PLEASE JOIN ON NOVEMBER 15 – SEC VIRTUAL OUTREACH

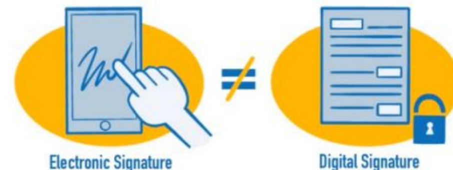
The U.S. Securities and Exchange Commission is announcing that its Compliance Outreach Program's National Seminar for investment companies and investment advisers will be held virtually on November 15, 2022, starting at 8:30 am (Eastern Time). The SEC's Division of Examinations (EXAMS), Division of Investment Management (IM), and the Asset Management Unit (AMU) of the Division of Enforcement jointly sponsor the Compliance Outreach Program. This program is intended to help Chief Compliance Officers (CCOs) and other senior personnel at investment companies and investment advisory firms enhance their compliance programs for the protection of investors.

The November program will be offered as a live webcast—both speakers and attendees will be participating in the program remotely. Registration is not required to attend the live webcast. Investment advisers and investment company senior officers may access the program via https://www.sec.gov page on the day of the event. Panels include:

- **Panel I:** Fiduciary Interp. and Form CRS
- **Panel II:** New Marketing Rule
- **Panel III:** Registered Funds Topics
- **Panel IV:** Environmental, Social and Governance-Related Topics
- **Panel V:** Private Fund Adviser Topics
- **Panel VI:** Hot Topics Lightning Round

A recording will be made available on the SEC's website after the event. For more information or general questions, contact: ComplianceOutreach@sec.gov

ELECTRONIC VS. DIGITAL SIGNATURES



In November 2020, the SEC announced the adoption of final rules amending Rule 302 of Regulation S-T to permit the use of electronic signatures. The amendment allowed flexibility in complying with the documentation requirements by providing individuals the option of signing manually or electronically. Prior to the change, Rule 302(b) required signatories of electronic filings to manually sign signature authentication documents (designed to authenticate the typed signatures in their filings) with a physical signature. The rule also required companies to retain physical copies of the signature authentication documents for five years. This placed companies in the awkward position of having to use a wet ink signature to authorize the use of electronic signatures in the same filing. The inefficiency of this process has been keenly felt during the pandemic, as registrants need to obtain signatures from their board of directors and executive officers, across a remote and distributed work environment. As amended, Rule 302(b) will permit the use of electronic signatures in these signature authentication documents.

Digital signature tools have become a go-to resource for many firms in today's largely remote work era, but this practice also brings an increased the risk of forgery or falsification. Regulators are taking a close look at a firm's policies and procedures and what is established to prevent any risk of forgery or falsification. The most popular scenarios involving this type of forgery or falsification include:

- ✓ account opening documents and updates,
- ✓ account activity letters,
- ✓ discretionary trading authorizations,
- ✓ wire instructions and
- ✓ internal firm docs related to the review of client.

The SEC updated its EDGAR Filer Manual to state that for a signatory to use an electronic signature in ***a signature authentication document***, the signing process for the electronic signature must:

- require the signatory to present a *physical, logical, or digital credential that authenticates the signatory's identity;*
- reasonably provide for non-repudiation of the signature;
- provide that the signature be attached, affixed, or otherwise logically associated with the signature page or document being signed; and
- include a timestamp to record the date and time of the signature.

The process relies on authentication through a "credential." Although the rule itself does not provide further guidance on this point, the EDGAR Manual defines a credential as "an object or data structure exclusively possessed and controlled by an individual to assert identity and provide for authentication." In other words, a credential is a way ***to prove the authenticity of the signature***. This is a broad definition and there will likely be differing views on how to fulfill this proof of authenticity requirement. Some commentators have taken the view that a simple email address can meet this need. Companies that wish to utilize this method can enable this with simple electronic signatures such as those provided with DocuSign eSignature.

However, some firms might argue that the individual will need to use a credential that is more closely linked to his or her identity such as confirmation of client identification document(s). For those who want to go beyond standard email-based identification, DocuSign or other similar firms can offer ID Verification. ID Verification allows companies to require that a signer verify their identity via a recognized form of identification before accessing the agreement. This ensures compliance for those who take a more conservative view of the new rule.

DIGITAL SIGNATURES:

- Used to secure a document
- A digital signature is authorized and regulated by certificate authorities
- Comprised of more security features
- Common types of digital signatures are based on Adobe and Microsoft
- A digital signature can be verified
- Preferred more than electronic signature die to high levels of authenticity
- Concerned about securing the document

ELECTRONIC SIGNATURES:

- Mainly used to verify a document
- Usually not authorized
- Comprised of less security features
- Main types of electric signatures include verbal electronic ticks or scanned signatures
- An electronic signature cannot be verified
- Easy to use but less authentic
- Shows intent to sign a contract

Simple email reviews are also a great way to identify situations where employees had forged or falsified signatures. For example, firms have identified instances where correspondence showed that documents were sent to non-customer emails, including the employees personal email address or that of their assistant, to a employees' firm-assigned email address, or an address associated with an employees approved outside business activity. Therefore, firms were able to identify instances where a client's email address changed in ways that were indicative of attempts to conceal information from a client.

Finally, it may be helpful to use an authentication process when obtaining digital signatures that asks customers to answer one or more questions with personal information to verify their signature. In some instances, representatives have been able to circumvent the authentication process because the verification questions were based on personal information contained in customer files accessible to the representative. Since representatives often have access to customer information, relying solely on this verification process may miss red flags of potential forgery or falsification. Additionally, your firm should ensure their procedures address safeguards around the authentication process and clearly indicate any restrictions on employee access to, for example, client passwords and answers to verification questions.

ATTENTION - FOR FIRMS INVOLVED IN SOLICITORS AND WRAP FEE PROGRAMS:

✓ **SEC WARNING EMAIL SENT SEPTEMBER 7, 2022 -** Solicitor to Promoter Updates

The SEC sent a 'reminder' to firms who have references to Solicitor relationships. This tells us there will be a focus on firms who have current solicitors be on alert to be examined to ensure compliance with the new marketing Rule.

> **SUBJECT LINE: Reminder – Rule 206(4)-3 (Cash Payments for Client Solicitations) to be Rescinded**
> Form ADV Part 2 brochure(s) filed for your investment advisory firm appear to include references to Rule 206(4)-3 (Cash Payments for Client Solicitations). This rule will be rescinded as of November 4th, 2022, and replaced with amended Advisers Act Rule 206(4)-1 (Marketing Rule). Advisers should review the accuracy their Form ADV Part 2A brochures' disclosures, including Item 14 (client referrals and other compensation), with respect to the Marketing Rule.
> **References:**
> - Adopting Rule Release No. IA-5653 - https://www.sec.gov/rules/final/2020/ia-5653.pdf
> - Marketing Compliance Frequently Asked Questions - https://www.sec.gov/investment/marketing-faq
> - Rule 206(4)-1 - https://www.ecfr.gov/current/title-17/chapter-II/part-275 - 275.206(4)-1
>
> If you have interpretive questions, please contact the Division of Investment Management's Investment Adviser Regulation Office at (202) 551-6787 or IM-Rules@sec.gov.

CCO ACTION ITEMS

- ☐ **Review the "Promoter' for any disqualifying events (refer to June 2022 TMIC)**
- ☐ **Execute a "Promoter Agreements" by all your existing relationships.**
- ☐ **Review the requirements for disclosure on advertising materials**
- ☐ **Amend the P&P, ADV Part 1 and Part 2A Brochure documents**
- ☐ **Does your Firm use Lead Generation Firms?**
  Work with CRP on updating ADV Part 2A and Part 1 to reflect disclosure of the relationship.

✓ **WRAP FEE – RECENT ENFORCEMENT ACTIVITY**

Set it and forget it isn't a good approach for investment advisory firms that are putting clients into wrap programs, and another SEC enforcement action is making that point. A Firm agreed to settle charges by the SEC on a failure to monitor wrap accounts from 2015 through August 2018 to determine whether they were suitable for the clients using them. *In a wrap program, a client pays a single fee for advisory and brokerage services. They are meant to be a cost-effective account for investors who don't frequently make transactions.* Clients in the Kovack wrap program paid an all-inclusive fee for asset management, trade execution and other costs, according to the settlement. The SEC has long focused on the use of wrap accounts and issued a risk alert about them last year. In the settlement with Kovack Advisors Inc., the agency explained why such accounts aren't always in a client's best interests.

> ***"Advisory clients with infrequent trading activity, for example, may pay higher fees on a wrap account than they would if they maintained their assets in a non-wrap account or brokerage account where the client would otherwise pay trading costs as incurred, but a lower advisory fee in a non-wrap account, or no advisory fee in a brokerage account," the settlement states.***

During the time period covered by the enforcement action, the Firm didn't monitor the accounts for inactivity to determine whether the wrap accounts were in clients' best interests, the SEC said in the settlement. Kovack agreed to pay $899,513 to settle the SEC charges. ($700,000 civil penalty; $163,239 in disgorgement; and $33,274 in prejudgment interest) Kovack stopped offering wrap accounts to clients in August 2018, according to the settlement. From that point, some Kovack advisers had agreements with their clients to cover some transaction costs.