

# bullet point

**a note from Tannenbaum Helpern Syracuse & Hirschtritt LLP**

**SEC Permits Registered Investment Advisers to Provide Past Specific Recommendations in Response to Unsolicited Requests for Information<sup>1</sup>**

**To: Clients of Tannenbaum Helpern Syracuse Hirschtritt LLP**

**Date: March 3, 2004**

---

On March 1, 2004, the Division of Investment Management of the Securities and Exchange Commission (the "SEC") clarified its view on the application of Rule 206(4)-1 of the Investment Advisers Act of 1940, as amended (the "Advisers Act") in a letter to the Investment Counsel Association of America, Inc.<sup>2</sup> The SEC staff stated that the act of providing past specific recommendations by a registered investment adviser in response to an unsolicited request of a client, prospective client or consultant is not an advertisement within the meaning of Rule 206(4)-1(b) of the Advisers Act. Moreover, the SEC staff stated that a registered investment adviser responding to an unsolicited request by a client, prospective client or consultant for specific information about the adviser's past specific recommendation would not be prohibited to do so by Rule 206(4)-1(a)(2) of the Advisers Act *provided* that the adviser did not directly or indirectly solicit the client, prospective client or consultant to make the request. Furthermore, the SEC stated that a written communication by a registered investment adviser to its existing clients generally would not be an advertisement within the meaning of Rule 206(4)-1(b) of the Advisers Act merely because it discusses the adviser's past specific recommendations concerning securities that are or were recently held by each of those clients *provided* that such communications are not designed to offer advisory services. The ICAAI Letter is a significant clarification of the advertising rules under the Advisers Act that recognizes the flow of information in the market and the services an adviser provides to its clients in the normal course of business.

## **Providing Past Specific Recommendations to Clients, Prospective Clients and Consultants**

Registered investment advisers are subject to a number of restrictions with respect to advertisement.<sup>3</sup> Under Rule 206(4)-1(a)(2) of the Advisers Act, it is fraudulent if an adviser publishes, circulates, or distributes any advertisement that refers directly or indirectly to the adviser's past specific recommendations that were or would have been profitable to any person. This general prohibition on advertisements that contain past specific recommendation stems from

---

<sup>1</sup> This memorandum provides general information on the subject matter described, and it should not be relied on for legal advice on any matter, which may turn on specific facts. You should seek specific legal advice before acting with regard to the subjects treated here.

<sup>2</sup> Division of Investment Management of the Securities and Exchange Commission, Letter to Investment Counsel Association of Americas, Inc., dated March 1, 2004 ("ICAAI Letter").

<sup>3</sup> Rule 206(4)-1(b) of the Advisers Act defines "advertisement" to include: any notice, circular, letter or other written communication addressed to more than one person, or any notice or other announcement in any publication or by radio or television, which offers (1) any analysis, report, or publication concerning securities, or (2) any graph, chart formula or other devise to be used in making any determination as to when to buy or sell any security, or which security to buy or sell, or (3) any other investment advisory service with regard to securities.

the SEC's concern that an adviser could "cherry-pick" its profitable recommendations and omit unprofitable recommendations. Nevertheless, an adviser could advertise its past specific recommendations *provided* that certain conditions are satisfied as described under Rule 206(4)-1(a)(2)(A) and (B) of the Advisers Act.<sup>4</sup> Among the key conditions is that an adviser must furnish a list of *all* recommendations made by such adviser during the pertinent time period.

Quite often, current clients, prospective clients and consultants contact a registered investment adviser to request information about the adviser. Such requests should be expected as part of the due diligence process prospective clients and consultants conduct and as a form of monitoring by current clients. Until the ICCAI Letter, advisers have been constrained in their ability to furnish information about their past specific recommendations because of the danger of violating the advertising rules and in particular Rule 206(4)-1(a)(2) of the Advisers Act. According to the SEC staff in the ICCAI Letter, an adviser that does no more than respond via a written communication to an *unsolicited* request by a client, prospective client or consultant for specific information about the adviser's past specific recommendations is not an "advertisement." As such, an adviser can provide past specific recommendations in response to unsolicited requests by prospective clients, current clients or consultants without having to comply with the onerous conditions set forth under Rule 206(4)-1(a)(2)(A) and (B) of the Advisers Act because such acts do not constitute advertisement.<sup>5</sup> As a consequence, information about an adviser's past specific recommendations can now be more freely disseminated. For example, according to the SEC staff, it would be permissible for an adviser to provide information about its past specific recommendations to a consultant requesting information on behalf of several of its own clients.

Note that a critical requirement is that the request must be "unsolicited." According to the SEC staff, a solicited request would be the result of "any affirmative effort by an investment adviser that is intended or designed to induce a client, prospective client or consultant to request the adviser to provide past specific recommendations or an advertisement indicating that the adviser is willing to provide past specific recommendations upon request."<sup>6</sup>

### **Written Communications to Current Clients that Contain Past Specific Recommendations**

In practice, registered investment advisers periodically distribute written communications to their existing clients about the performance of their accounts, and the SEC staff recognizes that this is a normal part of the adviser's advisory services. Accordingly, in the ICAAI Letter, the SEC staff is giving comfort to advisers that sending written communications to their existing clients would not be considered to be advertisement within the meaning of Rule 206(4)-1(b) merely because the written communication discusses the adviser's past specific recommendations concerning securities that were or are recently held by the client. The SEC staff cautions that if past specific

---

<sup>4</sup> Rule 206(4)-1(a)(2)(A) and (B) of the Advisers Act provides that the prohibition against including past specific recommendations that were or would have been profitable does not apply if the advisement includes or offers to furnish a list of all recommendations made by the adviser and includes the following information: (1) the name of each security recommended; (2) the date and nature of each recommendation (e.g. whether to buy, sell or hold); (3) the market price at the time of the recommendation; (4) the price of the security when the recommendation was to be acted upon; (5) the market price of each such security at the most recent practicable date; and (6) a disclaimer regarding the profitability of recommendations in the future.

<sup>5</sup> Although an adviser may now respond to unsolicited requests regarding past specific recommendations without complying with Rule 206(4)-1(a)(2)(A) and (B) of the Advisers Act, an adviser's written communications must still comply with the general anti-fraud provisions under Sections 206(1) and (2) of the Advisers Act.

<sup>6</sup> ICAAI Letter, note 1.

recommendations are presented in a manner that suggests an offer of advisory services, then such communications would be considered to be advertisement.<sup>7</sup> As such, advisers must remain conscientious of the restrictions on advertising when drafting reports and statements to existing clients so as not to violate the applicable provisions under the Advisers Act.<sup>8</sup>

## Recap

To recap, a registered investment adviser can now provide written materials about its past specific recommendations in response to inquiries from current clients, prospective clients, and consultants provided that certain conditions are met:

- The request is from a current client, a prospective client or a consultant;
- The request for past specific information is unsolicited;
- The response does no more than provide past specific recommendations of the adviser; and
- The response is not designed to offer advisory services.

Furthermore, written communications by a registered investment adviser to its existing clients that discuss the adviser's past specific recommendations would not be considered to be advertisement provided that certain conditions are met:

- The written communications is directed towards current clients;
- The past specific recommendations concern securities that are or were recently held by each of those clients; and
- The written communications are not designed to offer advisory services.

While a registered investment adviser can take comfort in the issue of past specific recommendations, in general an adviser's written communications that are advertisement in nature should be drafted carefully and reviewed by counsel to ensure that such written communications are within the proscriptions of the advertisement rules. Also, registered investment advisers that operate hedge funds should note that the ICAAI Letter does not relax any of the restrictions on general advertisement and general solicitation applicable to hedge funds.

Overall, the SEC staff's response in the ICAAI Letter is a significant step in the promotion of greater transparency in the market.

\* \* \* \* \*

---

<sup>7</sup> For example, a letter written by an adviser that discussed its past specific performance recommendations concerning securities not held or not recently held by some of the clients to whom the letter was directed would suggest that a purpose of the communication was to promote the advisory services of the adviser and thus may constitute an advertisement and be prohibited by Rule 206(4)-1(a)(2) of the Advisers Act. See ICAAI Letter.

<sup>8</sup> See Rule 206(4)-1(a) and Sections 206(1) and (2) of the Advisers Act.

If you have any questions or comments regarding the ICAAI Letter or compliance with the advertising rules under the Advisers Act, please feel free to contact:

Michael G. Tannenbaum  
(212) 508-6701  
[tannenbaum@tanhelp.com](mailto:tannenbaum@tanhelp.com)

Ricardo W. Davidovich  
(212) 508-6710  
[davidovich@tanhelp.com](mailto:davidovich@tanhelp.com)

Roderick J. Cruz  
(212) 702-3149  
[cruz@tanhelp.com](mailto:cruz@tanhelp.com)

Tannenbaum Helpern Syracuse & Hirschrift LLP  
New York London  
[www.tanhelp.com](http://www.tanhelp.com)