media website; and (b) the receipt or non-receipt of advertising revenue did not influence which public commentary is included or excluded from the independent social media website.
- **Non-Social Media Advertisements** – An adviser could reference in non-social media advertisements (for example, newspaper, radio, television) the fact that public commentary regarding the adviser may be found on an independent social media website (for example, by taking out a newspaper advertisement that says, “see us on *Facebook*”) without implicating the Testimonial Rule. Conversely, an adviser could not publish a testimonial from the independent social media website on its own non-social media (such as a newspaper advertisement) without implicating the Testimonial Rule.
- **Client Lists** – An advertisement on an adviser’s website that can be viewed by the general public which contains a list of “friends” or “contacts” would not violate the Testimonial Rule, provided the friends or contacts are not grouped so as to be identified as current or past clients. A partial client list that does no more than identify certain clients of the adviser cannot be viewed either as a statement of a client’s experience with, or endorsement of the adviser, and therefore, is not a testimonial. However, if an adviser attempts to create the inference that the friends or contacts experienced favorable results from the adviser, the advertisement could be in violation of the Testimonial Rule.
- **Fan/Community Pages** – A third party’s creation and operation of unconnected community or fan pages generally would not implicate the Testimonial Rule. However, the Guidance Update “strongly cautions” advisers when publishing content from or driving users traffic to such websites, particularly if the website does not meet the “no material connections” and “independence” conditions described above.
- **Anti-Fraud** – Even if an advertisement uses independent social media commentary that does not implicate the Testimonial Rule, it still must comply with the anti-fraud provisions of the Advisers Act.

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Please contact Meryl Wiener, 212-984-7731, [mwiener@wbcsk.com](mailto:mwiener@wbcsk.com) or your regular Warshaw Burstein attorney, for assistance in preparing appropriate policies and procedures tailored to your specific social media needs.

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